

29 October 2021

Hong Kong Exchanges and Clearing Limited
8th Floor, Two Exchange Square
8 Connaught Place
Central
Hong Kong

Re: Special Purpose Acquisition Companies CP

Subject: Response to the Stock Exchange of Hong Kong's Consultation Paper, *Special Purpose Acquisition Companies*

Dear Sir/ Madam,

Deloitte Touche Tohmatsu ("Deloitte China") welcomes the consultation from the Stock Exchange of Hong Kong ("the Exchange") on *Special Purpose Acquisition Companies* ("SPAC").

With the Exchange having opened a discussion with the market through this consultation on whether a SPAC listing regime should be created in Hong Kong, we express our support for the proposed tailored regime and measures, believing these will underscore Hong Kong's leadership as an international financial centre and at the same time safeguard investors' interests, especially retail investors.

In view of the momentum of SPAC listings in the US over the last few years, including in attracting companies from Greater China and South East Asia to make such listings, and the recent introduction of SPAC listings in Singapore, it is truly time for Hong Kong, one of the world's top listing destinations, to devise and develop such a regime.

Following its 2018 listing regime reform, Hong Kong's ecosystem for nurturing technology and innovative businesses has become more developed, and its listing mechanism has matured, improving market sentiment. We believe more technology companies, especially those involved in Asia's booming mergers and acquisitions ("M&A") activity, will be drawn to make SPAC listings in Hong Kong once this regime is established. Chinese technology firms will continue to be drawn to list in Hong Kong due to the attractiveness of making a SPAC listing as an alternative to a traditional initial public offering ("IPO") and the greater certainty of having a reasonable valuation through a SPAC listing.

In the last couple of years, the Exchange has embarked on several important reforms, introducing more listing options for issuers and investment products for investors. This has not only enhanced Hong Kong's attractiveness and diversity as a listing venue for Greater China and overseas issuers, but also made Hong Kong's capital market more resilient and vibrant amid macro-economic and geopolitical challenges such as the COVID-19 pandemic. This proposed regime will be an important step for the Exchange to respond to growing demand for listings of this kind, particularly among technology and innovative businesses.

A De-SPAC Transaction can offer a De-SPAC Target greater certainty of valuation than it might otherwise receive through the pricing process of a traditional IPO. This, and the use of tailored M&A to structure a negotiated valuation among the SPAC Promoters, target shareholders and private investments in public equity ("PIPE"), could also make the SPAC listing route more lucrative to companies with no or few peers from the same market sector.

Although some of the Exchange's reforms, such as allowing listings of weighted voting rights structures, were controversial before their implementation, the Exchange's approaches, including 2018's listing reforms, have been a huge success. This success includes drawing deep liquidity to the market and issuers, and elevating Hong Kong to become the world's 2nd largest listing venue for biotech companies. We appreciate that this success is attributable to the Exchange's carefully designed measures, including requirements that address the needs and situation of a market with substantial retail participation and the lack of a class action mechanism in Hong Kong.

Compared with SPAC listing regimes in the US, UK and Singapore, some might suggest that the proposed regime for Hong Kong would be a more premium market, appealing to a niche of investors and companies, such as by limiting SPAC investment to Professional Investors and having more safeguards. However, it also might:

- Provide one of the longest De-SPAC Transaction deadlines among similar regimes, potentially up to a maximum of 42 months if a SPAC obtains approval from its shareholders for the extension at a general meeting, with a maximum of 6 months, and the Exchange permits such an extension. This is necessary as the proposed De-SPAC process in Hong Kong will require a complete due diligence and vetting process. Generally speaking, a usual IPO process takes at least 8 to 9 months. It would become unreasonable to provide merely another 12 months for a SPAC to handle these processes once a De-SPAC Transaction is announced, and on top of this granting another 6 months' grace period if its shareholders and HKEX agree. This would provide greater flexibility for SPAC Promoters to engage in optimal De-SPAC Transactions; and
- Given the initial offering must be at least HKD1 billion (the 2nd highest threshold after the UK SPAC regime's GBP100 million), such an entrance requirement could encourage SPAC Promoters to raise more IPO funds and eventually raise more proceeds to support the future growth of Successor Companies.

Given the example of implementing the 2018 listing reforms, it is desirable that the Exchange continues to innovate and reform while taking Hong Kong's market situation into consideration, rather than directly adopting the types of listing regimes of other leading financial markets merely for the sake of competition. We agree that there is also a need to enhance Hong Kong's reputation for quality listings with proper investor safeguards and balance this with the openness of the market. A fully open new market for general participation in SPAC listings might be detrimental given the Hong Kong market's substantial retail participation, the nature of SPAC listings and investments, and rising risks of listings of sub-standard businesses and/or assets in instances where circumvention of the criteria for new listings occurs. Nevertheless, after the application of various safeguards and mechanisms to help remove a combination of risks associated with SPACs, when the Successor Company is listed by meeting all of the new listing requirements after a De-SPAC Transaction, every investor, including retail ones, can still have the opportunity to trade the securities of the Successor Company.

