

# Hong Kong's New Listing Regime for Emerging and Innovative Companies

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The Hong Kong Stock Exchange has amended its Listing Rules to allow listings of biotech companies that do not meet financial eligibility tests, high growth and innovative companies with weighted voting rights structures, and innovative companies listed elsewhere seeking a secondary listing through a concessionary route.

On 24 April 2018, The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) published its Consultation Conclusions on a Listing Regime for Companies from Emerging and Innovative Sectors, introducing three new chapters in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “**Listing Rules**”) with the aim of attracting high growth companies from emerging and innovative sectors to list in Hong Kong, subject to appropriate safeguards. The Listing Rules amendments are supplemented with guidance letters on the suitability for listing of companies applying to be listed under each of these chapters.

## Biotech Companies

The Stock Exchange has introduced a new Chapter 18A of the Listing Rules to allow the listing of biotech companies that do not meet the financial eligibility tests (including companies with no revenue or profit). “Biotech” is defined as the application of science and technology to produce commercial products with a medical or other biological application, and “biotech company” is defined as a company primarily engaged in the research and development (“**R&D**”), application and commercialisation of biotech products. Applicants are required to satisfy the requirements of Chapter 18A in addition to the listing requirements under Chapter 8 of the Listing Rules. They must also demonstrate that they are both eligible and suitable for listing.

## Listing Requirements

### [Suitability for Listing](#)

A biotech company applicant is required to demonstrate the following features:

- having developed at least one core product beyond the concept stage (having met developmental milestones specified for the relevant type of product including pharmaceutical (small molecule drugs), biologics, medical devices and other biotech products. For pharmaceutical and biologics, this would generally mean completing Phase I clinical trials and the competent authority (including US Food and Drug Administration, the China Food and Drug Administration, the European Medicines Agency and other authorities recognised by the Stock Exchange) has no objection for the applicant to commence Phase II (or later) clinical trials;

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- having been primarily engaged in R&D for the purposes of developing its core product(s), and having been engaged with the R&D of its core product(s) for a minimum of 12 months prior to listing;
  - having as its primary reason for listing the raising of finance for R&D to bring its core product(s) to commercialisation;
  - having registered patents, patent applications and/or intellectual property in relation to its core product(s);
  - if the applicant is engaged in the R&D of pharmaceutical (small molecule drugs) products or biologic products, demonstrating that it has a pipeline of those potential products; and
  - having previously received meaningful third party investment from at least one sophisticated investor at least six months before the date of the proposed listing (which must remain at IPO). The Stock Exchange would assess on a case-by-case basis: (a) whether the investor is a sophisticated investor, considering factors such as net assets, assets under management, investment experience, and relevant knowledge and expertise; and (b) what would be considered meaningful investment, with the following being indicative benchmarks: not less than 5% of share capital for a market capitalisation of HK\$1.5 billion to HK\$3 billion, not less than 3% of share capital for a market capitalisation of between HK\$3 billion and HK\$8 billion, and not less than 1% of share capital for a market capitalisation of more than HK\$8 billion.

The above factors are not exhaustive or binding and the Stock Exchange retains the discretion to find the applicant is not suitable for listing even if the above features are satisfied.

### Other Listing Requirements

A biotech applicant is also required to satisfy the following listing requirements:

- having been in operation in its current line of business for at least two financial years prior to listing under substantially the same management;
- having a minimum expected market capitalisation at the time of listing of HK\$1.5 billion; and
- having available working capital to cover at least 125% of the group's costs for at least the next 12 months (after taking into account the proceeds of the listing), which must substantially consist of general, administrative and operating costs, and R&D costs.

### Subscription by Cornerstone Investors and Shareholders

In addition to the usual public float requirements – in general, at least 25% of the total number of issued shares must be held by the public – biotech applicants are subject to an additional requirement to have at least HK\$375 million of its market capitalisation to be held by the public at the time of listing. Shares subscribed by cornerstone investors and shares subscribed by existing shareholders in the IPO will not be considered to be held by the public for the purpose of calculating the HK\$375 million.

