

Part B Consultation Questions

Please indicate your preference by checking the appropriate boxes. Please reply to the questions below that are raised in the Consultation Paper downloadable from the HKEX website at:

<http://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/June-2018-Backdoor-and-Continuing-Listing/Consultation-Paper/cp201806.pdf>

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

1. Do you agree with the proposal to codify the assessment criteria under the principle based test in a Note to the proposed Rule 14.06B?

Yes

No

If your answer is "No", please give reasons for your views.

However, owing to the nature of the subject, which is always evolving, this is best dealt with by Guidance from the Exchange, to be updated from time to time. As evident by the proposed changes in the consultation paper, while the Exchange's intention is to make them "qualitative" in nature, they came out lengthy and tried to cover all the bases, which lend support to my view that these assessment criteria should not be codified.

Once these changes have been codified, any future changes will need another round of consultation, which is not desirable, because in that case, the Exchange would be deprived of the ability to swiftly and effectively react to changes in the market and business environment, which in all fairness, the Exchange has been good at.

2. Do you agree with the proposal to extend the current criterion "issue of restricted convertible securities" in the principle based test to include any change in control or de facto control of issuers?

Yes

No

If your answer is "No", please give reasons for your views.

This in effect makes the "change of control" requirement in the brightline test redundant.

Further, unlike the "change of control" concept in the Takeovers Code, "de facto" control is not defined, and the market favours certainty. The existing "issue of restricted convertible securities" test is also sufficient to plug any loophole in the brightline test, because not only that the effect of these restricted securities can be quantified, their mere presence in the design of a deal is an obvious reflag..

In any event, I would submit that the Exchange can take comfort from the established "concert party" triggers in notes 1 and 6 to Rule 26.1 to the Takeovers Code and the various Panel Decisions (e.g. Wing Hang Bank, Limited decision) which have sufficiently dealt with the Exchange's concerns in this regard.

The proposed amendments to Rule 14.06E also rely on the Takeovers Code "control" concept, and, thus, the proposed changes here will be at odds with Rule 14.06E.

3. (a) As regards the "series of arrangements" criterion, do you agree with the proposal to include transactions and arrangements that take place in reasonable proximity or are otherwise related and normally within a three-year period?

Yes

No

If your answer is "No", please give reasons for your views.

No objection in principle regarding the aggregation, but:

First, in the fast changing business environment, 24 months is already a long period of time, and I would suggest the Exchange stick to this long established practice. In any event, I would suggest that whether it's 2 years or 3 years, there should be a hard cut-off (i.e. remove the word "normally") to provide certainty.

Second, I would submit that "greenfield projects" should be excluded from all the proposed changes in the Consultation Paper. A lot of times, investors buy into a company on the strength of its management. If the original business is failing (which will become more frequent due to innovation, globalisation and the imminent and escalating trade war), and the management see an opportunity to start a new business, they are the best judge of that and should be left alone to make that call and proceed. This is especially the case where the issuer makes use of or modifies its existing assets and resources (e.g. production facilities or land resources) to produce new products or change the business model to the provision of contract manufacturing services (as opposed to producing and selling the end products), or develop its factory land into commercial or residential properties with bank or shareholder financing. Any concern on the part of the Exchange on "shell creation" can be addressed by requiring the issuer to supply a "viable and sustainable business" proposal with a positive recommendation of an independent financial adviser and the approval of an independent shareholders' vote.

Rider 11A

(b) Do you agree with the proposal to amend the RTO Rule 14.06B to clarify that a series of acquisitions may include proposed and/or completed acquisitions?

Yes

No

If your answer is "No", please give reasons for your views.

Yes and No.

