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**Sent via email**

1 September 2017

Dear Sirs

**Questionnaire on the New Board Concept Paper (June 2017)**

The Alternative Investment Management Association (**AIMA**)<sup>1</sup> writes further to the New Board Concept Paper (the "**Concept Paper**") dated June 2017 issued by The Stock Exchange of Hong Kong Limited (the "**SEHK**") and inviting written comments on the matters discussed in the Concept Paper.

We are grateful to the SEHK for the opportunity to provide written commentary on the matters presented in the Concept Paper. The purpose of this letter is to outline in general terms our members' views regarding the proposals as opposed to providing a detailed response to all of the questions set out in Part B of the Questionnaire on the New Board Proposal ("**Questionnaire**") attached to the Concept Paper.

**Overview**

AIMA is desirous of supporting all SEHK initiatives which seek to promote the ongoing development and success of the capital market ecosystem in Hong Kong, and ensure that the SEHK both remains an attractive market to new and existing market entrants at a global level and is optimally placed to compete with other international exchanges, whether established or developing.

That said, we believe that the creation of the New Boards as envisaged in the Concept Paper (in particular the New Board PRO), is neither necessary nor appropriate at this juncture. We consider that the establishment of

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<sup>1</sup> AIMA is the global representative of the alternative investment industry, with more than 1,800 corporate members in over 50 countries. AIMA's fund manager members collectively manage more than US\$1.8 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. References to AIMA in this letter incorporate the ACC. The ACC is the sole global trade association representing the interests of the private credit and non-bank finance participants in asset management. The ACC currently represents over 80 members that manage US\$300 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. For further information, please visit AIMA's website [www.aima.org](http://www.aima.org).

such further boards has the real potential to result in a dilution of the existing Main Board simply as a platform for dual share class structures.

Moreover, we believe that it is inappropriate at this time to create segments (such as a "PREMIUM" or a "PRO" segment) within the existing Main Board structure. The establishment of such "sub-boards" (primarily the New Board PREMIUM) accommodating only large global tech stocks, may even serve to detract from the primacy of the Main Board

Instead, AIMA believes that SEHK's efforts should rather be focussed on addressing existing structural deficiencies within the current Main Board and considering areas for the improvement and development of the Main Board, in order to continue to improve the overall integrity of the Hong Kong market. Where structural changes are deemed by SEHK to be necessary or desirable, AIMA's preference would be for these changes to be addressed by way of amendments to the existing Main Board itself, in order to create a single, inclusive and all-encompassing board which is able to accommodate the requirements of a variety of different types of issuers.

AIMA considers that the following points undermine the proposals in the Concept Paper and should be taken into account when implementing the next stage of the development of the SEHK:

### **Concept of "New Economy" Industry**

AIMA members believe that clarification is required regarding the criteria for determining what a "new economy" industry is and that this term will need to be clearly defined.

If SEHK is seeking to attract "new economy" companies to list on a new board separate from the current Main Board or GEM Board, it must be clear what the criteria for qualifying for listing on the New Board as a "new economy" company is. In part, this is to avoid any dilution of the existing Main Board and the GEM Board, as highlighted above.

The listing rules of any such additional board should be drafted in a manner so as to make it clear that the primary space for new listings remains the Main Board (or the GEM Board) and that a listing on the New Board PRO or the New Board PREMIUM should only be sought by companies which clearly meet the criteria set out for such "new economy" companies.

### **"Pre-Profit" Companies**

AIMA is broadly in favour of a relaxation of the existing Main Board rules which impose a profits test on new entrants to the market. AIMA appreciates that: (i) certain companies follow less traditional routes to listing; and (ii) increasingly, fast growth companies with non-traditional financial models (often within the tech sector) may seek a listing earlier on in their life cycle.

Rather than preventing such applicants from listing due to an inability to satisfy traditional profitability / cashflow requirements at the time of wishing to list, AIMA is supportive of SEHK permitting such companies to list via SEHK, subject of course to ensuring that there is adequate financial disclosure to SEHK investors, both at the time of listing, and on an ongoing basis.

Such an amendment would be demonstrative of the continued evolution of Main Board listing requirements in order to meet the changing circumstances of new market entrants in the 21<sup>st</sup> century.

### **Secondary Listing of Mainland Companies already Listed Elsewhere**

AIMA is broadly in favour of allowing Mainland companies with a primary listing on another international financial exchange to obtain a secondary listing in Hong Kong.

SEHK should seek to relax the existing restrictions on such applicants, in order to best position itself as the primary market in Asia on which such Mainland companies choose to list.

