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27 October 2016

Dear Sirs

**Re: Consultation Paper on Proposed Enhancements to The Stock Exchange of Hong Kong Limited's Decision-Making and Governance Structure for Listing Regulation**

We welcome the opportunity to respond to your consultation on the listing regulation.

We support initiatives to develop the quality of and the public trust in the capital market. Given the importance of an efficient and effective listing regulation regime for Hong Kong's role as an international financial centre, we support the overall objectives and direction stated in the Proposals of, inter alia, fostering a closer working relationship between the SFC and HKEX, strengthening policy development, streamlining IPO vetting process, more collective engagement and formalising accountability for decision-making.

In achieving these goals, we consider there should be a balance between public interest, investor protection and ensuring Hong Kong's market competitiveness as an international financial centre. The existing listing regulatory regime, of which the Listing Committee is a distinguishing feature, has served Hong Kong well and therefore we note that the stated objectives may be achievable, in part, by developing and strengthening parts of the existing model. However, we recognize there is merit in new structures and forums to facilitate the delivery of the proposed enhancements. We also note the practical challenge of ensuring

in practice that efficiency is achieved, and seen to be achieved, whilst establishing two new Exchange committees (the Listing Policy Committee and the Listing Regulatory Committee).

We set out below for your consideration our comments and suggestions which are intended to be constructive and to facilitate further development or consideration of the proposals where appropriate. We have focused on how and whether the specific proposed enhancement measures would achieve their intended purposes and making suggestions for their effective implementation and possible variations to consider.

Unless otherwise defined, terms used herein shall have the same meanings as those defined in the consultation paper.

#### **A. Listing Policy Committee and policy development**

We support the proposal of establishing a Listing Policy Committee (LPC) to steer HKEX's work on Listing Rule amendments and overall listing policy which is intended to simplify and more closely align policy decision-making amongst the Listing Department (LD), the Listing Committee (LC) and the SFC and thus achieving a more efficient and more responsive system in dealing with policy issues as they arise.

We agree there is a need for a more holistic, comprehensive and integrated approach to policy development and for a structured forum to facilitate HKEX and SFC discussions and communication on policy.

We would like to provide some constructive comments on the composition of the LPC, the role of the LC and the terms of reference of the LPC.

##### ***Composition of the LPC***

While we consider a separate committee which focuses on policy formulation (i.e. apart from the oversight function of listing applications and other listed issuer matters) would serve to improve on efficiency and responsiveness of policy making, we question whether the proposed composition of the LPC could result in a significant reduction in market participation. Under the Proposals, the LPC is equally represented by four SFC officials and four members from HKEX. Of these eight LPC members, only three are market participants (being the Chairperson and two Deputy Chairpersons of the LC).

We highlight the significant reduction in market participation as compared with the existing structure, where policy matters are discussed and decided amongst 28 LC members who are experienced market practitioners with business knowledge and market insights, including senior partners from law firms and accounting firms, leading investment banks and corporate financial advisers and representatives from reputable listed issuers.

Insights from market practitioners with the latest market information and hands-on experience are important to policy formulation and regulatory decision making, especially in the current rapid changing and complex capital markets and in maintaining Hong Kong's leading role as an international financial centre.

Accordingly, we suggest that consideration be given to expanding the membership of LPC to include more market practitioners in addition to the four representatives from each of the SFC and HKEX under the Proposals. The additional LPC members could be nominated from within or outside the LC and should possess the highest standard of integrity and a sound knowledge of their respective areas of professional expertise. We believe a broad representation in the membership of the LPC would ensure that there are balanced views and perspectives in the formulation of the Listing Rules and other policy matters. This may also help retain the pool of talents within the LC and quality input from the LC members.

#### ***Role of the LC***

Under the Proposals, policy matters will first be put forward to the LC for '*non-binding views*' only before they are presented to the LPC for considerations or final decisions. There are different interpretations of what '*non-binding*' means, one of which is that the LC will lose influence and authority. Further explanation of this term is needed to clarify this.

We consider it important that the LC continues to play an important role on policy development and market practitioners' viewpoints are considered. The proposed arrangements need to ensure the views of the LC are being adequately considered, that there is a retained interest in the LC members in rendering their views on policy matters and, in the longer term, a retained interest in LC membership for market participants who are senior stewards in their respective areas of expertise.