I believe that it is fair to look at and aggregate completed acquisitions when considering how the upcoming / proposed transaction should be treated. However:

(i) it would be unreasonable to subject a previously completed acquisition to the RTO Rules (for example, as suggested in paragraph 49 of the Consultation Paper). Issuers/business managers do transactions to accomplish one objective, that is such would be in the interest of the issuer/profitable to do so. Thus, it is logical and natural that the target of a "subsequent" transaction would be in a similar or even the same line of business as the "earlier" target's; it is only because the earlier acquisition is a success or its result indicates that it is the right way forward, the issuer would then consider to expand the business in the same direction. I would submit that this is how most of the issuers behave, and such "facts" should not conclude that the acquisitions form a "pre-ordained" series of transactions. Such logic would lead to the aggregation of a lot of transactions that plainly are not what the Exchange wants to tackle. I would be grateful if the the proposed changes to the Rules make such a distinction.

(ii) the concepts of "attempt" and "subsequently aborts" (in parageaph 52 of the Consultation Paper) should be left out, because issuers abort deals for many reasons. It could be a commercial decision, as a better opportunity emerges, or that the effort and costs involved in resolving the regulatory hurdles become too great, or a combination of many factors. Thus, if the proposed acquisition is aborted, and in such situation the Exchange is still empowered to take action with regard to previously completed acquisitions, such action on the part of the Exchange (triggered by the existence of an aborted deal) tantamounts to a presumption under the Listing Rules that the previous acquisition was a part of a "pre-ordained" series of acquisition, where that is never proven to be the case (especially where the subsequent acquisition is aborted, which also goes to show that the first acquisition can survive and subsist independently without the proposed acqusition), and this, in other words, is a presumption of guilt, and that goes against the fundamentals of the legal system of Hong Kong.

The proposal to empower the Exchange to require an issuer to engage a financial adviser as outlined in that paragraph, which power, if exercised, will be unduely burdensome on the issuer, as it will detract the management in that situation from its business and casue the issuer to incur the costs (that it desperately needs) for a report that adds nothing to the disclosures that one can find in its annual report, which is also not in the interests of the shareholders as a whole.

4. (a) Do you agree with the proposal to retain the bright line tests under Rules 14.06(6)(a) and (b) in a Note to the proposed Rule 14.06B?

Yes

No

If your answer is "No", please give reasons for your views.

- (b) Do you agree with the proposal to extend the aggregation period from 24 months to 36 months under the bright line test currently set out in Rule 14.06(6)(b)?

Yes

No

If your answer is "No", please give reasons for your views.

In the fast changing business environment that we are in, 24 months is already a long period of time, and I would suggest the Exchange stick to this long established practice.

5. (a) Do you agree with the proposed changes to Rule 14.92 (proposed Rule 14.06E) as described in paragraph 56 of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

The drafting refers to a "proposed or intended" change in control. (i) What does the Exchange plan to capture here (presumably there has to be a connection between the "disposal" and "change in control")? (ii) What does "intended change in control" mean, how does it differ from a "proposed change in control"?

I would agree with this proposal if the drafting says "... its existing business (a) in connection with a proposed change in control..."

But please:

(i) limit this to 24 months; and

(ii) set out the quantitative benchmark for what constitutes a "material" disposal.

(b) Do you agree with the proposal to add a Note to proposed Rule 14.06E as described in paragraph 59 of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

See comments above

6. (a) Do you agree with the proposal to add a new Rule 14.06C for "extreme transactions" as described in paragraph 62 of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

But:

1. the requirement of "... under the control of a large business enterprise..." in the proposed Rule 14.06C(1)(b) should be changed to:

(i) the concept of single largest substantial shareholder (i.e. as opposed to "control"); OR

(ii) being single largest substantial shareholder for a period of not less than 2 years before the time of the proposed acquisition AND being the controlling shareholder (within the meaning of the Takeovers Code) at the time of the proposed acquisition.

I would submit that Rule 14.06C(1)(b) should be amended per above so that it can work with the Exchange's "de facto control / single largest substantial shareholder" concepts in the proposed Note 1(d) to Rule 14.06B.

