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The Hong Kong Institute of Chartered Secretaries

Submission:

Consultation on Review of the Growth Enterprise Market (GEM) and
changes to the GEM and Main Board Listing Rules

16 August 2017

By Email Only: response@hkex.com.hk

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

Dear Sirs,

Re: Consultation on Review of the Growth Enterprise Market (GEM) and changes to the GEM and Main Board Listing Rules

About HKICS

The Hong Kong Institute of Chartered Secretaries (HKICS) is an independent professional institute representing Chartered Secretaries as governance professionals in Hong Kong and Mainland China with over 5,800 members and 3,200 students. HKICS originates from The Institute of Chartered Secretaries and Administrators (ICSA) in the United Kingdom with 9 divisions and over 30,000 members and 10,000 students internationally. It is also a Founder Member of the Corporate Secretaries International Association (CSIA), an international organisation comprising 14 national member organisations to promote good governance globally.

The Consultation

These HKICS submissions to HKEX are in response to HKEX's invitation for comments to the 'Review of the Growth Enterprise Market (GEM) and changes to the GEM and Main Board Listing Rules' (**Consultation Paper**) issued by HKEX in June 2017. In these submissions, capitalised terms used herein shall have the meanings set out under the Consultation Paper, unless the context requires otherwise.

GEM Board Reform Issues

In terms of the reform to the GEM Board, along with related rule changes to the GEM and Main Board Listing Rules over which comments were invited by HKEX under the relevant Consultation Paper, HKICS would focus itself upon the governance aspects relating to the various proposals put forward under the Consultation Paper.

HKICS takes cognisance, as explained under the Consultation Paper that the GEM Board was initially, in 1999, a trade-off between the less stringent admission requirements than the Main Board with enhanced disclosure regime and prominent buyer be aware features under the listing documents to attract 'dot.com' listings. Following the bursting of the 'dot.com' bubble in early 2000, the GEM Board was in a period of doldrums. Subsequently, in July 2008 the GEM Board was reinvented as a stepping stone to the Main Board following alignment of the GEM Listing Rules with the Main Board Listing Rules.

With assertions under the Consultation Paper that there had been limited success for the current purpose of being a stepping stone for GEM Board companies to the Main Board, HKEX now consults the market as to proposals for reform of the GEM Board for the GEM Board to reinvent itself yet again as a stand-alone board for SME companies to raise capital.

For HKICS, without commenting as to the business case relating to whether the GEM Board should or should not remain a stepping stone for a Main Board Listing and/or whether it would or would not be fit for purpose for the GEM board to become a stand-alone platform for SME capital raising platform, HKICS would be approaching the matter from a governance perspective. From the governance perspective, HKICS would support the following reforms proposed under the Consultation Paper on the basis that they are conducive to good governance irrespective of the ultimate positioning of the GEM Board proposed under the Consultation Paper:

1. All GEM Transfer applicants to have (i) published and distributed at least two full financial years of financial statements after their GEM listings; and (ii) not been subject to any disciplinary investigations by the Exchange in relation to a serious breach or potentially serious breach of any Listing Rules for 24 months before they can be considered for a GEM Transfer.
2. The retention of the current track record requirement under the GEM Listing Rules (i.e. two financial years).
3. The retention of the current practice of not requiring a GEM applicant that could meet the Main Board admission requirements to list on the Main Board instead of GEM.
4. The retention of the current Profit Requirement to determine eligibility to list on the Main Board.

5. The increase of the post-IPO lock-up requirement on controlling shareholders from one year to two years for GEM, and where appropriate, the Main Board.
6. The introduction of a mandatory public offering mechanism of at least 10% of the total offer size for all GEM IPOs.
7. The alignment of the GEM Listing Rules on (1) placing to core connected persons, connected clients and existing shareholders, and their respective close associates; and (2) the allocation of offer shares between the public and placing tranches and the clawback mechanism, with the relevant requirements under the Main Board Listing Rules.
8. The unwinding of the Delegate Authority and to return the power to approve or reject GEM listing applications to the Listing Committee.
9. The adoption of measures to enhance an open market for the securities under a mandatory public offering mechanism, in place of the GEM Board's current optional placing-only offering mechanism.
10. The increase of the lock-up requirements for controlling shareholders on the Main Board to align these with the GEM Board requirements.

For the avoidance of doubt, HKICS offers no views as to the following business aspects which should be matters for the comments from other market participants as these measures do not *per se* relate to governance but to the strategic decision of which companies should seek to list on which Exchange board:

1. The increase of the Cashflow Requirement from at least HK\$20 million to at least HK\$30 million;
2. The increase of minimum market capitalisation requirement from HK\$100 million to HK\$150 million for GEM, and from HK\$200 million to HK\$500 million for the Main Board;
3. The corresponding increase of the minimum public float value of a GEM issuer's securities from HK\$30 million to HK\$45 million, and from HK\$50 million to HK\$125 million for a Main Board issuer's securities;
4. The GEM Board delisting procedures;

5. The proposed increase in the minimum market capitalisation requirement of Main Board applicants from HK\$200 million to HK\$500 million; and
6. The corresponding increase in minimum public float from HK\$50 million to HK\$125 million being 25% of the issued share capital of the listed issuer.