#### ***Terms of reference of the LPC***

There are market concerns that the LPC will be predominately regulatory driven and this may be potentially at the risk of market innovation, leaving little scope for flexibility and adaptability to a rapidly changing market and leading to a risk of deterioration in Hong Kong's competitive edge. For this reason, we recommend the terms of reference of the LPC include specific reference to a market development objective to develop the capital market and Hong Kong's competitiveness as an international financial centre. Indeed, it may be considered to re-name the proposed LPC as the '*Listing Policy and Market Development Committee*'.

## **B. Composition and procedures of the Listing Regulatory Committee**

We agree with the importance of suitability concerns to the overall quality of the market and that there are individual cases that can give rise to much broader implications for policy and the overall market. Accordingly, it is important that these two areas have specific additional and formal focus by the SFC and HKEX which is structured, consistent and timely. Earlier consideration of such matters by the ultimate regulatory decision-makers and *'having the right people in the right room at the right time'* are important factors to enhancing the effectiveness of the framework.

Under the Proposals, the LD will be responsible for deciding whether a listing matter (IPO or post-IPO) has suitability concerns or broader policy implications (LRC matter) and, if so, will refer it to the Listing Regulatory Committee (LRC) for decision. The LRC will comprise three representatives of the SFC and the Chairperson and two Deputy Chairpersons of the LC.

The LRC is intended to enable the SFC to have earlier and more direct input on listing matters and to collaborate with HKEX on decision making, which will make the overall process more efficient and we agree with this direction.

We stress the importance of ensuring this intended efficiency is defined, measured, tracked and communicated in a transparent manner.

We also suggest that an important matter to consider is whether and how to give listing applicants and listed issuers the facility to raise direct with the LRC, issues relating to suitability, compliance, policy, or other listing matters.

### ***Composition of the LRC***

As with the composition of the LPC, the proposed composition of the LRC may result in a loss of market insights from senior market practitioners and that decisions on important listing matters will be made by a committee with significantly fewer members as compared with the existing regime. In addition, a practical factor is that since the Chairperson and two Deputy Chairpersons of the LC are all market participants, they may be conflicted in a number of cases that are brought to the LRC for decision.

Therefore, if the proposal on the formation of the LRC is to be successfully implemented, we recommend consideration be given to expanding its membership to include more market practitioners in addition to the three representatives from each of the SFC and HKEX under the Proposals, or to ensure by other means such market perspective is sufficiently considered.

As an alternative or additional concept to the formation of a separate committee (i.e. the LRC), SFC representatives may be introduced onto the LC who will have direct participation in the LC discussion on listing matters with suitability concerns or broader policy listing implications and decisions can only be reached by the LC with the agreement of the SFC representatives. This would enable the SFC to have direct and early input on listing matters and should enhance the collaboration amongst the SFC, LD and LC on decision-making.

#### ***Criteria used to determine a LRC case***

Notwithstanding the Exchange published guidance on application of eligibility and suitability requirements for new listings and post-listing matters, the view on suitability or broader policy implications can be highly judgmental and in many cases is 'facts and circumstances' driven. With this background, we note the need for more clear guidance within the Proposals on the criteria to be used by the LD in determining what constitutes a LRC case and therefore be brought forward to the LRC for vetting and approval.

The early resolution of clarity as to which cases will be referred to the LRC for consideration is key to not jeopardize the intended objective to improve the efficiency of the decision making process within HKEX. For example, in the absence of clarity, the LD may take a cautious approach in deciding which cases are referred to the LRC for determination which would result in a larger number of LRC cases than that envisaged under the Proposals.

We acknowledge the intention that pre-IPO enquiries under the Proposals should reduce the level of uncertainty to some extent as they provide an opportunity for prospective listing applicants to seek informal and confidential guidance on suitability for listing. The guidance on any pre-IPO enquiry is preliminary and is provided by the LD based on information provided by the listing applicant and/or its sponsor(s), which may or may not be inclusive of all relevant factors. Therefore pre-IPO enquiries and similarly for listed issuers, consultations with the LD on post-listing matters, cannot be used as substitutes or surrogates for a clear set of criteria on the determination of LRC matters. Also, the extent of and possible over reliance on pre-IPO enquiries could hinder the efficiency of the vetting process.

