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Panel on Financial Affairs

Meeting on 2 March 2020

Background brief on the reforms made to the Main Board and Growth Enterprise Market Listing Rules in 2018 and the Hong Kong Exchanges and Clearing Limited's Three-year Strategic Plan of 2019-2021

Purpose

This paper provides background information on the reforms made to the Main Board and Growth Enterprise Market ("GEM") Listing Rules in 2018, the enhancements to the Hong Kong listing regulatory regime in 2018 and 2019, and the Hong Kong Exchanges and Clearing Limited ("HKEX")'s Three-year Strategic Plan of 2019-2021. It also summaries the major views and concerns raised by Members on issues relating to the subjects since the 2016-2017 session.

Reform on the Growth Enterprise Market

2. The Stock Exchange of Hong Kong Limited ("SEHK")¹ launched GEM in November 1999 to provide emerging companies with a capital formation platform and as an alternative market to the Main Board. In order to encourage the listing of emerging and growth companies, GEM was designed to have less stringent admission requirements than the Main Board. In July 2008, GEM was re-positioned from an alternative board for emerging and growth companies to a "stepping stone" to the Main Board. As a result, most of the original features of GEM were repealed and many of the GEM Listing Rules were amended to align with those of the Main Board. Since then, there have been comments that the revamped GEM requirements have been exploited by some market players, thereby affecting the quality of the

¹ The Stock Exchange of Hong Kong Limited ("SEHK") is a wholly owned subsidiary of the Hong Kong Exchanges and Clearing Limited ("HKEX").

market. Moreover, it is believed that GEM's "stepping stone" positioning has achieved limited success.

3. On 16 June 2017, HKEX published a consultation paper entitled "Review of the Growth Enterprise Market (GEM) and Changes to the GEM and Main Board Listing Rules" ("the GEM Consultation Paper") to seek views from the public on the proposed reform to GEM. The reform proposals focus on four key areas, namely (a) GEM's position as a "stepping stone" to the Main Board; (b) GEM admission requirements and delisting mechanism; (c) the open market requirement; and (d) certain Main Board listing requirements to preserve the Main Board's position as a market for larger companies that can meet Hong Kong's highest market standards.

4. Based on the responses received on the proposals in the public consultation and discussions with the Securities and Futures Commission ("SFC"), SEHK decided to implement substantially all of the proposals in the GEM Consultation Paper.² Listing Rules amendments were made to reflect the new role of GEM as a market for small and mid-sized companies and to ensure that there would be a clear distinction between issuers listed on GEM and the Main Board. The key changes made to the GEM and Main Board Listing Rules, which came into effect on 15 February 2018, are set out in **Appendix I**.

Review of the listing regulatory regime

5. SEHK is the frontline regulator of all listing-related matters and issuers listed on its markets. SEHK's Listing Department is responsible for the day-to-day administration of the Listing Rules, while the Listing Committee ("LC")³ acts an independent review body for decisions made by the Listing Department and formulates the listing policy. On the other hand, SFC performs a lead role in market regulation. SFC has powers to object to the listing of, and to suspend trading in or delist, any securities under the Securities and Futures (Stock Market Listing) Rules (Cap. 571V); to investigate and take enforcement on cases of market misconduct; and to supervise and monitor SEHK's performance of its listing-related functions and responsibilities.

² HKEX published the consultation conclusions on 15 December 2017.

³ The members of the Listing Committee include representatives of investors, listed companies and market practitioners, as well as the Chief Executive of HKEX as an ex officio member.

Consultation and conclusions on the review of The Stock Exchange of Hong Kong Limited's decision-making and governance structure for listing regulation

6. Given that regulatory considerations relating to listing in Hong Kong had become increasingly complex and involved new risks and operational challenge, SFC and HKEX jointly issued a consultation paper entitled "Proposed Enhancements to The Stock Exchange of Hong Kong Limited's Decision-making and Governance Structure for Listing Regulation" ("the Joint Consultation") in June 2016 to seek the market's views on proposed structural and procedural enhancements to a number of areas, including (a) development of listing policy; (b) processing of listing applications; (c) review and publication of listing decisions; and (d) oversight of the listing function.

7. The consultation conclusions were published in September 2017 setting out enhancements to the listing regulatory structure in Hong Kong, including (a) establishing a new Listing Policy Panel ("LPP") as an advisory, consultative and steering body on listing policy with broader regulatory or market implications; (b) increasing SFC's direct involvement in more serious listing matters; (c) continuing SEHK's power in making all decisions under the Listing Rules; and (d) maintaining the role of the LC.

Consultation on review structure in relation to listing committee decisions

8. SEHK conducted a separate consultation on the review structure of LC's decisions and published a consultation paper entitled "Review Structure in relation to Listing Committee Decisions" in August 2018 with proposals to establish a new independent committee to replace the Listing (Review) Committee and Listing Appeals Committee, and to routinely publish decisions of the new committee for non-disciplinary matters.

