



By email < response@hkex.cm.hk > and by post

18 August 2017

Our Ref.: [REDACTED]

Hong Kong Exchanges and Clearing Limited
12/F, One International Finance Centre
1 Harbour View Street
Central, Hong Kong

Dear Sirs,

**Re: (i) New Board Concept Paper ("Concept Paper")
(ii) Consultation Paper on Review of the Growth Enterprise Market (GEM) and
Changes to the GEM and Main Board Listing Rules ("Consultation Paper")**

The Hong Kong Institute of Certified Public Accountants ("the Institute") welcomes the opportunity to provide comments on the subject papers in relation to capital market enhancements. The Concept Paper sets out proposals for the establishment of a New Board to open Hong Kong's capital markets to a broader range of issuers, while the Consultation Paper proposes to reposition GEM as a stand-alone board to serve small to medium-sized companies and to amend Listing Rules to address concerns on the quality and performance of GEM new listing applicants and listed issuers.

The Institute supports that HKEX should continuously review Hong Kong's listing regime and identify areas where the current regime could be strengthened and expanded in order to meet the evolving needs of investors and issuers and enhance Hong Kong's competitiveness as a global capital centre.

"New Economy" industries

The Institute supports that HKEX should review and, if appropriate, expand its listing framework so as to attract a more diverse range of companies to come to list in Hong Kong. While the Institute has no objection, in principle, to the establishment of a New Board to attract potential issuers which do not fit into the current listing regime, we have reservations on the proposal set out in the Concept Paper.

The proposed New Board is intended for "New Economy" industries but there is no generally accepted definition of New Economy¹.

We note that examples of "New Economy" industries are provided in the Concept Paper for demonstration but they need to be further clarified. For example, "Internet & Direct Market Retail" appears to relate to a new mode of operation by the retail industry, while "Software and Technology Hardware" appears to relate to new and innovative products.

¹ "New Economy", as defined under OECD Glossary of Statistical terms, describes aspects or sectors of an economy that are producing or intensely using innovative or new technologies. This relatively new concept applies particularly to industries where people depend more and more on computers, telecommunications and the Internet to produce, sell and distribute goods and services.

In view of the unclear scope, it could be argued that financial services industries such as banking and insurance industries, which continuously develop new products and services and apply new technologies in their operations, would also qualify as "New Economy" industries.

This "New Economy" concept, even if exists, is an evolving concept which can potentially embrace all new industries when technology is constantly being improved and/or any industry that use new technologies to partly or wholly produce, sell or distribute their goods and services. In our opinion, it is impractical to restrict the New Board to any particular industries and any attempt to draw a line will be arbitrary. Consequently, the New Board will simply be for companies that fail to satisfy existing listing requirements.

Companies with non-standard governance structure

--- We would draw attention to the Institute's position expressed in its response to the HKEX consultation on weighted voting rights ("WVR") submitted in November 2014 ("WVR submission", attached at Appendix 1). The Institute has no objection, in principle, to HKEX exploring the feasibility of permitting companies with different voting right structures to be listed in Hong Kong, but changes should not be made on a piecemeal basis without a holistic review of the implications of the WVR on investor protection. We reiterate our recommendations in the WVR submission for introducing wider changes to the corporate governance and regulatory framework in Hong Kong to maintain appropriate investor protection, and for educating the market and investors on the non-standard governance structure and the associated risks.

We maintain our view that companies with WVR structures would need to explain and justify the adoption of a WVR structure and have effective safeguards to protect the interests of ordinary shareholders before being permitted to be listed. Consideration should be given to impose restrictions or conditions on WVR structure that take into account the circumstances of each company to avoid abuses of WVR, such as:

- restrictions on the types of persons that can hold WVR
- restrictions on transfer of WVR to third parties
- requirements to impose a sunset clause on WVR structure.