Importantly, in order to achieve a level of balance between promoters and investors, such a relaxation should be offset by a requirement on such companies to ensure that they have adopted comprehensive and well drafted corporate governance policies and procedures.

## **Considerations on Hong Kong's Overall Listing Framework**

AIMA is in favour of the various changes proposed in the Concept Paper to the GEM Listing Rules which seek to ensure that the GEM Listing Rules address regulatory and market concerns on GEM listing candidates and listed issuers. These changes would include (but are not limited to) lengthening the lock-up on controlling shareholders upon listing (from one year to two years) and increasing the minimum market capitalisation for new entrants from HK\$200 million to HK\$500 million.

## **Corporate Governance Concerns Regarding Weighted Voting Right "WVR" Structures**

Notwithstanding the desire of SEHK to broaden the range of entrants capable of listing on the Hong Kong market and the need to ensure that the Hong Kong market remains competitive internationally and attractive for new entrants (in particular technology companies) seeking a listing, AIMA members have a number of serious concerns from a corporate governance perspective regarding the WVR proposals.

AIMA members have concerns regarding the proposed voting rights attached to the founders' shares which may lead to the oppression of minority shareholders. Minority shareholders are likely to have little or no say in the appointment and removal of directors and the board may be conflicted when it comes to its representation of minority shareholders.

This effective disenfranchisement of minority shareholders runs counter to the principles as set forth in the Hong Kong Securities and Futures Commission's "Principles of Responsible Ownership", which emphasized that "Ownership of shares brings with it important responsibilities, particularly the right to speak and vote on matters that can influence the way in which a business is conducted."<sup>2</sup>

This disenfranchisement is particularly relevant in the context of Hong Kong shareholders who do not have access to redress by way of class action suits against a company. The option exists in the US as a counterbalance to the inequities that are created through the use of WVR structures and is often pursued on the basis of contingency fee arrangements.

In the event that SEHK permits companies with a WVR structure to list in Hong Kong, AIMA members would strongly advocate a range of safeguards in order to deliver a level of protection for the interests of minority shareholders. Such safeguards might include the following:

- (1) the introduction of an effective "class action" rights concept in Hong Kong, as a mechanism for enforcing claims. Class action rights in Hong Kong (in addition to the existing statutory and common law protections in Hong Kong afforded to minority shareholders) would ensure that management of companies are likely to be more scrupulous about making decisions which could potentially oppress minority shareholders;
- (2) a disclosure-based approach - whereby such companies are required to prominently disclose to investors (and potential investors) the existence of a WVR structure, and the corresponding risks associated with a WVR structure. In addition, AIMA members would endorse the proposal in para 153 of the Concept Paper regarding the disclosure of the identities of the WVR holders. The purpose here is to achieve a level of transparency for investors (current investors and prospective investors): (a) so that investors are clearly alerted to the fact that a company has a WVR structure in place, and that their rights as a shareholder in that company will be limited compared with their rights as a shareholder in a company listed on the Main Board; and (b) so that full details of the WVR structure implemented within the company are disclosed to investors in the listing documents, in order that investors are fully aware of how the WVR structure operates and are able to understand the identities of the persons controlling the company and the manner in which such control powers are exercised;
- (3) a restriction on companies currently listed with SEHK from delisting and then relisting on the New Board (to prevent the erosion of rights of shareholders in existing listed companies);
- (4) minimum equity participation requirements for WVR arrangements in order to ensure that the person(s) controlling the company are actually invested to a material extent in the company;

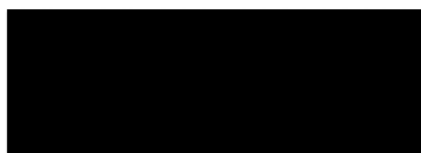
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<sup>2</sup> <http://www.sfc.hk/web/EN/rules-and-standards/principles-of-responsible-ownership.html>

- (5) a requirement that where the company is listed on a recognized exchange and then pursues a secondary listing on the New Board PREMIUM / New Board PRO, the company **must** have a clean corporate governance compliance track record;
- (6) additional ongoing market disclosure obligations for WVR companies - particularly in the context of connected party transactions by that company and involving WVR participants, and any changes to the WVR structure; and
- (7) a "sunset" arrangement, whereby the WVR arrangement falls away following a set period of time after listing on the New Board, to be replaced by conventional voting rights arrangement (one share one vote). This reflects a better compromise between the founders and shareholders in terms of balancing the founder's desire for control of a company (at least in the initial stage following listing) against the "cost" of accessing third party equity investment on international capital markets.

We hope that the SEHK will find the points set out above helpful. We would be very happy to further discuss the responses provided in this letter (if needed).

Yours faithfully



Kher Sheng Lee  
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