Although there have been widespread concerns over the implementation of a SPAC listing regime against the backdrop of heightened scrutiny and intensive efforts by the Exchange and the Securities & Futures Commission's ("SFC") to address shell activities in recent years, Deloitte China, having been the reporting accountants of many IPOs in Hong Kong, acknowledges that many designed safeguards outlined in the Consultation Paper will help to mitigate this major risk, including by:

- limiting the marketing and trading of SPAC's securities to Professional Investors;
- allowing only SPACs with experienced and reputable SPAC Promoters seeking quality De-SPAC Targets to list, such as requiring that at least one SPAC Promoter holds one or two types of licences issued by the SFC, and holds at least 10% of the Promoter Shares at listing and during the lifetime of the SPAC;
- setting a high entry point for SPAC listing applicants, including the need to raise at least HKD1 billion in their IPOs;

- requiring each Successor Company to meet all the new listing requirements of the Main Board;
- applying the Takeover Code to a SPAC during its listing;
- requiring a De-SPAC Target to value at least 80% of the SPAC IPO proceeds; and
- excluding investment companies from being eligible to become De-SPAC Targets.

Furthermore, to alleviate the risk of having an artificial valuation of a De-SPAC Target to meet the minimum market capitalisation requirement for the listing of its Successor Company, we believe that the proposed valuation mechanism is being carefully designed, including by:

- requiring a valuation validation of the target by independent third parties, such as outside PIPE investors, which is not mandatory in the US and UK regimes;
- having an outside, independent PIPE investment take up at least 25% of the expected market capitalisation of the Successor Company (or a lower percentage of 15% to 25% in the case of a Successor Company with an expected market capitalisation, at the time of listing, of more than HKD1.5 billion);
- having at least one independent PIPE investor as an asset management firm to manage assets or funds of at least HKD1 billion; and
- requiring that an independent financial advisor determine the independence of a PIPE investor in a De-SPAC transaction.

Although the regime might be open only to Professional Investors, we appreciate the Exchange's effort in considering the safeguards for "minority SPAC shareholders", such as allowing them to redeem the shares in the event that they intend to vote against:

- a material change in the SPAC Promoter managing a SPAC or the eligibility and/or suitability of a SPAC Promoter;
- a De-SPAC Transaction; or
- a proposal to extend a De-SPAC announcement deadline or the completion deadline of a De-SPAC Transaction.

All these safeguards are crucial for successful implementation of the proposed regime. We furthermore suggest that:

- the corresponding safeguards be incorporated into the Listing Rules in compulsive terminology to facilitate their enforcement, so that serious consequences would result from any breach of these Listing Rules;
- the Exchange considers requiring a SPAC Promoter to provide an undertaking to the issuer that they will comply with these safeguards for the benefit of all existing and future minority shareholders; any circumvention of or non-compliance with these requirements under the Listing Rules be regarded as a contravention of the Securities and Futures (Stock Market Listing) Rules and/or the Securities and Futures Ordinance, so that the SFC retains the capacity to exercise its powers over listing applicants and issuers;
- the Listing Rule disclosure requirements to be still applied to SPACs prior to a De-SPAC Transaction such as those set out in Appendix 14 of the Listing Rules for Corporate Governance report. This will provide useful information about a SPAC, including its corporate governance capabilities, to potential investors on a timely basis instead of allowing them access to such information only upon the listing of the Successor Company;

- safeguards on share redemption be enhanced by including the potential for shareholders to vote in favour of the De-SPAC Transaction while still being given an option to redeem a portion of the SPAC Shares for their own cash requirements and retain the remaining shares in the Successor Company. For example, “bulldog provisions” are being applied to listed SPACs in the US. These allow SPAC shareholders (together with parties they are acting together with) to redeem only up to a limit of the percentage of publicly held shares, which is generally between 10% to 20%; and
- specify whether the requirements set out at paragraph 216 for SPAC Promoters, which are viewed favourably by the Exchange, are mandatory or recommended. Many of those conditions are quantitative. SPAC Promoters who can meet such conditions might not have experience in the relevant industries of the De-SPAC Targets, and those with such relevant experience might not be able to meet the conditions. Hence, clarification is also needed as to whether the track record of the deals SPAC Promoters have completed, or their experience in the industries of De-SPAC Targets, comes first.

We thank the Exchange for giving such a valuable opportunity to express our views on this potential regime. We also look forward to seeing it come into effect soon.

Yours faithfully,

