

Hong Kong Proposes Changes to Attract Listing of Innovative Companies on the Main Board

Listing of innovative companies with weighted voting rights (WVR) has been the subject of much controversy since the Hong Kong Stock Exchange (“Exchange”) put forward the WVR Concept Paper in August 2014. After two separate rounds of consultation, the Exchange announced its decision to expand the Main Board regime, rather than creating a new board, to allow:

- listing of WVR companies from emerging and innovative sectors, subject to additional disclosure and safeguards;
- listing of pre-profit/pre-revenue companies from biotech industry; and
- secondary listing of overseas companies with “centre of gravity” in Greater China.

To put the proposals into effect, the Exchange is in the process of drafting the proposed amendments to the Main Board Listing Rules (“Listing Rules”) with a view to proceed with the formal consultation on the proposed Rule amendments in the first quarter of 2018.

In this article, we will discuss the Exchange’s various proposals as set out in the Consultation Conclusions to the New Board Concept Paper.

Listing of WVR Companies

The Exchange proposes to facilitate the listing of innovative companies with a WVR structure through a new chapter in the Listing Rules.

PROPOSED LISTING CRITERIA

1. *New applicants* only;
2. Minimum expected *market capitalisation of HK\$10 billion* at the time of listing;
3. Minimum *revenue of HK\$1 billion* in its most recent audited financial year (such requirement will be waived if its expected

market capitalisation reaches HK\$40 billion or above).

4. Having *more than one* of the characteristics of an “**innovative company**”. Instead of a fixed definition, the Exchange proposes to publish a guidance letter on the characteristics of an innovative company, which include:
 - a. its success is demonstrated to be attributable to the application of new technologies/innovations and/or new business model to the company’s core business;
 - b. research and development (R&D) is a significant contributor of expected value and constitutes a major activity and expense;
 - c. its success is demonstrated to be attributable to unique features or intellectual property; and
 - d. it has an outsized market capitalisation/intangible asset value relative to its tangible asset value.
5. *Eligible and suitable* for listing with a WVR structure. The Exchange proposes to publish a guidance letter with factors that will be taken into account when assessing the eligibility and suitability of an applicant a WVR structure, amongst which include:
 - a. Contribution of WVR holders: each WVR holder has been materially responsible for the growth of the business, by way of their skills, knowledge and/or strategic direction where the value of the company is largely attributable or attached to intangible human capital.
 - b. Responsibility of WVR holders: each WVR holder (i) has an active executive role within the business, and contributes to a

material extent to the ongoing growth of the business; and (ii) is or would assume the role of director of the issuer at the time of listing.

- c. External validation: the applicant has received meaningful (being more than just a token investment) third-party funding from sophisticated investors (including financial institutions). Such investors will be required to retain an aggregate 50 per cent of their investment at the time of listing for a period of at least six months post-IPO (subject to exceptions for de-minimis investments by specific investors).

PROPOSED MANDATORY INVESTOR PROTECTION SAFEGUARDS

To address the concerns on investor protection raised in the consultations, the Exchange proposes that applicant with WVR structures must put in place appropriate investor protection safeguards:

1. *The WVR structure restrictions*

a. WVR shares:

- WVR structure must be attached to a specific class (or classes) of shares, and that the rights attached to the WVR shares and ordinary shares must be the same in all respects other than voting rights.
- The voting power attached to WVR shares must be capped at not more than 10 times of the voting power of ordinary shares.
- The proportion of WVR in issue cannot be increased after listing nor can there be further issue of WVR shares (save for pro rata offering to all shareholders).

b. WVR beneficiaries:

- Must be restricted to those who are (and remain as) directors of the company and the WVR attached to such shares will lapse permanently (i) if the beneficiary ceases to be a director; (ii) dies or is incapacitated; or (iii) if the shares are transferred to another person.
- Must hold a minimum equity threshold at IPO to help ensure that their interests are commercially aligned with other

shareholders.

c. Non-WVR shareholders:

- must hold at least 10% of the votes eligible to be cast at general meeting; and
- those holding at least 10% of the voting rights on a one-share one-vote basis must be able to convene a general meeting.

d. Matters to be decided on a one-share one-vote basis:

- material changes to the issuer's constitutional documents, variation of rights attached to any class of shares, the appointment and removal of independent non-executive directors (INEDs), the appointment and removal of auditors and the winding-up of the company.

