

CADWALADER, WICKERSHAM & TAFT LLP

in association with

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BY HAND

4 November 2014

Corporate and Investor Communications Department
Hong Kong Exchanges and Clearing Limited
12/F, One International Finance Centre
1 Harbour View Street
Central
Hong Kong

Dear Sirs,

Re: Concept Paper on Weighted Voting Rights (the “Paper”)

Cadwalader, Wickersham & Taft LLP, in association with Joseph P. C. Lee & Associates (collectively, “**Cadwalader**”) wishes to respond to the questions raised by Hong Kong Exchanges and Clearing Limited (“**HKEx**”) in the Paper.

Cadwalader’s comments are set forth in response to each specific question included in the Paper, and repeated below. Unless otherwise defined, capitalized terms used herein have the meanings given to such terms in the Paper.

Question 1: Should the Exchange in no circumstances allow companies to use WVR structures?

We believe that if the Exchange were to continue to enforce a blanket prohibition on WVR structures, it would place itself in a position of considerable competitive disadvantage to exchanges in other major global financial centers, which we believe is neither useful for the Exchange nor, importantly, necessary for the protection of investors. Rather, we think it more reasonable for the Exchange to develop standards allowing exceptions in certain circumstances, without making WVR structures and analogous corporate governance fixtures universally available to all listed companies.

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While we do not intend to propose a comprehensive list of circumstances in which a listed company should be permitted to enact a WVR or similar structure, we think that companies having large capitalizations, widely-held (pre-Hong Kong initial public offering or with the expectation of such thereafter) equity bases and/or highly liquid shares are obvious choices to be allowed to diverge from one-share-one-vote, as the potential for abuse of any particular investor – single investors being less likely to have equity stakes controlling a significant enough percentage of voting rights to, by themselves, have meaningful voting power – is more limited, and the ability of a dissatisfied investor to exit the investment is improved, in these situations as compared to smaller cap, more closely-held, companies. Further, whatever objective standards might be chosen by the Exchange to enable companies to utilize WVR and similar structures, we believe that the Exchange should also be expressly granted discretion to allow use of these structures in other circumstances where the Listing Committee determines that the issuer's situation makes use of such structures reasonable, without posing undue risk to investors.

Question 2: Should the Exchange permit WVR structures:

- (a) **for all companies, including existing listed companies; or**
- (b) **only for new applicants; or**
- (c) **only for:**
 - (i) **companies from particular industries (e.g. information technology companies), please specify which industries and how we should define such companies;**
 - (ii) **“innovative” companies, please specify how we should define such companies; or**
 - (iii) **companies with other specific pre-determined characteristics (for example, size or history), please specify with reasons; or**
- (d) **only in “exceptional circumstances” as permitted by current Listing Rule 8.11 and, if so, please give examples.**

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In addition to focusing on the size of a prospective listed company and the liquidity of its shares, we think it is reasonable to limit the use of WVR structures to new applicants (as is the case in the United States). An investor that is going to enter an investment with a substantial variance to typical corporate governance principles should be fully informed prior to making an investment decision and, indeed, there is something intuitively objectionable to the disenfranchising of existing equity investors.

While there may, in certain cases, be some validity to the point that companies in particular industry sectors, or in highly technical or innovation-requiring businesses, may be run more efficiently and effectively through the use of WVR or analogous structures (and are therefore deserving of the right to do so), we do not believe that these sectors or businesses lend themselves to objective categorization, and therefore they yield no black-and-white criteria upon which to distinguish listing applicants that should be allowed to put these structures in place from those that should not. Rather, we believe that the relevance of these factors will best be assessed on a case-by-case basis, falling within the range of Listing Committee discretion rather than objective acceptability.

We note that the “exceptional circumstances” concept mentioned in Listing Rule 8.11 has not, to this point, been useful in providing flexibility to balance the Exchange’s concerns and those of prospective listing applicants. Our proposed approach of objective standards supplemented by flexibility and discretion is effectively a complete replacement for Listing Rule 8.11 “exceptional circumstances”.

We suggest that the Exchange consider not just the circumstances in which WVR structures will be permitted, but also those where, once permitted, they may be stripped away. As a starting point, we suggest that the Exchange consider requiring that new listing applicants that are allowed to embed WVR structures or other exceptions to typical corporate governance standards in their articles of association also be required to include provisions that will cause such standards to revert to “normal” if a major corporate governance violation by the Company or its controlling parties has been found by the Exchange, a court, and/or perhaps some type of corporate governance association established by the Exchange for this purpose. In this way, the privilege of an issuer being permitted to avail itself of these measures would be rescinded if a relevant party abused the privilege.

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Question 3: If a listed company has a dual-class share structure with unequal voting rights at general meetings, should the Exchange require any or all of the restrictions on such structures applied in the US, or others in addition or in substitution?

