

## Deepening Capital Market Reform Speech at Financial Street Forum 2023

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Good afternoon, everyone. I am honoured to be invited by the China Securities Regulatory Commission (CSRC) to participate in this year's Financial Street Forum.

The registration-based initial public offering (IPO) system reform has been implemented across the board in Mainland China for six months now, and we are pleased to see the continued steady operation of its capital market. Both the efficiency and predictability of IPO approvals and registrations have improved under the framework where the Mainland stock exchanges review IPOs and the CSRC approves registrations, with different focuses but connected with one another. In the first half of 2023, amid the sluggish global IPO market, the A-share market took the lead globally in both the number of new share issuance and the size of funds raised.

The CSRC emphasised repeatedly in public that the registration system does not mean relaxing quality standards. Rather, it is necessary to establish a comprehensive set of regulatory arrangements covering all aspects of the listing process — before, during and after. I fully agree with this.

The Central Financial Work Conference held in Beijing last week highlighted: the financial sector must provide high-quality services for economic and social development; the pivotal role of the capital market must be given full play; the effectiveness of financial regulation must be vigorously enhanced; and Hong Kong's position as an international financial centre must be strengthened. These have always been the top priorities of the Securities and Futures Commission (SFC) as well. To maintain the market's long-term development and to benefit society at large, we have been implementing sound regulation and taking decisive enforcement action to protect investors' interest and manage financial risks.

Next, I would like to take this opportunity to briefly introduce the Hong Kong stock market based on what happens before, during and after listings, including our pre-listing vetting, post-listing regulation and enforcement action, as well as the enhancements we have introduced in recent years.

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Note: This is an English translation of the original speech which was delivered in Chinese.

## **Implementing dual filing regulatory regime to ensure quality of information disclosures**

There is no one-size-fits-all approval or registration model for stock issuance and listing in the world. Each country or region adopts a regime most suited to its needs, taking into account such factors as its development stage, legal system, levels of regulation and enforcement and investor mix. However, in general, a sound system essentially encompasses a set of clear and explicit listing regulatory requirements, with a focus on disclosures and rules to ensure that listing procedures are open, transparent and predictable, emphasising the issuers' responsibility to disclose information fully and diligently.

The dual filing regime has been in place in Hong Kong's stock market since 2003. All listed companies must file their applications and disclosure materials with the SFC via Hong Kong Exchanges and Clearing Limited (HKEX). The SFC and HKEX's respective roles in listing regulation have been clarified through a memorandum of understanding. HKEX is the frontline regulator of listing-related matters and the primary contact point for listing applicants. The SFC may comment on draft listing documents and disclosure materials, or request further information, and may object to listing applications if necessary.

Both regulators have their own areas of focus. HKEX is mainly responsible for vetting listing applicants' eligibility for listing and disclosures in relation to their business, profit, market capitalisation and corporate management in accordance with the Listing Rules. The SFC primarily focuses on whether there is false or misleading information in listing applications and whether the issuance and listing of securities are in the public interest under the Securities and Futures Ordinance and its subsidiary legislation<sup>1</sup>.

At times, some market participants have a misconception that relevant requirements under the dual filing regime will cause a delay in the process of vetting listing applications. In reality, the SFC and HKEX carry out their vetting processes concurrently and strive to maintain high efficiency and transparency. Over the past three years, more than 90% of listing applications were vetted by the SFC within 60 business days, whilst the remainder generally involved more serious issues, such as the genuineness of applicants' financial data or compliance matters.

To give an example, the majority of one applicant's revenue was not paid directly by its clients, but through certain third parties. What's even more suspicious is that some of the payers have close relationships with connected persons. This has raised the SFC's concern as to whether the sponsor has conducted reasonable due diligence to check the genuineness of its sales.

## **Enhancing IPOs' inclusiveness to attract more new economy companies**

In recent years, the SFC and HKEX have moved with the times by finetuning their regulatory frameworks with a view to enhancing the inclusiveness for IPOs. New listing regimes, including the weighted voting rights structure, the "homecoming" of Mainland concept stocks for secondary listings, and the pre-profit biotech regime, have helped finance the nation's booming new economy and expanded the number and market capitalisation of growth stocks in the Hong Kong market.

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<sup>1</sup> The Securities and Futures (Stock Market Listing) Rules.

Following the launch of the listing regime for pre-profit biotech companies in 2018, HKEX introduced a new regime for specialist technology companies on 31 March this year to support their continuous funding needs for research and development and commercialisation purposes. The two listing regimes allow pre-revenue or pre-profit biotech and specialist technology issuers to go public on the Main Board. To date, more than 60 biotech companies have listed through the new regime with over HK\$100 billion in total funds raised, whilst the listing application of the first specialist technology company is currently in progress.

### **Combatting market misconduct like shell activities and ramp and dump scams**

Combatting the misconduct of listed companies is one of our top priorities.

