HK FINANCIAL SERVICES DEVELOPMENT COUNCIL 香港金融發展局

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27 October 2021

Mr Alejandro Nicolas Aguzin
Chief Executive
Hong Kong Exchanges and Clearing Limited
8th Floor, Two Exchange Square
8 Connaught Place, Central, Hong Kong

BY HAND

Dear ~~Nicolas~~, Dear Nicho,

Re: Consultation Paper on Special Purpose Acquisition Companies

We refer to the captioned consultation paper published in September 2021 by the Stock Exchange of Hong Kong ("SEHK") and are delighted to submit our comments (enclosed) for the SEHK's consideration.

Should you have any queries, please contact the FSDC by post, by telephone on [redacted] or by email at [redacted].

[redacted]

(Mr Laurence Li)
Chairman
Financial Services Development Council

Encl.

cc The Honourable Laura Cha Shih May-lung, GBM, GBS, JP, Chairman, Hong Kong Exchanges and Clearing Limited

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HK FINANCIAL SERVICES DEVELOPMENT COUNCIL 香港金融發展局

Press Release

FSDC releases response to SEHK's Consultation Paper on Special Purpose Acquisition Companies

Hong Kong, 27 October 2021 - The Financial Services Development Council (FSDC) published a response to Consultation Paper on Special Purpose Acquisition Companies (SPAC), issued by the Stock Exchange of Hong Kong Limited (SEHK) in September. In general, the FSDC is in support of introducing a new listing option, which will add to Hong Kong's proposition as an ideal listing and capital formation market.

"Over the years, Hong Kong has been a premier IPO centre of choice, ranking the first in the world in seven of the last twelve years. In recent years, we have seen the rise of SPAC listings, due in part to the evolving investment demands in global markets. We applaud the HKEX's effort to address the trend and bringing creativity to the market, which will help us to become an appealing market in the international IPO arena" said Laurence Li SC, Chairman of the FSDC. "Alongside the SPAC regime, a balanced protection mechanism to safeguard interests of the investing public is crucial, while proper investor education is also essential."

The response acknowledges that as a complementary regime to the traditional IPO route, SPAC framework for Hong Kong is judicious with enhanced multi-level safeguards and strong emphasis placed on investor protection and market quality. It aims at achieving an ultimate goal of long-term success by attracting sizeable companies with substantial quality and protecting public interest.

"The proposed SPAC regime will be able to integrate with the existing listing mechanism, providing an additional channel for companies to raise funds and expand options for investors. Owing to the relatively high-risk nature of and uncertainties around SPAC investments, the proposals set out by the SEHK is conducive to striking a balance between market opportunities and scalability, while safeguarding investors' interests. The SPAC regime will further strengthen the city as one of the world's best fundraising centres." Dr King Au, Executive Director of the FSDC, added.

FSDC agrees that the proposals set out will bring about betterment of the fundraising capabilities. Some other observations are also shared in the response with a view to further enhancing popularity of the regime among potential market participants over the longer term.

The full version of the response can be downloaded from the FSDC website: www.fsdc.org.hk.

About the FSDC

The FSDC was established in 2013 by the Hong Kong Special Administrative Region Government as a high-level, cross-sectoral advisory body to engage the industry in formulating proposals to promote the further development of the financial services industry of Hong Kong and to map out the strategic direction for the development.

The FSDC has been incorporated as a company limited by guarantee with effect from September 2018 to allow it to better discharge its functions through research, market promotion and human capital development with more flexibility.

Keep up with the latest FSDC news by following our LinkedIn, Twitter & YouTube.

- Ends -

FSDC's Response to SEHK's Consultation Paper on Special Purpose Acquisition Companies

The Financial Services Development Council ("FSDC") welcomes the Stock Exchange of Hong Kong Limited ("SEHK")'s publication of the Consultation Paper (the "Consultation Paper") on Special Purpose Acquisition Companies ("SPAC") in September 2021. The FSDC is in principle supportive of the introduction of a new listing option, which will further enhance Hong Kong's capital formation capabilities as an international financial centre by providing an additional option for both investors and potential issuers.

I. Background

Despite SPACs having been around since 1993, its proliferation has only accelerated in the US since 2019. Since then, funds raised comparable to traditional IPOs, amounting to US$4.2 billion and accounting for 53% of all IPO funds raised in 2020 and 62% as of Q2 2021[1].