### Enhanced Disclosure

Biotech applicants must include prominent warning statements and enhanced risk disclosures in their listing documents, including disclosures on:

- the phases of development for its core product(s);
- material communications with all relevant competent authorities in individual cases) in relation to its core product(s) (unless restricted under applicable requirements);
- all material safety data relating to its core product(s);
- the immediate market opportunity and any potential increased market opportunity of its core product(s);
- its rights and obligations in respect of any in-licensed core products;

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- disclosure of operating costs, including details of R&D spending;
  - patents granted and applied for in relation to its core product(s) (unless the applicant is able to demonstrate that this would require the applicant to disclose highly sensitive commercial information); and
  - the R&D experience of management and measures to retain key management or technical staff.

In addition, they will be required to provide ongoing disclosures regarding their R&D activities in their interim and annual reports.

## Risk Management Measures

A biotech applicant will be subject to the following restrictions and measures after listing until it could demonstrate that it is able to satisfy one of the financial eligibility tests:

- it will be restricted from effecting any transaction that will result in a fundamental change to its principal business without the prior consent of the Stock Exchange;
- where it fails to meet its continuing obligation to maintain sufficient operations or assets, it will be required to re-comply with the requirement within 12 months, failing which the Stock Exchange will cancel its listing; and
- it must be prominently identified through a unique stock marker “B” at the end of their stock name.

## WVR Structures

The Stock Exchange has introduced a new Chapter 8A of the Listing Rules setting out the qualifications for listing of companies with a weighted voting rights (“WVR”) structure and the ongoing safeguards that they must put in place. These requirements apply in addition to the usual listing requirements (including the financial tests). Applicants are required to demonstrate that they are both eligible and suitable for listing with a WVR structure.

## Listing Requirements

### Suitability for Listing

An applicant with a WVR structure would normally be considered suitable for listing in Hong Kong if it is able to demonstrate the following characteristics:

- the applicant must be an innovative company. The Stock Exchange expects the applicant to possess more than one of the following characteristics:
  - its success is demonstrated to be attributable to the application, to the applicant’s core business, of new technologies, innovations and/or a new business model;
  - R&D is a significant contributor of its expected value and constitutes a major activity and expense;
  - its success is demonstrated to be attributable to its unique features or intellectual property; and/or
  - it has an outsized market capitalisation / intangible asset value relative to its tangible asset value.

The Stock Exchange recognises that what is considered “innovative” depends on the state of the industries and markets in which an applicant operates, and will change over time. It will therefore review the facts and circumstances of each case to determine if an applicant has demonstrated that it is an innovative company;

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- the applicant must demonstrate a track record of high business growth, as can be objectively measured by operational metrics such as business operations, users, customers, unit sales, revenue, profits and/or market value (as appropriate) and its high growth trajectory is expected to continue;
  - each WVR beneficiary must have been materially responsible for the growth of the business, by way of his skills, knowledge and/or strategic direction in circumstances where the value of the company is largely attributable or attached to intangible human capital;
  - each WVR beneficiary must be a director of the issuer at the time of listing. The WVR beneficiary must also have an active executive role within the business, and has contributed to a material extent to the ongoing growth of the business; and
  - the applicant must have previously received meaningful third party investment from at least one sophisticated investor (which must remain at IPO). Such investors will be required to retain an aggregate 50% 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 provided that the main investors are in compliance). The Stock Exchange would not normally require an applicant to demonstrate that it has received meaningful third party investment if the applicant is a spin-off from a parent company.

The above factors are not exhaustive or binding, and the Stock Exchange retains absolute discretion to reject an application even if these requirements are met or on suitability grounds if the WVR structure is an extreme case of non-conformance with governance norms.

### Expected Market Capitalisation

The applicant must satisfy either of the following: (a) have a market capitalisation of at least HK\$40 billion at listing; or (b) have a market capitalisation of at least HK\$10 billion at listing and revenue of at least HK\$1 billion in its most recent audited financial year.

### Minimum Economic Interest

All WVR beneficiaries must collectively beneficially own at least 10% of the underlying economic interest in the applicant's total issued share capital at listing. The Stock Exchange may accept a lower minimum shareholding percentage on a case-by-case basis if the lower percentage shareholding still represents a very large amount in absolute dollar terms (for example, if the applicant has a market capitalisation of over HK\$80 billion at listing) taking into account other factors as appropriate.