2. *Enhanced corporate governance*

Establishment of a mandatory corporate governance committee comprised of INEDs; and the engagement of a compliance adviser on a permanent basis.

3. *Constitutional backing*

The Exchange will require the prescribed safeguards to be incorporated in the applicant's constitutional documents.

4. *Enhanced disclosure*

Issuer with WVR structures will be prominently identified through a unique stock code/marker and appropriate warning to be included in its ongoing corporate communications; appropriate warning language and a full description of the issuer's WVR structure, rationale and associated risks to be disclosed in its listing documents.

Listing of Pre-revenue Biotech Companies

The Exchange proposes to facilitate the listing of pre-revenue biotech companies (including, for instance, companies in pharmaceuticals, biotechnology and life sciences; healthcare equipment and supplies; and healthcare technology) through a new chapter in the Listing Rules. The proposed requirements include:

1. minimum expected *market capitalisation of HK\$1.5 billion* at the time of listing,
2. having the features of “**biotech company**” to be set out in the Exchange's guidance letter,

amongst which include:

- a. has at least one product/process/technology which has proceeded beyond the concept stage (for example, having passed Phase I stage in relation to the clinical trial of a drug regulated by relevant drug and safety authorities such as the US Food and Drug Administration, CFDA (China) or EMA (Europe) and has received all the necessary regulatory approvals to proceed to Phase II);
 - b. has a portfolio of durable patents, registered patents and/or patent applications that demonstrates its rights to the new technologies or innovations that form the basis of its listing application; and
 - c. has previously received investment from at least one sophisticated investor (including financial institutions).
3. *enhanced working capital* of up to 125% of the issuer's current requirement over the next 12 months and has been in operation for at least two years prior to listing.
 4. *enhanced disclosures* on (a) the phases of development for its product(s); (b) the potential market of its product(s); (c) details of spending on R&D, patents granted and applied for; and (d) the R&D experience of management, to ensure that investors are fully informed of the business and R&D risks involved.

The New Concessionary Secondary Listing Regime

1. *Target companies*

The Exchange proposes to modify the existing Listing Rules to create a new route to secondary listing for companies with *all* of the following characteristics:

- a. be an innovative company (by reference to the characteristics set out above);
- b. be primary listed on the New York Stock Exchange, NASDAQ or the Main Market of the London Stock Exchange (and belonging to the UK FCA's "Premium Listing" segment), each a "**Qualifying Exchange**";
- c. have a good record of compliance for at least two years on a Qualifying Exchange; and
- d. have an expected market capitalisation at the time of secondary listing in Hong Kong of at least HK\$10 billion. A secondary listing applicant (i) with a WVR structure; and/or (ii) with a "centre of gravity" in Greater China will also be required to have a minimum revenue of HK\$1 billion in its most recent audited financial if it has an expected market capitalisation at the time of secondary listing in Hong Kong of less than HK\$40 billion.

