Think Ahead ACCA

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

16 August 2017

Dear Sir

New Board Concept Paper (Concept Paper)

On behalf of ACCA (the Association of Chartered Certified Accountants) Hong Kong, we are pleased to submit the below response to the abovementioned Concept Paper.

Over the past few decades, Hong Kong has successfully established itself as an international financial centre in Asia that offers an efficient and well-regulated capital market to channel capitals from investors to corporates. With the development of technology, the emergence of new economy as well as the fierce competition from other capital markets, Hong Kong listing rules need to be constantly measured up to international standards to secure Hong Kong's long-term future as a pre-eminent IPO centre.

ACCA appreciates and supports the direction of Hong Kong Exchanges and Clearing Limited (HKEX) to attract a more diverse range of companies to list in Hong Kong, in order to address our current issue of market's dominance by financial and property sectors as highlighted in the Concept Paper. However, in order to increase the diversity of our offering to investors as well as attractiveness to issuers, we are of the view that the current Growth Enterprise Market (GEM) and Main Board should be revamped and enhanced instead of a New Board to be created.

Evolving definition of 'New Economy'

It is proposed in the Concept Paper that the New Board is designed for New Economy companies. Yet with technology changing so quickly that the definition of 'New Economy' will be fluid and the 'New Economy' in which the companies seek listing may become old within a short timeframe. While it is not practicable to redefine 'New Economy' from time to time and judgement will be required in determining if the issuer is a 'New Economy' company, the segmentation of the New Board, Main Board and GEM would however become blurred and the purpose of the New Board will be weakened.

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Proposed New Board Premium included into the Main Board by allowing weighted voting rights and non-standard governance structures

The proposed financial eligibility criteria and track record eligibility requirements for New Board Premium are equivalent to those for the Main Board except that weighted voting rights (WVR), which would preclude listing on the Main Board, are permitted in the New Board. We understand that WVR structures have been prevalent in innovative companies from the technology sector which Hong Kong needs to attract and compete globally for listings.

In this regard, we refer to our submission in November 2014 regarding the Concept Paper on Weighted Voting Rights released by HKEX. ACCA was of the view that WVRs should be made available to new applicants for listing on the Main Board on the basis that appropriate investor protection mechanism was introduced. Listing applicants should justify, with supporting evidence, why and how WVR is necessary to benefit the company's long term development and to provide proper disclosures of the details of the WVR structure in the listing documents. Special stock codes could be used to differentiate those shares with WVR such that investors are fully aware that their rights are inferior to those given superior rights. Under the free market mechanism, investors would decide if the WVR structure is beneficial to the company.

While applicants for the proposed New Board Premium have the same financial eligibility criteria and track record eligibility requirements as those for the Main Board apart from governance structure, instead of having a separate segment on the New Board, we counter-propose that this separate segment could be included in the current Main Board, with the addition of differentiated coding for investor trading as well as regulation.

Shareholders protection

We appreciate that a right balance between the needs of business and investor protection should be attained so as to maintain Hong Kong's reputation as an international financial centre. We refer to our submission on the Concept Paper on Weighted Voting Rights and suggest that the means available for investors to take action against companies should be considered. Investor protection could be enhanced by introducing class action, whereby aggrieved minority shareholders shall be provided with less costly tool to initiate a class action lawsuit against companies for violation of listing rules and regulation as a deterrent to poor governance.

Shareholders that are enjoying a privileged right under WVR would certainly assume more rights in the management of the listed entity. It is from this skewed share of management rights where the company shall be subject to more obligations in terms of corporate governance.

For instance, most of the 'Recommended Best Practice' at present in the listing rules could be mandated against WVR companies. WVR companies shall also be subject to a demand of higher ratio of Independent Non-Executive Directors (INEDs) on the board versus the current requirement of not less than 1/3 or 3 INEDs.

Regarding shareholder communications, an independent shareholders committee could be set up whereby its representatives shall be briefed by executive management (largely representing WVR shareholders) twice a year, along with a voluntary disclosure of board decisions by these WVR representative members on the board.

Reinventing GEM by absorbing New Board Pro

GEM has long been criticised for low liquidity and having a series of shell activities. With the proposed introduction of New Board Pro that targets new economy companies with high-growth potential, and by removing the GEM Streamlined Process for GEM Transfers, GEM would become simply a standalone board for small and medium-sized enterprises.

This also implies that GEM would be left for companies of old economy with low-growth rate. Its attractiveness to issuers would be further worsened by the raising of eligibility requirements of listing on GEM. All these changes would remove liquidity and reduce attractiveness of GEM to both issuers and investors.

ACCA agrees that pre-profit companies should not be denied from access to the capital market, provided that they have promising business models that appeal to market investors. Instead of introducing a New Board Pro for these pre-profit companies and limiting market participants to be professional investors, we recommend permitting listing of these pre-profit companies on a specifically designated segment on GEM. Special stock codes can be used to differentiate and highlight those shares of companies without track record or minimum financial criteria, and with WVRs.

We note that it is proposed in the Concept Paper that less onerous standards be applied for this segment and specifically, only a "Financial Adviser" is required instead of a sponsor. In this regard, ACCA considers that the market quality and integrity should be maintained and hence new listing of pre-profit companies on GEM should only be allowed with the appointment of sponsors to ensure the qualification and suitability of these companies. And we agree to the proposal that companies listed on this designated segment of GEM should also comply with the standards applicable to GEM / Main Board listed companies.

To enhance the liquidity of GEM, with the sub-segment for pre-profit companies, the possibility of a market-making mechanism can be explored. We do not see the need to impose any restriction on the types of investors that can participate in this sub-segment, as long as investors make conscious decisions to undertake the risks involved, which could be confirmed through a self-declaration process. In this regard, ACCA strongly encourages investor education be always in place along with investor protection measures.

By attracting target companies to list on the current GEM instead of creating a new board, it would help eliminate the challenge in defining what companies are qualified as 'New Economy' for them to apply to list on the proposed New Board. New initiatives such as implementation of investor protection measures and enhancement of market liquidity should also be in place to improve the attractiveness of GEM to both issuers and investors. Or else, by creating the New Board and removing the GEM Streamlined Process for GEM Transfers and raising the eligibility requirements for listing on GEM, the current GEM board will become less attractive which will not help enhance the sustainable development of Hong Kong's capital market.

Conclusion

ACCA supports the initiatives to improve quality of the Hong Kong capital market and to reinforce Hong Kong's position as an international financial centre and as a world leader in IPO fundraising. While we shall be bold to introduce changes to the corporate governance and the regulatory framework to accommodate the evolving business and economic environment, we should not sacrifice the attractiveness of GEM and complicate the market structure without a promising beneficial outcome. As such, we are of the view that it is more helpful to introduce measures to improve our current Main Board and GEM, making them more competitive, liquid and resilient, in order to capture a greater share of the fastest-growing companies emerging from the new economy.

Should there be any questions, please do not hesitate to contact the undersigned at 2973 1108.

Yours faithfully,

Alice Yip
Chairman
ACCA Hong Kong