The momentum has led to the emphasis on such listing structures across the globe. For instance, the UK revised the SPAC rules in August this year, enhancing its flexibility to attract more listings; in Asia, in addition to Korea and Malaysia, Singapore has also made SPACs listing on its Mainboard permissible in September.

Over the years, Hong Kong has been a premier IPO centre of choice, with IPO funds raised ranking first in the world in seven of the last twelve years and second only after the US in 2020. The FSDC believes it is imperative for the city to maintain its competitiveness as a leading international financial centre by keeping pace with global developments. Given the evolving market needs and investment appetites, now is an opportune time for Hong Kong to permit SPAC listings, with an optimal set of safeguards. Such optimisation of the market structure will offer an additional channel for companies to raise funds and expand investment options for market participants, while upholding investor protection.

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[1] EY Global IPO Trends 2021 Q2 Report (https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/ipo/ey-global-ipo-trends-2021-q2-v1.pdf)

Benefits and opportunities of introducing SPACs to Hong Kong

It is worth noting that the proposed SPAC regime will be complementary to the traditional IPO route, strengthening the SEHK's offerings rather than replacing the mainstream listing. The FSDC echoes the viewpoint in the Consultation Paper that enabling SPAC listings in Hong Kong with strong investor protection can bring benefits to the economy. With the above in mind, we applaud the SEHK's design of Hong Kong's SPAC regime, which has highlighted the city's determination to adopt a far-reaching approach by integrating it into the existing listing market.

The proposed regime aims at achieving an ultimate goal of long-term success by attracting sizeable companies with substantial quality and protecting public interest. As a result of established trust and credibility, genuine interest in our capital market among stakeholders will be induced, and market liquidity can be enhanced. In addition, amidst ongoing geopolitical uncertainties, we believe the proposed SPAC regime will add to Hong Kong's proposition as an ideal listing and capital raising market for new economy companies around the globe, including Mainland China.

II. Comments on the Consultation Paper

Characteristics of the proposed SPAC regime

Drawing references from other financial markets such as the US, UK and Singapore, the proposed SPAC framework for Hong Kong is judicious with enhanced multi-level safeguards and strong emphasis placed on investor protection and market quality.

Among others, the FSDC is, in principle, agreeable to the key safeguards proposed in the Consultation Paper, for the following reasons:

- **Investor Suitability – Restricting the subscription and trading of SPAC securities to Professional Investors (PIs) only.** As SPAC is a new and relatively complex investment option for local investors, there is a need for investor education about SPAC for the investing public. In the light of this and a higher level of risk tolerance for more experienced and sophisticated investors with the appetite for such products, the FSDC believes that certain threshold for participation, at least for the initial stage, would be beneficial.

- **SPAC Promoters – The proposed regime sets out suitability and eligibility requirements of SPAC Promoters which in general are more stringent than other jurisdictions.** For instance, the proposed regime stipulates that one of the SPAC Promoters must be licensed for Type 6 and/or Type 9 activities by the Securities and Futures Commission and hold at least 10% of promoter shares. In view of the absence of operational track record in SPACs, the FSDC acknowledges that SPAC Promoters and its management team will play a key role in the transactions and relevant processes, including but not limited to identifying and negotiating with quality De-SPAC targets for the best interests of investors. In this context, it is necessary to ascertain qualifications of SPAC Promoters as investors are highly dependent on their expertise to make investment decision.

- **Mandatory PIPE Investment – Private investment in public equity (PIPE) is proposed to be a mandatory engagement in the Successor Company** (i.e. the listed issuer resulting from the completion of a De-SPAC Transaction). The Consultation proposes that PIPE investors' contribution should constitute at least 25% of the expected market capitalisation of the Successor Company. Noting that these PIPE investors tend to be more sophisticated and knowledgeable than retail investors, by requiring them to have skin in the game, such an add-on can help ensure reasonable valuations of the Successor Company.

- **Redemption Option and Shareholder Vote – Shareholders who do not agree with the De-SPAC transaction can vote against it at a general meeting and redeem their shares.** The flexible arrangement allows shareholders to steer clear of or reduce exposure to the acquisition in case their interests with SPAC Promoters are deemed not to be aligned. In addition, the FSDC concurs with the proposal of aligning shareholders' vote with redemption rights (i.e. shareholder who vote for the De-SPAC transaction is not eligible to redeem shares), as fairness and genuine transactions are essential to safeguard interests of non-redeeming shareholders.

- **De-SPAC Transaction Deadline – The proposed 36-month timeframe for completing De-SPAC offers more flexibility compared to the 24-month timeframe commonly adopted in other jurisdictions.** This is due in part to extra time required for performing due diligence, and the FSDC trusts that it will allow more flexibility to ensure high quality transaction for the best interest of SPAC investors.