Between 2015 and 2018, shell-related trading activities were exceptionally active. The lower entry requirements for GEM made it easy to “make shells”, creating a more pronounced effect on the GEM board. Many companies changed hands soon after listing, and, as shells, saw the injection of the new controlling shareholders’ businesses to circumvent the listing requirements. Shell making was often associated with various types of market misconduct, such as ramp and dump scams. Bad actors use various means to ramp up the share prices of stocks that are more susceptible to cornering with low trading turnover and small market capitalisation. They then take advantage of social media platforms, on which they may open fake accounts with photos of investment experts or key opinion leaders to lure investors to buy the illiquid stocks before dumping them. This often causes losses to retail investors.

To rid the market of bad practices and harm and ensure coordinated, targeted and effective regulatory action, the SFC has set up an internal cross-divisional working group by bringing together experts from the Intermediaries, Corporate Finance and Enforcement divisions. With timely communication and discussion, the working group can coordinate resources, flexibly adopt different regulatory measures and handle cases in a collaborative manner.

As part of our ongoing enhancements to the SFC’s listing and post-listing regulation and enforcement efforts, we focus on the following four strategic priorities:

#### *1. Improving the implementation arrangements for the dual filing regime*

- Adopting a front-loaded approach to listing regulation in recent years, the SFC has acted and responded in a swift and timely manner, with an emphasis on early, targeted and systematic intervention. We may raise objections to listing applications at the pre-listing stage. In addition, if the application documents contain any false or misleading information, or if the application process involves any illegal act, we will investigate and prosecute relevant persons as appropriate.

#### *2. Strengthening post-listing regulation*

- Over the past few years, under the SFC’s guidance, HKEX has introduced various policies to enhance market quality and credibility. These measures include limiting highly dilutive capital raising, establishing a more efficient delisting process, tightening the restrictions on backdoor listings and shell activities, raising the profit requirements for Main Board listings, as well as expanding the powers to take disciplinary actions, etc.
- Following a series of regulatory actions and rule changes by the SFC, it has become much more difficult and costly for backdoor listings to take place and the demand for shell companies has reduced, leading to a sharp fall in shell prices. The drastic

reduction in shell activities has no doubt tipped the balance towards a fairer and more transparent market.

### *3. Enhancing collaboration with other local law enforcement agencies*

- We have stepped up our market surveillance and enforcement work to focus on ramp and dump cases, and the scope of our investigations has been expanded to disrupt mastermind syndicates. We have enhanced our collaboration with the Independent Commission Against Corruption, the Commercial Crime Bureau of Hong Kong Police Force as well as overseas regulators to ensure that bad actors have nowhere to hide. Moreover, about HK\$1.8 billion worth of assets have been frozen, involving 10 stocks targeted by the scams. To date, a sizeable number of people have been arrested and prosecuted.

### *4. Deepening cross-boundary enforcement cooperation with the CSRC*

- Since the majority of the companies listed in Hong Kong are Mainland-based, we and the CSRC have maintained close regulatory and enforcement cooperation in respect of the listing of these companies in Hong Kong. We also joined forces in combating cross-boundary illegal activities. These efforts are important for ensuring the healthy and stable development of the two capital markets and safeguarding the legitimate interests of investors.

## **Promoting the sustainable development of Hong Kong's stock market ecosystem**

We are committed to improving the quality of listed companies and promoting the sustainable development of the Hong Kong stock market ecosystem. For instance, with respect to board independence, transparency and accountability, ongoing amendments have been made to the Listing Rules and the Corporate Governance Code to continuously enhance the corporate governance of listed companies.

Furthermore, in recent years, a growing number of institutional investors demand to access listed companies' sustainability information and how this affects their profitability, financing ability, investment opportunities and company prospects. Meanwhile, many multinational companies need to calculate the carbon emissions of supply chains, and China is playing a pivotal role in global supply chains. The quality of listed companies' sustainability information disclosures is particularly important to sustain their business ties with these multinational companies.

Hong Kong supports the adoption of the IFRS<sup>2</sup> Sustainability Disclosure Standards published by the International Sustainability Standards Board (ISSB) this June. These standards aim to serve as an international language for the communication of sustainability information. Becoming well-versed in this language will help listed companies in Hong Kong meet the requirements of investors and multinational companies, enabling them to tap into the opportunities arising from sustainable and low-carbon transformation, and maintain their competitiveness. If listed companies in Hong Kong do not make appropriate disclosures or if they disclose low-quality information, they may be bypassed by international capital in investing and financing.

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<sup>2</sup> International Financial Reporting Standards.



There are many large companies from the Mainland listed on HKEX. Encouraging them to make high-quality disclosures on sustainability will facilitate the accomplishment of the national goals of carbon peaking and carbon neutrality, as well as global climate goals.

Lastly, having a robust market ecosystem, maintaining an open, transparent and predictable market, plays a vital role in boosting investor confidence.

I believe the Mainland regulators' ongoing efforts to enhance the supporting systems will improve the access to financing for the Mainland stock market, further optimise the A-share market structure, and enable the capital market to better serve our nation in its road towards technological self-reliance and economic transformation.

Thank you.