Consultation Paper, Review of the Growth Enterprise Market (GEM) and changes to the GEM and Main Board Listing Rules – Questions and Answers

In relation to the specific questions raised under the Consultation Paper, to assist HKEX, we set out our views, from a governance perspective, as follows:

1. **Do you agree with the proposal to re-position GEM as a stand-alone board and hence remove the GEM Streamlined Process for GEM Transfers and re-introduce the requirements to (a) appoint a sponsor to conduct due diligence for GEM Transfers; and (b) publish a "prospectus-standard" listing document such that GEM Transfer applications are treated as a new listing application (without requiring the applicant to conduct an offering)?**

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance. Nevertheless, we hope that there would be consistency across the boards as it is not desirable for there to be potential regulatory arbitrage.

2. **Do you agree with the proposal to require all GEM Transfer applicants to have (a) published and distributed at least two full financial years of financial statements after their GEM listings; and (b) not been subject to any disciplinary investigations by the Exchange in relation to a serious breach or potentially serious breach of any Listing Rules for 24 months before they can be considered for a GEM Transfer?**

We agree with the proposal from a governance perspective. These are important disclosures for the investing public to make informed investment decisions.

3. **Do you agree with the proposal to retain the current track record requirement under the GEM Listing Rules (i.e. two financial years)?**

We agree with the proposal from a governance perspective. This is an appropriate track record for investor protection.

- 4. Do you agree with the proposal to retain the current practice of not requiring a GEM applicant that can meet the Main Board admission requirements to list on the Main Board instead of GEM?**

We have no issue with the current requirements.

- 5. Do you agree with the proposal to increase the Cashflow Requirement from at least HK\$20 million to at least HK\$30 million?**

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

- 6. Do you agree with the proposal to increase the minimum market capitalisation requirement at listing from HK\$100 million to HK\$150 million?**

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

- 7. Do you agree with the proposal to increase the post-IPO lock-up requirement such that controlling shareholders of GEM issuers:**

**(a) cannot dispose of any of their equity interest in a GEM issuer within the first year of listing;
and**

(b) cannot dispose of any interest in the subsequent year that would result in them no longer being a controlling shareholder as defined under GEM Listing Rule 1.01?

We agree with the proposal from a governance perspective in terms of the protection to the minority shareholders that would be provided by the proposal. We have Member views that HKEX should consider the commercial issue as to whether a lender, upon exercising power of sale, and/or an underwriter could dispose of the related GEM shares during the lock-up.

8. Do you agree with the proposal to introduce a mandatory public offering mechanism of at least 10% of the total offer size for all GEM IPOs?

We agree with the proposal in terms of the protection to the minority shareholders that would be provided by the proposal with diversification of the shareholder base.

9. Do you agree with the proposals to align the GEM Listing Rules on:

- (a) placing to core connected persons, connected clients and existing shareholders, and their respective close associates with those under Appendix 6 to the Main Board Listing Rules and Guidance Letter HKEX-GL85-16 "Placing to connected clients, and existing shareholders or their close associates, under the Rules"; and
- (b) the allocation of offer shares between the public and placing tranches and the clawback mechanism with those in Practice Note 18 to the Main Board Listing Rules?

We agree with the proposal to align with the Main Board these governance related provisions to increase the level of safeguards to GEM shareholders.

10. Do you agree with the proposal to increase the minimum public float value of securities from HK\$30 million to HK\$45 million?

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

11. Do you agree with using the Profit Requirement to determine eligibility to list on the Main Board? If not, what alternative test should be used? Please give reasons for your views.

We have no issue with the current requirements. Additionally, we have Member views that HKEX could explore developing an additional sustainability test, which could be referenced to indexes like Dow Jones Sustainability Index which measures the company's ESG performances. As Main Board issuers have sizeable market capitalisations and relatively large public float, there should be an indicator that their businesses are sustainable for the long terms value creation for shareholders.

- 12. If you agree to retain the Profit Requirement, do you agree that the current level of profit under the Profit Requirement should remain unchanged?**

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

- 13. Do you agree with the proposal to increase the minimum market capitalization requirement at listing for Main Board applicants from at least HK\$200 million to at least HK\$500 million?**

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

- 14. Do you agree with the proposal to proportionately increase the minimum public float value of securities for Main Board applicants from HK\$50 million to HK\$125 million?**

In line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

- 15. Do you agree with the proposal to increase the post-IPO lock-up requirement such that the controlling shareholders of Main Board issuers:**

- (a) cannot dispose of any of their equity interest in a Main Board issuer within the first year of listing; and**
- (b) cannot dispose of any interest in the subsequent year that would result in them no longer being a controlling shareholder as defined under Main Board Listing Rule 1.01?**

We agree with the proposal in terms of the protection to the minority shareholders that would be provided by the proposal.

- 16. Alternatively, do you believe that it is not appropriate to extend the post-IPO lock-up requirements for Main Board applicants, given that they are less likely to have the characteristics identified in the 2016 Suitability Guidance Letter because of their larger size and our proposal to raise the minimum market capitalisation requirement to HK\$500 million.**

Not applicable.

17. Do you agree that the proposals for the Main Board should be considered independently irrespective of the outcome of the proposals for GEM?

We agree with the two year lock-up which is conducive towards good governance. As to other proposals in line with our general comments, we offer no views as to detailed business issues which do not *per se* affect governance.

Should you have any questions, please feel free to contact Samantha Suen FCIS FCS(PE), Chief Executive, HKICS or Mohan Datwani FCIS FCS(PE), Senior Director, and Head of Technical and Research, HKICS at 2881 6177 or research@hkics.org.hk.

Yours faithfully,

Ivan Tam FCIS FCS

President

The Hong Kong Institute of Chartered Secretaries