2. Summary of requirements under the new secondary listing route

	COMPANIES WITH A CENTRE OF GRAVITY IN GREATER CHINA AND LISTED ON QUALIFYING EXCHANGE <i>ON OR BEFORE</i> 15 DEC 2017	COMPANIES WITH A CENTRE OF GRAVITY IN GREATER CHINA AND LISTED ON QUALIFYING EXCHANGE <i>AFTER</i> 15 DEC 2017	COMPANIES LISTED ON QUALIFYING EXCHANGE, WITH CENTRE OF GRAVITY NOT IN GREATER CHINA
<i>Automatic waivers from full compliance with Listing Rules (details to be codified in the Listing Rules)</i>	Apply <i>but</i> will cease to apply if 55% of the total trading volume in the shares migrates to Hong Kong in the most recent fiscal year, in which case the companies would be treated as having a dual-primary listing in Hong Kong		Apply
<i>Shareholder protection standards (to be codified in the Listing Rules)</i>	<i>No need</i> to amend constitutional documents <i>but</i> need to comply with the standards to set out in the Listing Rules	<i>Need to amend</i> constitutional documents (as necessary) to meet equivalent standards to those of Hong Kong	<i>No need</i> to amend constitutional documents <i>but</i> need to comply with the standards to set out in the Listing Rules
<i>WVR structure (if applicable)</i>	<i>No need</i> to meet WVR safeguards nor change WVR structure to meet Hong Kong primary listing requirements	<i>Must</i> meet WVR safeguards and WVR structure must conform with Hong Kong primary listing requirements	<i>No need</i> to meet WVR safeguards nor change WVR structure to meet Hong Kong primary listing requirements

3. Takeovers Code implication

It is stated in the Exchange's papers that the current thinking of Securities and Futures Commission (SFC) is that the Takeovers Code would not apply to secondary listings of companies which centre of gravity is in Greater China. However, if the bulk of trading moves to Hong Kong and therefore a company is treated as having a dual primary listing in Hong Kong, the Takeovers Code would apply at that point.

Details of the above proposals are set out in the [consultation conclusions](#) released on 15 December 2017, which is available on the HKEX website along with [Frequently Asked Questions](#) about the consultation conclusions.

Contact Us

For enquiries related to this Legal Update, please contact the following persons or your usual contact at our firm.

Jeckle Chiu

Partner

T: +852 2843 2245

E: jeckle.chiu@mayerbrownjism.com

Billy Au

Partner

T: +852 2843 2254

E: billy.au@mayerbrownjism.com

Mayer Brown JSM is part of Mayer Brown, a global legal services organisation advising many of the world's largest companies, including a significant portion of the Fortune 100, FTSE 100, CAC 40, DAX, Hang Seng and Nikkei index companies and more than half of the world's largest banks. Our legal services include banking and finance; corporate and securities; litigation and dispute resolution; antitrust and competition; employment and benefits; environmental; financial services regulatory & enforcement; government and global trade; intellectual property; real estate; tax; restructuring, bankruptcy and insolvency; and wealth management.

OFFICE LOCATIONS AMERICAS: Charlotte, Chicago, Houston, Los Angeles, Mexico City, New York, Palo Alto, San Francisco, Washington DC
ASIA: Bangkok, Beijing, Hanoi, Ho Chi Minh City, Hong Kong, Shanghai, Singapore
EUROPE: Brussels, Düsseldorf, Frankfurt, London, Paris
MIDDLE EAST: Dubai
TAUIL & CHEQUER ADVOGADOS in association with Mayer Brown LLP: São Paulo, Rio de Janeiro

Please visit www.mayerbrownjism.com for comprehensive contact information for all our offices.

This publication provides information and comments on legal issues and developments of interest to our clients and friends. The foregoing is intended to provide a general guide to the subject matter and is not intended to provide legal advice or be a substitute for specific advice concerning individual situations. Readers should seek legal advice before taking any action with respect to the matters discussed herein. Please also read the Mayer Brown JSM legal publications [Disclaimer](#). A list of the partners of Mayer Brown JSM may be inspected on our website www.mayerbrownjism.com or provided to you on request.

Mayer Brown is a global legal services provider comprising legal practices that are separate entities (the "Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP and Mayer Brown Europe-Brussels LLP, both limited liability partnerships established in Illinois USA; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales (authorized and regulated by the Solicitors Regulation Authority and registered in England and Wales number OC 303359); Mayer Brown, a SELAS established in France; Mayer Brown Mexico, S.C., a sociedad civil formed under the laws of the State of Durango, Mexico; Mayer Brown JSM, a Hong Kong partnership and its associated legal practices in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. Mayer Brown Consulting (Singapore) Pte. Ltd and its subsidiary, which are affiliated with Mayer Brown, provide customs and trade advisory and consultancy services, not legal services. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.

© 2017 The Mayer Brown Practices. All rights reserved.