9. According to the consultation conclusions published in January 2019, the major changes adopted for the review structure of LC's decisions included (a) decisions of material significance⁴ made by LC will be subject to only one level of review, and the Listing Appeals Committee will be

⁴ Decisions of material significance refer to (i) rejection of a new applicant's listing application solely on the ground of unsuitability for listing; (ii) cancellation of listing; and (iii) imposition of certain disciplinary sanctions.

discontinued;⁵ (b) replacing the Listing (Review) Committee and the Listing (Disciplinary Review) Committee by an independent review committee (to be named as Listing Review Committee) for hearing reviews currently conducted by the two committees; (c) decisions of the new Listing Review Committee for non-disciplinary matters will be published routinely; and (d) SFC may request a review of any matter, including a decision of LC by the new Listing Review Committee.

Three-year Strategic Plan of the Hong Kong Exchanges and Clearing Limited for 2019-2021

10. HKEX announced its Strategic Plan 2019-2021 on 28 February 2019, which sets out its vision and strategic objectives for the next three years. The Strategic Plan states that HKEX Group's vision is to be "the Global Markets Leader in the Asian Time Zone – Connecting China, Connecting the World". HKEX's plan to support its vision is summarized in **Appendix II**.

Major views and concerns expressed by the Panel on Financial Affairs

11. The Panel on Financial Affairs ("FA Panel") has not conducted discussion specifically on the proposed reform to GEM. The major views and concerns expressed by members when FA Panel discussed issues relating to the enhancements to the listing regulatory regime at the meetings on 6 February and 18 April 2017 are summarized in the ensuing paragraphs.

12. Regarding the Joint Consultation in 2016, some members stressed the need for SFC to accord priority to dealing with issues concerning public interest, protection of investors and ensuring a level playing field in the securities industry. Some other members considered that SFC should review whether the proposals in the Joint Consultation were ultra vires the Securities and Futures Ordinance (Cap. 571) and they also cautioned that SFC should refrain from interfering with the operation of HKEX.

13. SFC stressed that it would not act beyond its powers. Proposals included in the Joint Consultation had been agreed by the leaderships of SFC and HKEX before publication. The overarching goal of the Joint Consultation was to enhance market quality, efficiency, accountability and

⁵ Originally, decisions of material significance made by the Listing Committee are subject to two levels of review, a first review by the Listing (Review) Committee or the Listing (Disciplinary Review) Committee, as the case may be, and a further and final review by the Listing Appeals Committee.

transparency. SFC would carefully analyse all views received, including those dealing with legal aspects of the proposals. The Administration supplemented that the Joint Consultation had been conducted within the framework of the existing legislation.

14. Some members expressed concern about the proposed creation of the Listing Regulatory Committee ("L(R)C") and the Listing Policy Committee⁶ ("L(P)C") which they believed would make the existing listing regulatory structure cumbersome, pose more hurdles for listing applicants, slow down the approval process of listing applications, and turn the existing disclosure-based regulatory regime into a regulation-based regime.

15. Some other members considered that the proposals in the Joint Consultation could enhance the listing regulatory regime by tackling problems associated with the quality and governance of listed companies, which in turn would strengthen protection for investors and their confidence in the local stock market. Moreover, these members were of the view that the proposed establishment of the L(P)C would provide a joint platform for SFC, SEHK and the stakeholders to discuss important listing policies and tackle listing issues, as well as to promote sustainable development of the market.

16. SFC responded that Hong Kong had never adopted a purely disclosure-based approach and the suitability concept had been in the Listing Rules for a long time. The proposed L(R)C would streamline the vetting and approval process for Initial Public Offering ("IPO") applications that had suitability concerns or broader policy implications as these applications would be decided on by the committee. LC would continue to be the decision-maker of IPO applications and matters involving listed issuers that do not involve suitability concerns or broader policy implications, which should constitute the large majority of cases.

Discussions at Council meetings

Council questions

17. At the Council meeting on 9 November 2016, Hon Mrs Regina IP raised an oral question on the Joint Consultation conducted by SFC and HKEX in 2016. Major issues covered in the oral question included (a) the

⁶ According to the Joint Consultation Conclusions, the proposed Listing Regulatory Committee would not be established and the proposed Listing Policy Committee would be renamed as Listing Policy Panel.

possible violation of the market participant-based regulatory principle by the proposals in the Joint Consultation; and (b) the impact of the implementation of the proposals on the competitiveness of Hong Kong as an international financial centre.

18. At the Council meeting on 23 October 2019, Hon Kenneth LEUNG raised a written question on the integrity of the listing process, including the remedial action that might be taken to deal with the listing of companies whose listing had been found to have been approved improperly.