2. please remove the concept of "large business enterprise", because the scale and size of which are impossible to define; and, if there is more than one ultimate owner, what are the different relationships between the owners that will make them qualify for this exception.

Rider 15A

(b) Do you agree with the disclosure requirements for circulars of extreme transactions set out in proposed Rules 14.53A(1) and 14.69?

Yes

No

If your answer is "No", please give reasons for your views.

No views

(c) Do you agree with the due diligence requirements for extreme transactions under proposed Rule 14.53A(2)?

Yes

No

If your answer is "No", please give reasons for your views.

No views

7. (a) Do you agree with the proposal to amend Rule 14.54 and to add Rule 14.06C(2) as described in paragraph 69(i) of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

If an issuer is not suitable for Listing, the Exchange should delist it. For so long as it is not delisted, then the pre-acquisition business of the issuer, hence the concept of "enlarged group" (in Rule 14.06C(2)) should not enter the equation here.

As this is not an IPO situation, whether there is "sufficient public interest" and "300 public shareholders" (as reasons cited in paragraph 71) should and can only be judged by the public AFTER the completion of the proposed acquisition and the effect of the full integration thereof transpires, but not before the deal is done. The number of shareholders and investors' interest in the issuer before the deal is only a reflection of the pre-acquisition business, and should not be used as a proxy for the target or the issuer after the acquisition.

Furthermore, for example, an existing issuer may develop certain continuing connected transactions over the years (after its initial Listing) for various genuine business reasons, but "continuing connected transactions" are generally frowned upon by the IPO division of the Exchange, hence a conflict here.

- (b) Do you agree with the proposal to amend Rule 14.54 to impose additional requirements on RTOs proposed by Rule 13.24 issuers as described in paragraph 69(ii) of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

My views on the inclusion of the concept of the enlarged group in 7(a) apply here.

8. (a) Do you agree with the proposed Rule 14.57A to clarify the track record requirements for extreme transactions and RTOs that involve a series of transactions and/or arrangements?

Yes

No

If your answer is "No", please give reasons for your views.

No views

- (b) Do you agree with the proposed Rule 4.30 that sets out the requirements for preparing pro forma income statement of all the acquisition targets in the entire series of acquisitions (where applicable, would include any new business developed by the issuer that forms part of the series) for the track record period?

Yes

No

If your answer is "No", please give reasons for your views.

No views

9. Do you agree with the proposal to add a new Rule 14.06D to codify, with modification, the practice under Guidance Letter GL84-15 as described in paragraph 81 of the Consultation Paper?

- Yes
 No

If your answer is "No", please give reasons for your views.

No views

10. Do you agree with the proposal to require issuers to have a business with a sufficient level of operations and assets of sufficient value to support its operations to warrant the continued listing of the issuer's securities?

- Yes
 No

If your answer is "No", please give reasons for your views.

Agree to remove the existing note, as it is out of date.

Yes with regard to "sufficient level of operations", but No with regard to "assets of sufficient value". The latter should NOT be a requirement in this day and age, especially with new technologies, new business models and new economies emerging so frequently, where "asset value" is not a meaningful benchmark anymore.

I would respectfully submit that, as a matter of principle, the Listing Rules should not provide that "... the Exchange considers that the issuer does not have a business that has substance and/or that is viable and sustainable..."; as this is not something that is appropriate for the Exchange, as a regulator, to raise. This is in any case implied in the the wording of Rule 13.24.

11. (a) Do you agree with the proposal to add a Note to the proposed Rule 13.24(1) as described in paragraphs 107 to 109 of the Consultation Paper?

- Yes

No

If your answer is "No", please give reasons for your views.

Please see my comments on issues raised in Q10

(b) Do you agree with the proposal to remove the Note to Rule 13.24 as described in paragraph 112 of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

Please see my comments on issues raised in Q10

12. Do you agree with the proposal to exclude an issuer's securities trading and/or investment activities (other than a Chapter 21 company) when considering the sufficiency of the issuer's operations and assets under Rule 13.24?

