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Securities and Futures Commission
The Stock Exchange of Hong Kong Limited

15 November 2016

Dear Sirs,

SFC and SEHK Joint consultation on listing regulation – June 2016

I have read with considerable interest the recent joint consultation paper and wish to provide my input.

I lived in Hong Kong for almost 22 years to March 2016, and for many years during that period was involved in the listing regime and the policy challenges arising. In particular, from August 1998 to Sept 2005 I was an executive in the Corporate Finance Division of the SFC, working on the demutualisation and merger of the exchanges and clearing houses and the listing of HKEx in 2000, the legal and regulatory framework introduced at that time and supplemented by the SFO in 2003 including for the SFC's on-going regulatory supervision of the SEHK Listing Division, the introduction of the dual filing regime, and the handling of conflicts of interest concerning HKEx. Later, for a period of 10 months in 2014-15 I was employed by HKEx as an adviser to assist with the establishment of an independent Compliance Department for HKEx, and gained additional insight into the running of the HKEx group.

Quite apart from my direct experience in Hong Kong listing matters, I wish to ensure that Hong Kong maintains and continues to enhance its standing and reputation in financial services matters and retains its position as a premier destination for companies seeking to access the capital markets. In recent years the Global Financial Crisis has adversely affected business confidence and the resulting G20 initiatives since 2009 have had a profound effect on the financial services industry and indirectly impacted the broader commercial landscape, Mainland China has been undergoing huge economic change, and since the summer of 2016 the UK and US have experienced upheaval on the political front. While the scale of the impact of each of these developments separately and collectively for Hong Kong is not yet known, because of the nature of its position in the world the impact will be material and challenge the livelihoods of some of its citizens. During this period, stakeholders of listing matters are more likely to challenge regulatory initiatives that appear to threaten their livelihood and will generally favour continuity. Reform of the Hong Kong regulatory framework for listing matters must keep in tune with positive developments in leading markets overseas and with the Hong Kong market's particular needs, but extra care should be taken to ensure the reform is necessary, well designed and carefully implemented.

Although anyone familiar with Hong Kong would readily acknowledge that Hong Kong has from time to time faced very material local challenges - including SARS,

air pollution, real estate inflation, and the response to the democratic aspirations of its people - the three-tier regulatory structure for Hong Kong's securities and futures markets, with its well defined roles for FSTB, SFC and SEHK, has stood the test of time and generally served Hong Kong well. Along the way, the detail of the regulatory arrangements for listing matters specifically has been debated regularly by stakeholders and periodically scrutinised by independent experts, and incremental improvements have been made. The current structure - a blend of statutory provisions in primary and secondary legislation¹, the non-statutory SFC Code of Conduct governing the conduct of listing sponsors, SEHK Listing Rules and Guidance Letters, and contractual arrangements between SFC and SEHK² - adheres to the philosophy of the three-tier regulatory structure, and the respective roles and responsibilities of SFC and SEHK are clear.

It is with this context in mind that I have read the Joint Consultation Paper and noted the request that the Proposals be considered as a package. Like many of the predecessor changes introduced since 1989 the Proposals are incremental and no doubt a genuine compromise reached after much debate between the SFC and SEHK. The generally co-operative and mutually respectful relationship between SFC and HKEx, underpinned by the healthy tension inherent in a regulatory relationship, has ensured order and continuity and a regulatory framework that responds to market developments.

Notwithstanding that this is a joint consultation and results in arrangements that are a compromise, I am uncomfortable with some aspects of the Proposals. I believe the following elements present challenges for both SEHK and the SFC and will undermine the effectiveness of the current regime:

- It is not desirable for officers of the SFC to sit on SEHK Committees, because it produces a corporate law challenge for SEHK's board directors. The deadlocked nature of the Committee, and the presence of regulators, will each challenge and compromise their common law responsibility and accountability for supervising and managing SEHK.
- The deadlocked committee structure and presence of regulators may also be a corporate law challenge for the SFC officers concerned if they are deemed to be shadow directors of SEHK.
- These arrangements also produce a regulatory challenge for the SFC officers and SFC more generally because their presence on an SEHK committee will either compromise or be perceived to compromise the exercise of SFC powers and responsibilities and discharge the SFC's statutory functions³.

¹ Provisions such as the SFC's powers to propose statutory listing rules for negative vetting by LegCo, vet and approve changes to SEHK Listing Rules and with the approval of the Financial Secretary to mandate new SEHK Listing Rules, review listing applications and object to listings, and to investigate wrong-doing and bring enforcement proceedings.

² Agreements in the form of memoranda of understanding relating to listing matters.

³ The HKEx Risk Management Committee presents very similar challenges, but that Committee is provided for in primary legislation and this may perhaps moderate these effects to some extent.

- Elements of the Proposals obscure the traditional respective roles and responsibilities of the SFC and SEHK in the three-tier regulatory framework.
- Elements of the Proposals weaken, render redundant or potentially conflict with provisions of primary and secondary legislation, may be ultra vires for the SFC, and may increase the ability of parties to challenge SFC decisions.
- Although it is proposed to enhance the accountability of the individuals responsible for listing matters, and the Proposals are an improvement over the current arrangements, they do not achieve this definitively because in law ultimate responsibility for listing matters will rest with the board of SEHK and in practice will be delegated to the maximum extent possible to the Listing Committee, LRC and LPC which are proposed to have different responsibilities, non-static membership, and will include SEHK's regulators.
- Consulting the Listing Committee prior to the reference of any matter to the LPC and LRC, will materially increase the administrative burden borne by the Listing Division.
- In some rare cases a novel policy matter relating to an existing issuer may require a reference first to the LRC and then the LPC.
- The staff of the Listing Division will make fewer decisions themselves, will consult more with the SFC Corporate Finance Division, and may decide to refer more to the LRC or the LPC.

Although the Proposals aim to tackle some of the perceived weaknesses of the current listing regime, in practice they introduce new challenges that create uncertainty, muddle SFC and SEHK responsibilities, and undermine the overall effectiveness and credibility of the current regulatory framework. There are merits in seeking to bring about positive change by agreement with HKEx, but not at the expense of introducing arrangements that do not sit comfortably within the law. The SFC has at its disposal a selection of statutory and non-statutory powers and authorities and should be more ready to use these in a way that is in keeping with the current regulatory framework. If this is impractical, and the need for reform is great, the SFC should propose new primary legislation to adjust the current regulatory framework. Stakeholders that support the status quo cannot have their cake and eat it – with the listing function at SEHK material policy disagreements with the SFC will arise periodically, the SFC will need to consider making use of its formal powers, and these events and developments will be debated in the media, Government and LegCo. That will not always permit cordial relations among stakeholders and may be challenging and uncomfortable for some, but it is the three-tier model working as intended, is clear and well-understood, contains checks and balances, and has withstood and facilitated remarkable change in Hong Kong's securities and futures markets.

Yours faithfully,

William Pearson