## WVR Safeguards

The new rules contain WVR safeguards including those set out below. Some of these safeguards must be incorporated in the issuer's constitutional documents.

### Ring-Fencing

Companies with WVR rights will be subject to the following restrictions:

- only new applicants will be able to list with a WVR structure and the Stock Exchange will seek to ensure that companies do not use artificial means to circumvent this and other restrictions;
- they are prohibited from increasing the proportion of WVR in issue or issuing any further WVR shares;
- WVR beneficiaries have a limited right of pre-emption for pro rata offerings to all shareholders or pro rata issues of securities to all shareholders by way of scrip dividends, or stock splits (or similar transactions), provided that the proportion of WVRs in issue is not higher after the corporate action; and
- issuers will be prohibited from changing rights attached to WVR shares to increase the WVRs attached to those shares. Issuers may change terms to reduce the WVRs attached to its shares with prior approval from the Stock Exchange and an announcement.

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## Lapse of WVRs

The WVRs will lapse permanently if a WVR beneficiary:

- dies, ceases to be a director, or is deemed by the Stock Exchange to be incapacitated or to no longer meet the requirements of a director set out in the Listing Rules (for example, if the director failed to comply with the requirement for corporate actions to be conducted on a one vote per share basis); or
- transfers his beneficial interest or economic interest in those shares, or the voting rights attached to them, to another person (subject to limited exceptions in the case of trust and other structures for estate and/or tax planning purposes).

## Conversion Ratio

The WVR shares must be converted into ordinary shares (whether on a voluntary basis or mandated by the Listing Rules) on a one-to-one ratio. Applicants must seek from the Stock Exchange as part of the initial listing application approval of the issue of WVR shares and listing of shares upon conversion.

## Voting Rights

WVR structures must be subject to the following restrictions:

- a WVR structure must be attached to a specific class of unlisted shares. The WVRs attached to them must confer to a beneficiary only enhanced voting power on resolutions tabled at general meetings;
- voting power attached to WVR shares must be capped at not more than ten times the voting power of ordinary shares;
- the WVR structure must enable non-WVR shareholders to cast at least 10% of the votes eligible to be cast on resolutions at general meetings. Non-WVR shareholders holding at least 10% of the voting rights on a one vote per share basis must be able to convene a general meeting and add resolutions to the meeting agenda; and
- the following matters must be decided on a one vote per share basis: changes to the issuer's constitutional documents; variation of class rights; appointment or removal of an independent non-executive director or auditors; and voluntary winding-up of the issuer.

## Deemed Connected Person and Core Connected Person

A WVR beneficiary and any vehicle through which the WVR beneficiary holds the WVR shares are deemed to be connected persons and core connected persons of the issuer, and are subject to the connected transaction requirements under the Listing Rules.

## Corporate Governance

Issuers with WVR structures are required to implement the following enhanced corporate governance measures:

- establish a Corporate Governance Committee comprised entirely of independent non-executive directors ("INEDs"), and include a summary of the work of the committee in the Corporate Governance Report that it discloses in its half-yearly and annual report;
- mandate certain provisions of the Corporate Governance Code regarding the role of an INED, establishment of a nomination committee (comprised of a majority of INEDs and chaired by an INED) and retirement of INEDs by rotation at least once every three years. The nomination committee will be solely responsible for making recommendations to the board of directors regarding the nomination of INEDs;

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- require that the issuer engage a compliance adviser on a permanent basis and consult with the adviser on matters related to its WVR structure, transactions in which the WVR beneficiaries have an interest and where there is a potential conflict of interest between non-WVR shareholders and WVR beneficiaries; and
  - require directors, senior management and the company secretary to undergo appropriate training on WVR and its associated risks.

## Enhanced Disclosure

Issuer with WVR structures must make the following enhanced disclosures:

- prominently identify through a unique stock marker “W” at the end of their stock name;
- include the warning “a company controlled through weighted voting rights” and describe the WVR structure, the issuer’s rationale for having it and the associated risks for shareholders prominently on the front page of all its listing documents, periodic financial reports, circulars, notifications and announcements required by the Listing Rules; and
- identify the WVR beneficiaries, impact of potential conversion into ordinary shares on share capital, and circumstances under which the WVRs will cease in its listing documents, annual reports and interim reports.