19. Details of the two Council questions and the Administration's responses are provided in hyperlinks in **Appendix III**.

Council motion

20. At the Council meeting on 30 November 2016, Hon Christopher CHEUNG moved a motion urging the Government to prudently formulate a comprehensive listing policy. The motion, as amended by Hon James TO, was passed. Details of the motion are provided in hyperlinks in **Appendix III**.

Latest development

21. The Administration, SFC and HKEX will brief FA Panel at the meeting on 2 March 2020 on the strategic development of Hong Kong as a premier listing platform and the development of HKEX, including its Three-year Strategic Plan, and the latest position of the changes to the GEM and Main Board Listing Rules implemented since 2018.

Relevant papers

22. A list of relevant papers is in **Appendix III**.

The key changes made to the Growth Enterprise Market ("GEM") and Main Board Listing Rules, which came into effect on 15 February 2018

(a) GEM's position

GEM was re-positioned as a stand-alone board. The streamlined process for GEM Transfers to the Main Board was removed. GEM Transfer applicants are required to appoint a sponsor to conduct due diligence and publish a listing document to list on the Main Board, in addition to meeting the Main Board eligibility requirements;

(b) GEM admission requirements

The GEM admission requirements were enhanced by increasing (i) the cashflow requirement from at least \$20 million to at least \$30 million; (ii) the minimum market capitalization requirement from \$100 million to \$150 million; and (iii) the post Initial Public Offering ("IPO") lock-up requirement on controlling shareholders from one year to two years;

(c) Open market requirements

The open market requirements was enhanced by introducing a mandatory public offering mechanism of at least 10% of the total offer size for all GEM IPOs and increasing the minimum public float value of securities from \$30 million to \$45 million; and

(d) Main Board requirements

Certain requirements of the Main Board have been increased to ensure that there is a clear distinction between issuers listed on GEM and the Main Board, namely (i) an increase in the minimum expected market capitalization of Main Board applicants at the time of listing from \$200 million to \$500 million; and (ii) an increase in the minimum public float value of Main Board companies at the time of listing from \$50 million to \$125 million.

**Three-year Strategic Plan of
the Hong Kong Exchanges and Clearing Limited ("HKEX") for
2019-2021**

(a) China Anchored

Support international portfolio diversification by Mainland investors and facilitate further internationalization of the domestic capital markets through secure, effective and transparent channels across asset classes;

(b) Globally Connected

Attract global liquidity to Hong Kong by providing broader and more effective access to Asia Pacific underlying assets, creating a comprehensive and competitive one-stop shop for China and Asian exposures; and

(c) Technology Empowered

Leverage technology to modernize HKEX's core business and explore new frontiers through strategic partnerships with technology leaders.

To support its strategic objectives, HKEX will also make further investments in talent, capabilities, and developing the right corporate culture, to help drive a more commercial, innovative, and customer-centric approach throughout the organization with a view to boosting HKEX's international competitiveness and making Hong Kong even more relevant as a global financial centre.

Appendix III

List of relevant papers

Date	Event	Papers/Minutes of meeting
17 June 2016	Joint Consultation on Proposed Enhancements to The Stock Exchange of Hong Kong Limited's Decision-Making and Governance Structure for Listing Regulation	Joint Consultation paper Joint Consultation Conclusions
9 November 2016	Hon Regina IP raised an oral question on the consultation on listing regulation	Hansard
30 November 2016	Motion on "Formulating a comprehensive listing policy" moved by Hon Christopher CHEUNG	Hansard Wording of the motion passed Progress report
18 April 2017	Meeting of the Panel on Financial Affairs	Administration's paper (LC Paper No. CB(1)777/16-17(07)) Background brief (LC Paper No. CB(1)777/16-17(08)) Minutes (LC Paper No. CB(1)1344/16-17) Supplementary information provided by the Administration after the meeting (LC Paper No. CB(1)1348/16-17(02))

Date	Event	Papers/Minutes of meeting
16 June 2017	Consultation on Review of the Growth Enterprise Market ("GEM") and Changes to the GEM and Main Board Listing Rules	Consultation paper Consultation Conclusions
10 August 2018	Consultation on Proposed Changes to Review Structure for Listing Committee Decisions	Consultation paper Consultation Conclusions
August 2018	Information paper on Enhancements to the Stock Exchange of Hong Kong Limited's Decision-making and Governance Structure for Listing Regulation	Administration's paper (LC Paper No. CB(1)1406/17-18(01))
August 2018	Information paper on Review of the GEM and Changes to the GEM and Main Board Listing Rules	Administration's paper (LC Paper No. CB(1)1406/17-18(02))
28 February 2019	HKEX Strategic Plan 2019-2021	Press release
23 October 2019	Hon Kenneth LEUNG raised a written question on the integrity of the listing process	Hansard