

From:
Sent: 10, September, 2016 6:33 PM
To: Listing Regulation
Subject: Consultation Paper on Proposed Enhancements to the Exchange's Decision-Making and Governance Structure for Listing Regulation
Attachments: Submission.docx
Importance: High

Submission by Lawrence J. Lau

10 September 2016

Ladies and Gentlemen:

In response to the consultation underway on possible reforms of the listing procedures and requirements on the Stock Exchange of Hong Kong Limited (HKEx), I would like to submit the following comments and suggestions:

One of the proposals being considered is the establishment of two new committees to advise on the listing of new enterprises: a listing policy committee and a listing regulatory committee, in addition to the existing listing committee of the HKEx. While this structure may seem cumbersome, it is, in my opinion quite necessary. First, the listing policy committee will be able to consider such issues as “super-voting rights” and “secondary listing of shares already listed elsewhere as Hong Kong Depositary Receipts (HDRs)” on a generic level, that is, without reference to particular enterprises and to design appropriate regulations and procedures. Second, the listing regulatory committee will be able to consider the suitability of an enterprise to be listed, presumably after the existing listing committee of the HKEx has given its tentative approval. This double vetting makes sense because it is important for all investors, large and small, to be protected. The Securities and Futures Commission has the ultimate responsibility for the protection of investors whereas the HKEx, as a publicly listed profit-making enterprise, has its primary objective the maximization of shareholder value. This poses an inherent potential conflict of interest on the part of the listing committee of the HKEx. An analogy may make this clear: neither an association of drug companies, nor an association of pharmacy owners and managers, even an association of pharmacists, cannot substitute for the Food and Drug Administration in the process of approval of new drugs. The Securities and Futures Commission (SFC), the regulator, cannot and should not allow the HKEx to be the sole arbiter of the listing decisions. A joint listing regulatory committee composed of appointees of both the SFC and HKEx will be able to enhance and protect the reputation of Hong Kong as an efficient and fair securities marketplace.

I also have specific comments on “super voting rights” and “secondary listing” respectively.

First, on “super-voting rights”. In 2014, the Hong Kong Stock Exchange lost the IPO of Alibaba, the largest global IPO ever, because it would not allow any shareholder for any new enterprise to be listed in Hong Kong to have “super voting rights”. However, many prosperous private Mainland enterprises are still run by their relatively young founder-owners, and quite a few of them may wish to continue to control and manage them even after their IPOs. In fact, potential investors may also prefer that these founder-owners continue to hold their stakes and remain in charge after IPO. Hong Kong cannot afford to lose all of these potential listings to other stock exchanges. One possible way forward is to grant “super-voting rights” to the “controlling shareholder” and at the same time impose additional obligations on him or her in return, such as an absolute non-transferability of the “super-voting rights”, and a required prior public notification of any sale of such shares (or constructive sale of such sales via derivative or other means) by the controlling shareholder for a certain fixed period, say between three and six months, so as to allow the other shareholders an opportunity to exit first if they choose to do so. This should provide adequate protection for the other shareholders. Then with the full pre-IPO disclosure of the super-voting rights and the additional obligations of the “controlling shareholder”, as long as the investors are still willing to buy the shares at the IPO, the “super-voting rights” should not be considered unfair and the IPO should be allowed to proceed.

Second, on “secondary listing”. It is proposed that there be a clear division of labor with respect to the functions of regulation and supervision of these dually listed enterprises between the regulatory and supervisory agencies of the

country/region of the primary listing and the regulatory and supervisory agency for the stock market in Hong Kong. The basic principle is that one should rely on the home country or region regulator and supervisor exclusively when it pertains to the operations of the enterprise, such as compliance with the applicable local laws and regulations on the accuracy and timeliness of the financial information and required disclosures, the protection of shareholders' rights, especially those of minority shareholders, corporate governance, monitoring and enforcement against trading abuses such as front-running, insider trading and market manipulation in the home market. (If there are doubts that the home country or region regulator and supervisor has the ability to do so, the secondary listing should not be considered at all.) And one should rely on the regulator and supervisor of the Hong Kong market to maintain a fair and open environment for the trading of the depositary receipts, monitor market behavior and enforce against misbehavior such as front running, insider trading and market manipulation. This should greatly simplify the secondary listing process and the ensuing regulation and supervision.

Thank you for your consideration. Also attached is a word version of the submission. I can be contacted at the address below if there is any question.

Sincerely yours,

Lawrence J. Lau
Ralph and Claire Landau Professor of Economics
Lau Chor Tak Institute of Global Economics and Finance
The Chinese University of Hong Kong