The basic principle is to avoid abuse of the use of dual/ multiple class share structure to the disadvantage of other shareholders. The Institute considers that investor protection, which is central to Hong Kong's high regulatory standards and the core value of Hong Kong's securities market, should not be compromised.

New Board PRO and New Board PREMIUM

It is proposed in the Concept Paper that New Board PRO is targeted at earlier stage companies that do not meet the financial or track record criteria for GEM or the Main Board. New Board PREMIUM is targeted at companies that meet the existing financial and track record requirements of the Main Board, but which are currently ineligible to list in Hong Kong because they have non-standard governance structures.

We note that the proposed admission financial requirements, the vetting and approval process of new listing applicants and the continuous listing and corporate governance obligations of New Board PREMIUM issuers would be same as the Main Board, and,

this segment is open to both retail and professional investors. As such, it appears that there is little point in creating a New Board PREMIUM to accommodate companies with non-standard governance structures (e.g., WVR). Shares that carry different voting rights can be differentiated from other classes through use of different stock code and stock short names.

Given the above, we consider that there is no need for a separate New Board PREMIUM, and the New Board could simply be a listing venue for pre-profit/ early stage companies that do not meet the existing financial or track record eligibility requirements of the Main Board or GEM and for professional investors only (i.e., the New Board PRO). This would make the proposed listing framework, comprising three boards – New Board, GEM and Main Board, more distinctive and easier to understand. The New Board will be for companies which cannot fit into the current listing framework, while GEM will be re-positioned as a board for small to medium-sized companies and the Main Board for bigger-sized companies.

Given that a New Board PRO issuer would not involve an open offer to the public and only professional investors are eligible to participate, we consider that it is acceptable to adopt a light touch approach on the vetting process of New Board PRO applications.

Instead of applying the sponsor regime, it is acceptable that an applicant to list on New Board PRO would appoint a Financial Adviser, who would exercise its own professional judgement as to what extent of investigations and due diligence work are appropriate for the applicant.

Although it may not be necessary for a New Board PRO applicant to produce a prospectus-standard listing document, HKEX should have rules to set out certain specific items of information to be contained in the listing document, in particular the relevant financial information about the applicant and the level of due diligence work and assurance expected to be provided by certified public accountants on such information.

We do not have objection to the listing applications for the New Board PRO be vetted and approved by the Listing Department under delegated authority from the Listing Committee. Nevertheless, we recommend that there should be a mechanism for the Listing Department to regularly report back to the Listing Committee and seek Listing Committee's view whenever necessary.

In order to maintain the standard and reputation of the Hong Kong capital market, in particular from the investor protection perspective, we consider that applicants for listing on the New Board PRO should demonstrate that they are subject to shareholder protection standards equivalent to those of Hong Kong, irrespective of their place of incorporation, except those apply for a secondary listing on New Board PRO and can demonstrate to the satisfaction of the Listing Department, or the Listing Committee, that they are unable to do so due to the restrictions and regulations of the exchange that they are primary listed.

Segmented approach

While there are merits to adopt a segmented approach with multiple listing boards as a means to cater for the different needs of different types of issuers and different risk appetite of different investors, we consider that the characteristics and the scope of each of the boards should be clearly delineated to avoid confusion. In addition, we



suggest that HKEX should provide a clear roadmap and mechanism of how a listed issuer can migrate its listing from one board to another, when the characteristics of an issuer have changed due to growth and development. Such information would be important for the issuer to plan for its future corporate finance strategies and also crucial to the success of the segmented approach and the attractiveness of each board.

The Consultation Paper proposes that the migration or transfer of its listing from GEM to the Main Board be treated as a Main Board new listing applicant. We are concerned that the proposed re-positioning of GEM and removal of the streamlined transfer process from GEM to Main Board might discourage SME with ambitions and potential to grow from listing on GEM. Reduction in capital raising activities will lead to decrease in the volume of trading on GEM, thereby turning GEM into an inactive board.