In light of the concerns above, we suggest that the criteria used in determining a LRC case be clarified in detail with, inter alia, reference to the existing guidance letters on suitability.

### ***Clarity and efficiency of the IPO vetting process***

Under the Proposals, the views of the LC will be made known to the applicant and its sponsor(s) and any representations made by them in response to the LC's comments will be considered by the LRC before it makes the decision on the case. It is currently unclear from the Proposals under what circumstances the applicant and/or its sponsor(s) are required to address the LC comments, the time allowed in responding to the LC comments and how the responses will be disseminated to the LRC. While the Proposals state the LRC hearing for each LRC IPO case will be held as soon as practicable following the relevant LC hearing, reasonable time must be allowed if the LC comments are to be addressed by the applicant and/or its sponsor(s) and there is the risk this could result in a longer process than under the existing regime.

Also it is proposed that the SFC will no longer as a matter of routine, issue a separate set of comments on new applications. The 'dual-filing' system has been put in place for many years and is considered by many to be working well in practice. It is currently unclear from the Proposals as to how the SFC will participate in the vetting process as established under the dual-filing system and accordingly whether or when the SFC will issue a separate set of comments during the listing process. We support the move to just one set of comments and a commitment and delivery to this in practice would be a very visible indicator of a more efficient process.

In respect of GEM listings, we note that in practice GEM applicants are more likely to be the subject of suitability issues with reference to HKEX's latest guidance letter on IPO vetting and suitability for listing (HKEx-GL68-13A). The Proposals are silent as to whether the approval of a GEM listing will continue to be delegated by the LC to the LD and if so, the role of the LC (or the LRC) as regards the monitoring, review and appeal responsibilities for GEM listings.

We suggest that, for the proposals to be successfully implemented, the listing process including the SFC's involvement under the dual-filing system be clearly clarified and communicated. Also, there should be clarification as to the vetting process for GEM listings under the proposed new arrangements.

In addition, while we support the objective of improving the efficiency of the IPO vetting process, it would be helpful if further clarity can be provided as regards how the proposed enhancements will improve efficiency of the listing process in practice and the transparency and measurement thereof.

### **C. Reviews of listing decisions**

We agree with the need for a robust, structured and timely process for the review of listing decisions particularly those with policy developments or market development consequences.

The Proposals state the LRC will be the review body for decisions made by the LC and the Listing Regulatory (Review) Committee (LRRC) will be formed as the final review body. It is noted that the LRRC shall consist of the Chairperson of the SFC, the Chief Executive Office of the SFC, a Non-Executive Director of the SFC and three individuals who have formerly served on the LC and as nominated by the Listing Nominating Committee.

As three out of six members of the LRRC are more senior officials of the SFC, a question to address is to how the SFC members of the LRRC will, and be seen to, maintain their independence with respect to the original decision made by the LRC as these senior SFC officials would also be seen as responsible to oversee and supervise the work of the SFC representatives in the LRC.

As the need for the LRRC is largely dependent upon the proposed formation and composition of the LRC, we suggest that our comment on the composition of the LRRC be considered taking into account the final proposal as regards the LRC and its membership.

### **D. Oversight of the listing function**

We support the objective to establish clearer accountability for oversight of the listing function. Under the current model, the role of the LC in overseeing the LD is currently seen to be relatively limited in practice and in substance.

Under the Proposals, the LPC will replace the LC as the body responsible for oversight of the listing function and the LD's performance within HKEX. The LD will report to the LPC on its work and the LPC will have primary responsibility for appraising senior executives of the LD and HKEX's Remuneration Committee will take into account the assessment of the LPC when determining the compensation of the LD and its senior executives.

The proposals could give rise to practical corporate governance and/or internal control challenges within HKEX whereby its employees (i.e. LD executives) are evaluated by an external organisation body (i.e. the LPC). Also the potential effect of such a change on recruitment and retention of senior personnel in the LD would need consideration.

We consider the objective can also be achieved through alternative models. Considering the heavy involvement of the LC in the review process and the high degree of interaction between the LD and LC, either HKEX could retain the primary responsibility for appraising and assessing



the performance of senior executives of the LD with criteria established jointly by the LPC and the LC, or a '*balanced scorecard*' or '*two-pen*' approach be adopted whereby both HKEX and LPC give structured and formal input on performance.

If you have any questions relating to these comments or require further information please do not hesitate to contact

Yours faithfully