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6 November 2023

Dear Sirs

Consultation Paper on GEM Listing Reforms

Introduction

1. We refer to the Consultation Paper on GEM Listing Reforms (the "**Consultation Paper**") published by HKEX on 26 September 2023. Unless otherwise defined, terms used in this letter shall have the meaning ascribed to them in the Consultation Paper.
2. We welcome HKEX's initiative to increase GEM's attractiveness to small and/or medium sized enterprises. HKEX's proposals are encouraging, and we are in supportive of the proposals. Set out below are our specific comments.

New alternative eligibility test for companies in the high-growth segment (Question 2)

3. HKEX has proposed to introduce a new alternative eligibility test (alongside with the current cashflow test) that targets high growth enterprises that are heavily engaged in research and development activities.
4. In relation to the proposed minimum market capitalisation, in light of the recent depressed valuations experienced in the Hong Kong market (and around the world), we are wondering whether such level of market capitalisation may screen out some companies which are able to meet all other criteria except for the market capitalisation. However, we understand that there needs to be a meaningful distinction from the current minimum

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market capitalisation requirement under the existing rule. Would an amount between (and including) HK\$200 million and HK\$225 million be considered more desirable as it can cater for a wider group of potential listing applicants, whilst represents a meaningful difference from the HK\$150 million requirement.

Reduction in the lock-up period (Question 3)

5. We note that HKEX has proposed to align the lockup period to the lockup period that applies to the controlling shareholder of a "commercial company" under Chapter 18C of the Main Board Listing Rules. We are supportive of such alignment, and this appears to be consistent with the approach adopted by HKEX in other parts of your proposal.
6. We welcome the HKEX's further consultation/guidance on any free float requirement that may be suitable for GEM listings. It is understood that the free float requirement was introduced under Main Board Listing Rules Chapter 18C as it may be difficult to value special technology companies (especially those that are pre-commercial), hence ensuring a minimum amount of free float will aid price discovery and mitigate market manipulation. In view that some of the concerns for listing of special technology companies under Main Board Listing Rules Chapter 18C do not exist for listings on GEM, any potential additional free float requirement for GEM listings should be carefully considered.

Compliance officer (Question 6)

7. As the board (and each director) of a listed company has the responsibility to ensure the listed company complies with applicable laws, regulations and listing rules, we agree that it may not be necessary to appoint a director to take the role as the compliance officer. Removing the special role of a compliance officer does not affect or reduce the responsibility of the board (and each director) in this regard. We therefore welcome the proposal to align this aspect of the GEM Listing Rules with the Main Board Listing Rules.

Compliance adviser (Question 7)

8. On this aspect, it may be desirable to retain the existing 2 years requirement. Commonly, due to costs concern and resource constraints, GEM listed issuers may be less willing to engage external advisers to assist the board and the company in the compliance with listing rules. Such concern is less for Main Board listed issuers. We feel that having a mandatory "2 year" requirement for the appointment of the compliance adviser¹ would help GEM listed issuers to get familiar with the listing rules and enhance internal control mindset. This is also closer to a similar 3-year requirement for a BSE listed issuer.

Quarterly reporting requirement (Question 9)

9. As a general point, we feel that a higher level of transparency will help to increase investor confidence. However, we also consider this aspect of the requirement should align with the requirement on the Main Board as there are companies on the Main Board who could, in our view, benefit from enhanced transparency or more regular financial information disclosures. Given that this consideration is not unique to GEM listed

¹ Until the publication of financial results for the second full financial year commencing after the date of initial listing.

issuers, we agree that there should be equal treatment between Main Board and GEM in this regard. Given the proposed removal of the quarterly reporting requirement, we think GEM listed issuers will benefit from the longer appointment of the compliance adviser (see paragraph 8 above) in terms of compliance with, for example, inside information disclosure requirements and profit warning/alert disclosure requirements.

Streamlined transfer mechanism (Questions 11 – 14)

10. We are supportive of the proposals on the streamlined transfer mechanism and agree that this will enhance the attractiveness for issuers to pursue a new listing on GEM. We agree that the requirement of "no change in principal business or ownership" will mitigate some of the concerns over packaging of businesses or material acquisitions of businesses within a relatively short period of time prior to a transfer application.
11. We would welcome more guidance or clarification from the HKEX on what would constitute a fundamental change in principal business during the track record period. For example, if the listed issuer has undertaken a very substantial acquisition/disposal at some point during the track record period, or the listed issuer has undertaken major acquisitions/disposals over the track record period which, on an aggregated basis, would constitute a very substantial acquisition/disposal, or the HKEX prefers to adopt a principle-based approach in determining whether or not there has been a fundamental change in principal business. If a principle-based approach is preferred, the HKEX would need to consider the reference point in time to determine what is the principal business of the listed issuer. We believe that the reference point in time should be at the beginning of the 3-year track record period, instead of dated back to the time of the initial listing of the issuer on GEM. This is because businesses of a company evolve over time (especially in the tech sector) and it should not trace back to the time of the initial listing of the listed issuer to determine what is its principal business, especially when the initial listing was undertaken a few years ago.
12. As for the track record period requirement, a 2-year requirement (which is closer to the track record period requirements on some of the Selected Overseas Junior Markets) may be more attractive for future issuers considering a GEM listing. Considering the speed of growth in the businesses of companies in this day and age, an operation record of two full financial years after its initial GEM listing could see a company grows substantially and qualifying itself for meeting the Main Board listing requirements. A 2-year pre-listing track record, and a 2-year post-listing track record will mean that the company would have at least a track record of four full financial years before being qualified to apply for the transfer to the Main Board. This is already longer than the 3-year track record period requirement for a Main Board listing. In addition, the financial and market capitalisation thresholds under the Main Board listing requirements would mean that only companies that meet the Main Board thresholds would be qualified for the transfer. The ownership continuity requirement could also track the same 2-year period.
13. Regarding the proposed GEM Listing Rule 9B.01, we welcome HKEX's clarification on whether it is acceptable that a GEM transfer applicant satisfies any of the three eligibility requirements under Main Board Listing Rule 8.05(1) to (3).
14. In terms of the proposals to remove the requirements for sponsor due diligence and prospectus-standard listing document, we understand the rationale for implementing

these changes. On the other hand, we also note that many GEM listed issuers have had a long history of operation since its initial listing on GEM and the sponsor due diligence carried out at the listing stage would have long become stale. Should there be a distinction in the requirements for GEM listed issuers pursuing a transfer within a certain period of time after its initial listing (such as 5 full financial years) and hence qualifying for the streamlined process, and those pursuing a transfer within a longer period of time after its initial listing (such as more than 5 full financial years) and requiring the sponsor due diligence and prospectus-standard listing document, unless it is demonstrated to the satisfaction of HKEX that the principal business of the transfer applicant has not been subject to a fundamental change since its initial listing.



Clifford Chance