In addition, should a New Economy company initially listed on the New Board PREMIUM be allowed to migrate to the Main Board when its non-standard governance features ended or the industry in which it engaged no longer be considered as a New Economy industry? If so, how could this be done? Would it be required to withdraw its listing from the New Board PREMIUM before submission of an application to list on the Main Board? Or could it be traded on the New Board PREMIUM until it migrates its listing to the Main Board? We believe that if a listed issuer no longer has the characteristics for listing on a designated board/ segment and meets the listing criteria for another board/segment, there should be clear mechanism to facilitate their migration to a more suitable board/segment.

The Institute's comments on the detailed proposals in relation to the New Board and review of the GEM and changes to the GEM and Main Board listing rules are set out in the questionnaires attached to this letter.

If you have any questions on this submission or wish to discuss it further, please contact me at the Institute by phone on [REDACTED] or email <[REDACTED]> or Mary Lam, Director, Member Support by phone on [REDACTED] or email <[REDACTED]>.

Yours faithfully,

Raphael Ding
Chief Executive & Registrar

Enc.

Part B Consultation Questions

Please indicate your preference by checking the appropriate boxes. Please reply to the questions below on the proposed change discussed in the Consultation Paper downloadable from the HKEX website at:

<http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2017062.pdf>

Where there is insufficient space provided for your comments, please attach additional pages.

1. Do you agree with the proposal to re-position GEM as a stand-alone board and hence remove the GEM Streamlined Process for GEM Transfers and re-introduce the requirements to (a) appoint a sponsor to conduct due diligence for GEM Transfers; and (b) publish a "prospectus-standard" listing document such that GEM Transfer applications are treated as a new listing application (without requiring the applicant to conduct an offering)?

Yes

No

Please give reasons for your views.

We agree with the proposal to re-position GEM as a board to serve small to medium-sized listed issuers. Accordingly, it is more appropriate to change the name of the board to "SME Board" to properly reflect its position rather than renaming it as "GEM" which does not have any meaning and is not reflective of the type of its listing applicants or listed issuers.

We consider that the re-introduction of the requirements to (a) appoint a sponsor to conduct due diligence for GEM Transfers; and (b) publish a "prospectus-standard" listing document such that GEM Transfer applications are treated as a new listing application should apply only when there is public offering of shares in GEM Transfers. Otherwise, such requirements would only significantly increase the transaction costs of the listed issuer but with little benefit/ value-add to the existing shareholders, as the existing GEM listed issuers should have already had a period of track record and complied with all the continuous listing obligations.

The current proposal is to change the GEM into a board for SMEs. However, it is not uncommon that a smaller company initially listed on GEM will grow to meet the admission requirements of the Main Board and there may be good reasons for it to migrate to the Main Board. If GEM listed issuers are discouraged from migrating to the Main Board due to the stringent requirements and process and the high transaction costs involved (as they will be treated as new Main Board listing applicants), we are concerned that the proposals would discourage the listing of companies on GEM and reduce the liquidity of stocks trading, turning GEM into an inactive board.

We are of the view that a streamlined process for GEM transfer should be retained. The existing transfer process should be reviewed and enhanced but not to the extent equivalent to treat the transfer as a Main Board new application.

2. Do you agree with the proposal to require all GEM Transfer applicants to have (a) published and distributed at least two full financial years of financial statements after their GEM listings; and (b) not been subject to any disciplinary investigations by the Exchange in relation to a serious breach or potentially serious breach of any Listing Rules for 24 months before they can be considered for a GEM Transfer?

Yes

No

Please give reasons for your views.

3. Do you agree with the proposal to retain the current track record requirement under the GEM Listing Rules (i.e. two financial years)?

Yes

No

Please give reasons for your views.

4. Do you agree with the proposal to retain the current practice of not requiring a GEM applicant that can meet the Main Board admission requirements to list on the Main Board instead of GEM?

Yes

No

Please give reasons for your views.