The FSDC notes that the SEHK is mindful of potential issues around SPACs and believes that Hong Kong's long-standing competencies are underpinned by the fair and orderly financial market. With that in mind, the FSDC agrees it is crucial for Hong Kong's SPAC regime to strike the fine balance between capturing market opportunities and safeguarding investors' interests while thriving for market quality.

III. Additional Observations of Global SPACs

The proposals set out in the Consultation Paper are no doubt positive steps to extend the city's lead as one of the world's most prestigious fundraising hubs, the FSDC would like to share the following observations, with a view to consummating the regime for gaining popularity among potential market participants in the long run:

- **Investor Suitability** – In addition to restricting SPAC investment to PIs only, it is proposed that a SPAC must distribute SPAC Shares and Warrants to at least 75 PIs, of which 30 must be institutional PIs. While agreeing that institutional investors have a critical role to play in SPAC listings, various market practitioners have shared their views with the FSDC that an unnecessarily high threshold of relevant requirements would pose additional transaction costs, time and other resources, and in turn reducing the appeal of SPAC as a listing option. In this regard, it would be beneficial if a higher degree of clarity can be provided as to the rationale behind the proposed requirement of minimum number of PIs and institutional PIs, which should facilitate a higher level of understanding of such proposed minimum requirements among market participants.

- **New Listing Requirements of the Successor Company** – Under the SEHK's proposal, a Successor Company will be required to fulfil the new listing requirements in all respects, including due diligence by IPO sponsor, minimum market capitalisation and the usual eligibility and suitability tests. In this regard, market practitioners have shared concerns that such arrangements - especially the need to engage IPO sponsors to perform due diligence - may result in a De-SPAC timeframe essentially similar to that of a traditional IPO listing. It is of the view to some practitioners that it could undermine the intention of offering the SPAC as an alternative and streamlined listing approach. With an aim of allaying queries of practitioners in this respect, the SEHK may consider providing clearer guidance on its service commitment, such as the expected processing timeframe in relation to the De-SPAC process involving a Successor Company.

Furthermore, it is observed that requirements are already in place to safeguard public interest prior to the De-SPAC transaction in the proposed regime, including but not limited to eligibility requirements of SPAC Promoters, investor suitability, etc. With an aim of expediating the process, the FSDC suggests exploring relaxation in the operational arrangement at the De-SPAC transaction stage if the intended benefit could still be achieved.

- **Definition of Professional Investors (PIs)** – The proposed SPAC regime would only allow investments from PIs only. Hence, the definition is an overarching element that may impact investor participation and growth of PI only instruments. While it would go beyond the scope of the Consultation exercise, the FSDC is formulating policy recommendations in relation to Private Wealth Management and the definition of PI will be further studied, with a view to aligning with the evolving market.

- **Investor education** – SPAC is a new concept in Hong Kong's listing market, relatively high risk in nature with uncertainties around the investment. In addition to the proposed investment and trading restriction to PIs, adequate investor education for the public is still essential, especially so since De-SPAC transactions will be open to retail investors. Comprehensive educational materials should be developed to cover fundamentals of the regulatory framework, valuation basics, trading mechanisms as well as underlying risks to equip investors with sufficient knowledge and risk awareness.

- **Risk appetite of different segments** – In principle, professional investors and retail investors would have different risk investment appetites. Creating different levels of access to investments for these investors in both primary and secondary markets, might be the way forward to cater to the varied needs of investors of different segments. Each segment should be granted access to investment vehicles that are aligned with their risk appetites.

It is believed that adopting a market driven approach, allowing issuers to make decisions on investor suitability could raise effectiveness. In this regard, the FSDC is conducting a study on potentially adopting a market driven approach, where issuers will be allowed the discretion to choose their market segment, aiming to identify measure that can broaden the role of Hong Kong as a global fund-raising centre.

Conclusions

FSDC is appreciative of the SEHK's effort to cement Hong Kong's role as a leading global listing venue and is positive towards the proposals set out in the Consultation Paper. In view of the surging interest across the globe, introducing SPACs is believed to be valuable to the city's investment ecosystem and capital market.

At the same time, the FSDC believes the SPAC regime should be regularly reviewed for its efficiency and competitiveness relating to global market developments, with a view to enhancing the attractiveness of Hong Kong as an international financial centre.

Financial Services Development Council

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