## Secondary Listings of Qualifying Issuers

To attract large emerging and innovative companies with primary listings in the US and on other major international exchanges to list in Hong Kong, the Stock Exchange has added a new Chapter 19C of the Listing Rules to create a new concessionary route to secondary listing for “qualifying issuers”, while preserving important protections for Hong Kong investors.

### Listing Requirements

A qualifying issuer must demonstrate that it is both eligible and suitable for listing and must:

- be an innovative company, by reference to the characteristics set out above. The Stock Exchange retains a discretion to find a qualifying issuer not suitable for listing even if it satisfied these characteristics;
- have a good record of compliance for at least two full financial years on a qualifying exchange (namely, the New York Stock Exchange, Nasdaq or the “Premium Listing” segment of the London Stock Exchange’s Main Market); and
- have an expected market capitalisation at the time of secondary listing of at least HK\$10 billion. A secondary listing applicant (a) with a WVR structure; and/or (b) which has a “centre of gravity” in Greater China (a “**Greater China Issuer**”) is also required to have at least HK\$1 billion of revenue in its most recent audited financial year if it has an expected market capitalisation at the time of secondary listing in Hong Kong of less than HK\$40 billion.

An applicant applying for secondary listing under this route is entitled to make a confidential filing of its Application Proof.

### Automatic Waivers

The Stock Exchange has codified and applied to qualifying issuers the waivers in the Listing Rules that it currently automatically grants to eligible secondary listed companies, for example, with respect to notifiable and connected transactions and the Corporate Governance Code.

## Corporate Governance

A qualifying issuer must also prominently disclose in its listing documents provisions in its constitutional documents concerning governance that are unusual compared with normal practices in Hong Kong.

### Concessions for Grandfathered Greater China Issuers and Non-Greater China Issuers

The new rules apply different requirements depending on the type of issuer and are set out in the table below:

Issue	Non-Grandfathered Greater China Issuer	Grandfathered Greater China Issuer	Non-Greater China Issuer
Definition	Greater China Issuer that is primary listed on a qualifying exchange after 15 December 2017.	Greater China Issuer that was primary listed on a qualifying exchange on or before 15 December 2017.	Qualifying issuer that is not a Greater China Issuer.
Equivalent shareholder protection requirements	The issuer must vary its constitutional documents to ensure key shareholder protection standards are comparable to those of Hong Kong companies.	The issuer must demonstrate how the domestic laws, rules and regulations to which it is subject and its constitutional documents together provide key shareholder protection standards. The Stock Exchange may require the issuer to amend its constitutional documents to provide them.	
Variable Interest Entity (“VIE”) structures	The issuer is required to comply with existing Stock Exchange requirements (Listing Decision HKEX-LD43-3).	The issuer may list with an existing VIE structure. It must provide the Stock Exchange with a PRC legal opinion that the VIE structure complies with PRC laws, rules and regulations, and comply with disclosure requirements under Listing Decision HKEX-LD43-3).	
WVR structures	The issuer is required to meet eligibility and suitability criteria for listing with a WVR structure.  It must conform to all primary listing requirements including ongoing WVR safeguards.	The issuer is required to meet eligibility and suitability criteria for listing with a WVR structure.  It may list with existing WVR structure and is not required to comply with ongoing WVR safeguards (except for disclosure requirements).	
Permanent migration of the bulk of trading (taken to mean 55% or more of total worldwide trading volume) to Hong Kong	–	The issuer is not required to reconfirm with Hong Kong WVR safeguards (except for disclosure requirements) or amend their existing VIE structures.	
	The codified waivers granted under the new concessionary route will no longer apply. The issuer will be treated as having a dual-primary listing and waivers will be granted on a case-by-case basis.  The issuer will have a 12-month grace period to comply with the applicable requirements.	The issuer will be able to continue to enjoy automatic waivers granted.	

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## Next Steps

The Stock Exchange currently accepts formal pre-IPO enquiries and listing applications under the new rules. It expects the first listings under the new regime to take place in June or July 2018. The Stock Exchange plans to launch a separate consultation by 31 July 2018 to explore the option of allowing corporate entities to benefit from WVRs.

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