We do not agree to make this a mandatory requirement. Nevertheless, we believe that GEM listed issuers are more willing to migrate their listings to the Main Board if there is a streamlined process for such transfer. See also our response to Q1.

5. Do you agree with the proposal to increase the Cashflow Requirement from at least HK\$20 million to at least HK\$30 million?

Yes

No

Please give reasons for your views. We invite suggestions on other potential quantitative tests for admission to GEM.

As GEM is now proposed to be re-positioned as a board for SMEs, it is more appropriate to align its listing requirements with those of the Main Board but at a lower amount. Accordingly, we propose that the cashflow requirement be replaced by a profit requirement over the two years track record period. The level of profit could be determined later. An initial suggestion is an aggregate of HK\$20 million for the track record period.

6. Do you agree with the proposal to increase the minimum market capitalisation requirement at listing from HK\$100 million to HK\$150 million?

Yes

No

Please give reasons for your views.

7. Do you agree with the proposal to increase the post-IPO lock-up requirement such that controlling shareholders of GEM issuers:

(a) cannot dispose of any of their equity interest in a GEM issuer within the first year of listing; and

(b) cannot dispose of any interest in the subsequent year that would result in them no longer being a controlling shareholder as defined under GEM Listing Rule 1.01?

Yes

No

Please give reasons for your views.

8. Do you agree with the proposal to introduce a mandatory public offering mechanism of at least 10% of the total offer size for all GEM IPOs?

Yes

No

Please give reasons for your views.

9. Do you agree with the proposals to align the GEM Listing Rules on:

(a) placing to core connected persons, connected clients and existing shareholders, and their respective close associates with those under Appendix 6 to the Main Board Listing Rules and Guidance Letter HKEX-GL85-16 "*Placing to connected clients, and existing shareholders or their close associates, under the Rules*"; and

Yes

No

Please give reasons for your views.

(b) the allocation of offer shares between the public and placing tranches and the clawback mechanism with those in Practice Note 18 to the Main Board Listing Rules?

Yes

No

Please give reasons for your views.

10. Do you agree with the proposal to increase the minimum public float value of securities from HK\$30 million to HK\$45 million?

Yes

No

Please give reasons for your views.

11. Do you agree with using the Profit Requirement to determine eligibility to list on the Main Board?

Yes

No

If not, what alternative test should be used? Please give reasons for your views.

It is noted that there are already alternative tests for a Main Board listing applicant to meet the basic conditions for listing - profit test; market cap/revenue/cash flow test; or market cap/revenue test.

12. If you agree to retain the Profit Requirement, do you agree that the current level of profit under the Profit Requirement should remain unchanged?

Yes

No

Please give reasons for your views.

13. Do you agree with the proposal to increase the minimum market capitalisation requirement at listing for Main Board applicants from at least HK\$200 million to at least HK\$500 million?

Yes

No

Please give reasons for your views.

14. Do you agree with the proposal to proportionately increase the minimum public float value of securities for Main Board applicants from HK\$50 million to HK\$125 million?

Yes

No

Please give reasons for your views.

15. Do you agree with the proposal to increase the post-IPO lock-up requirement such that the controlling shareholders of Main Board issuers:

- (a) cannot dispose of any of their equity interest in a Main Board issuer within the first year of listing; and
- (b) cannot dispose of any interest in the subsequent year that would result in them no longer being a controlling shareholder as defined under Main Board Listing Rule 1.01?

Yes

No

Alternatively, do you believe that it is not appropriate to extend the post-IPO lock-up requirements for Main Board applicants, given that they are less likely to have the characteristics identified in the 2016 Suitability Guidance Letter because of their larger size and our proposal to raise the minimum market capitalisation requirement to HK\$500 million.

Please give reasons for your views.

16. Do you agree that the proposals for the Main Board should be considered independently irrespective of the outcome of the proposals for GEM?

Yes

No

Please give reasons for your views.

- End -