Yes

No

If your answer is "No", please give reasons for your views.

13. Do you agree with the proposal to extend the definition of short-dated securities in the cash company Rules to cover investments that are easily convertible into cash ("short-term investments")?

Yes

No

If your answer is "No", please give reasons for your views.

14. Do you agree with the proposal that the exemption under Rule 14.83 shall only be confined to clients' assets relating to the issuer's securities brokerage business?

Yes

No

If your answer is "No", please give reasons for your views.

15. Do you agree with the proposal to confine the revenue exemption to purchases and sales of securities only if they are conducted by banking companies, insurance companies and securities houses within the listed issuers' group?

Yes

No

If your answer is "No", please give reasons for your views.

16. Do you agree with the proposal to require issuers to disclose in their annual reports details of each securities investment that represents 5% or more of their total assets (as described in paragraph 134 of the Consultation Paper)?

Yes

No

If your answer is "No", please give reasons for your views.

Agree in principle, but can the Exchange elaborate on:

(i) why the threshold should be set at 5%, but not 8% or 10%; and

(ii) clarify what constitutes "securities investment". Does it only capture equity securities listed on the Hong Kong Stock Exchange? Does it include bonds? Further, the Exchange has, through Listing decisions HKEx-LD53-2 and HKEx-LD76-1, interpreted Listing Rule 14.04(1)(g) to exempt treasury activities. I would request that the Exchange confirm that "securities investments" that fall under the treasury activities are exempt, or that a disclosure of the issuer's treasury policy together with the total value of all such securities as at the balance sheet date would be sufficient. Presumably, "securities investment" also does not include those "short-term investments" in the proposed revisions to Rule 14.82.

17. Do you agree with the proposal to codify the requirements set out in Listing Decision LD75-4 (as described in paragraph 137 of the Consultation Paper) for significant distribution in specie of unlisted assets into the Rules?

Yes

No

If your answer is "No", please give reasons for your views.

18. Do you agree with the proposal to require disclosure on any subsequent change and the outcome of any financial performance guarantee of a target acquired by the issuer in a notifiable or connected transaction as set out in paragraph 140 of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

19. (a) Do you agree with the proposal to require disclosure on the identity of the parties to a transaction in the announcements and circulars of notifiable transactions?

Yes

No

If your answer is "No", please give reasons for your views.

(b) Do you agree with the proposal to require the disclosure on the identities and activities of the parties to the transaction and of their ultimate beneficial owners in the announcements of connected transactions?

Yes

No

If your answer is "No", please give reasons for your views.

20. Do you agree with the proposal that if any calculation of the percentage ratios produces an anomalous result or is inappropriate to the sphere of activities of the issuer, the Exchange (or the issuer) may apply an alternative size test that it considers appropriate to assess the materiality of a transaction under Chapter 14 or 14A?

Yes

No

If your answer is "No", please give reasons for your views.

Rider 11A

Third, as the Exchange is proposing in paragraph 46 of the Consultation Paper to capture “multiple new businesses in different sector”, I would respectfully ask the Exchange to grandfather announced transactions such that those previously announced “unrelated” transactions will not be taken into account in situations where the Exchange seeks to apply the new RTO and Extreme transaction rules.

Rider 15A

3. Please remove the requirement of “a principal business of a substantial size” for the issuer as a pre-requisite, because:

(i) it is impossible to define and quantify if a business has a “substantial” size, and will introduce another uncertainty to these already complicated new Rules; and

(ii) this concept is already captured in the Exchange’s proposed amendments to Rule 13.24(1), and I would respectfully submit that, instead of further complicating the matter and causing confusion to the market users, the Exchange can simply exercise its power under that provision to delist the issuer. Therefore, I would respectfully urge the Exchange to remove Rule 14.06C(1)(a) from the proposed amendments..

- End -