We note that the “sunset” and other restrictions to WVR and similar structures adopted by listed companies in the U.S. utilizing such structures are usually, if not always, put into place at the impetus of the company or its advisors, not the regulators, and principally for marketing reasons. While a company may have solid reasons to concentrate power within a particular group of members of management or investors (and/or may have the financial strength to absorb any type of economic penalty – in the form of lowered share pricing – that the market may apply), such reasons may change or dissipate, and investors may react favourably to there being an end in sight to a company’s atypical corporate governance provisions at the time an initial investment is made. We think that the availability and application of limitations on WVR and similar structures is a positive thing and should be encouraged, but we do not believe that any mandatory application of such limitations needs to be within the Exchange’s purview.

Question 4: Should other WVR structures be permissible, and, if so, which ones and under what circumstances?

We do not believe that the Exchange’s focus should be on structures, as much as on principles. If a company is deemed suitable to use a WVR or analogous structure, pursuant to the standards discussed above, we think that all manner of structures should be acceptable, as long as certain principles are satisfied. For example, we think that WVR and other structures may properly affect voting rights and management power, but not economic rights – we think that each ordinary share of a company’s equity should have the same economic rights as each other ordinary share. Further, we believe that the Exchange should consider whether to limit weighted voting rights to certain matters (e.g. election of directors) or prohibit their extension to others. If the Exchange, in conjunction with any other constituencies it thinks appropriate, can develop a list of essential principles, then in instances where use of a WVR or similar structure is deemed permissible, any structure could be accepted as long as it is fully disclosed, and does not compromise an essential principle.

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Question 5: Do you believe changes to the corporate governance and regulatory framework in Hong Kong are necessary to allow companies to use WVR structures? If so, please specify these changes with reasons.

WVR and analogous structures clearly increase at least the potential for abuse of certain groups of shareholders at the hands of other groups. As a result, if these structures become permissible in Hong Kong, it is important to ensure that shareholders that are potentially exposed to abuse under the structures have adequate means to address any such abuse. As has been expressed by numerous commentators on the issue of protection of corporate investors in Hong Kong, we believe that certain essential changes are merited, particularly class action litigation proceedings and use of contingency fee compensation to legal advisers in securities fraud and corporate derivative proceedings. These changes will need to be comprehensive (in the sense that permitting class actions without permitting lawyers to accept contingency fees will not be effective) and are beyond the scope of this response. We think, however, that if the Exchange decides (as we advocate) to accept the use of WVR and analogous structures, even in limited circumstances, then that decision must be accompanied by other necessary legal and regulatory reform.

Question 6: Do you have any comments or suggestions regarding the additional matters discussed in paragraphs 33 to 47 of the Paper:

- (a) using GEM, a separate board, or a professional board to list companies with WVR structures; and**
- (b) the prospect of overseas companies seeking to list for the first time on the Exchange with a WVR structure or seeking a further primary or secondary listing here?**

We do not consider that it will be useful to accept the use of WVR and analogous structures but limit that use to companies listed on GEM or a newly-created board. We believe that the effect to this would be to cast a de facto taint on such companies, when in fact the intent is precisely the opposite – as envisioned, companies with WVR or similar structures will be only those that merit the use of the structure, in compliance with the articulated standards. Further, as evidenced by history in Hong Kong and elsewhere (GEM, the U.S.’s lower-tier Nasdaq Capital Market, London’s AIM), liquidity invariably suffers by listing on second boards, which does not seem to be the best way to attract listings by companies that are strong

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enough to merit the use of WVR or similar structures through meeting the Exchange's standards for such use.

With respect to overseas (non-HK/China) businesses, we see no basis to distinguish these companies from local companies in the context of primary listings. The ability to use WVR or analogous structures should be subject to the same standards, limitations and principles, regardless of the location of the listed business. However, in the context of secondary listings, we see some basis to grant the Exchange/Listing Committee additional discretion. If a company has a primary listing in an established, highly-regulated market (and perhaps a list of these markets could be promulgated by the Exchange and supplemented from time to time, similar to the concept of "designated offshore securities market" utilized by the U.S. Securities and Exchange Commission pursuant to Regulation S under the U.S. Securities Act of 1933), it may make sense for the Exchange to accept the judgment of that market and its regulators as to the reasonability of use of an atypical corporate governance measure by an issuer, and its fairness to investors.

Question 7: Do you have any other comments or suggestions regarding WVR structures?

We do not believe (and the publication of the Paper by HKEx shows that it is rethinking) that operating without detailed regard for standards of corporate governance for listed companies in other markets is the best approach in this era of financial globalization and increasing competition among the world's most developed financial markets. We think that, in assessing and paving the way for institution of the use of weighted voting right and/or other similar structures, through the promulgation of standards, an emphasis on instituting principles and the development of additional infrastructure to ensure that this new flexibility is not abused, the Exchange should be able to maintain and even advance its core objectives without hampering its global competitiveness and further development as one of the world's preeminent stock exchanges.

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Cadwalader would be happy to discuss any part of this response with HKEx or answer any questions it may have. In the first instance, please feel free to contact [REDACTED] of Cadwalader, Wickersham & Taft LLP or [REDACTED] of Joseph P. C. Lee & Associates.

Yours faithfully,

Cadwalader, Wickersham & Taft LLP
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