

# Listings and takeovers

We oversee listing and takeovers matters in Hong Kong, including takeovers and merger activities, vetting of listing applications, disclosure requirements, corporate conduct and the listing-related functions of The Stock Exchange of Hong Kong Limited (SEHK). We review listing and takeovers policies to promote the development of a fair and orderly securities market in Hong Kong.

## Listing policy

On 15 September 2017, the SFC and SEHK issued conclusions to their joint consultation on proposed enhancements to SEHK's decision-making and governance structure for listing regulation. The conclusions paper clarifies the role of the SFC as the statutory regulator which administers the Securities and Futures Ordinance (SFO) and the Securities and Futures (Stock Market Listing) Rules (SMLR), and

which supervises, monitors and regulates the activities carried on by SEHK. It also clarifies SEHK's role as the regulator administering the Listing Rules<sup>1</sup>.

In March 2018, the SFC and SEHK signed an addendum to the Memorandum of Understanding Governing Listing Matters<sup>2</sup>, following which a new Listing Policy Panel<sup>3</sup> was established as an advisory, consultative and steering body to initiate and centralise discussions on listing policy with broader regulatory or market implications.

Given the high level of interest in infrastructure investment opportunities in developing markets, such as those related to the Mainland's "Belt and Road" initiative, we issued a statement in April 2017 setting out the factors we take into account when reviewing the listing applications of infrastructure project companies.

## Explaining SMLR

Under our new, front-loaded regulatory approach, we engage in targeted intervention at an early stage to suppress illegal, dishonourable and improper market practices and protect the integrity of financial markets and the interests of investors. This new approach has increased our direct presence in more crucial listing matters which fall within the scope of the SMLR<sup>a</sup> or the SFO.

Section 6(2) of the SMLR empowers us to raise objections to a listing of shares (including by listed companies). If it is likely that an objection would be raised, we will promptly issue a "letter of mindedness to object" (LOM)<sup>b</sup> to the applicant setting out our substantive concerns, which we then discuss with the applicant and its advisers.

This is a departure from the SFC's previous approach where comments on initial public offering (IPO) applications were raised via SEHK. It is more efficient for an applicant to communicate directly with the SFC regarding our concerns.

<sup>a</sup> SMLR is subsidiary legislation of the SFO.

<sup>b</sup> An LOM sets out the substantive concerns of the SFC along with detailed reasons.

<sup>c</sup> This decision is subject to review by the Securities and Futures Appeals Tribunal.

If the applicant's response to an LOM fails to address our concerns, we will issue a final decision notice to raise objections<sup>c</sup>. Cases handled so far involve doubtful financial projections and false or misleading information related to suppliers. In one case, a listed company failed to address our concerns about a share placement to be conducted at a substantial discount to a small group of subscribers and had to cancel the placement.

Section 8 of the SMLR empowers the SFC to direct the suspension of trading in a listed company's shares. Unless urgent action is required by circumstances such as protecting investors, the SFC would normally first issue a "show cause letter" setting out its concerns and give the company an opportunity to respond.

In July 2017, we published the first issue of the *SFC Regulatory Bulletin: Listed Corporations*, providing guidance on our new regulatory approach.

<sup>1</sup> SEHK will be the primary front-line regulator and will remain the contact point for all listing applications save in respect of concerns raised by the SFC under the SMLR.

<sup>2</sup> The Memorandum of Understanding Governing Listing Matters was signed in January 2003.

<sup>3</sup> The Listing Policy Panel consists of 12 members comprising senior representatives of the SFC, the Listing Committee, Hong Kong Exchanges and Clearing Limited (HKEX) and the Takeovers and Mergers Panel. It is not a committee under the SFC, HKEX or SEHK.

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We issued a guidance note in May 2017 on directors' duties regarding valuations in corporate transactions together with a statement on the liability of valuers for the disclosure of false or misleading information.

Jointly, the SFC and SEHK are conducting a holistic review of listing regulation which seeks to address issues relating to GEM<sup>4</sup>, capital raisings and the delisting framework under the Listing Rules.

SEHK issued a consultation paper on proposed changes to the regulation of GEM on 16 June 2017 and published consultation conclusions on 15 December 2017. The ensuing changes, which took effect on 15 February 2018, include:

- removing the streamlined process for GEM transfers to the Main Board;
- introducing a mandatory public offering requirement of at least 10% of the total offer size for all GEM initial public offerings (IPOs);
- increasing the minimum cash flow requirement for GEM applicants from \$20 million to \$30 million; and
- increasing the minimum market capitalisation of Main Board applicants at the time of listing from \$200 million to \$500 million.

In September 2017, SEHK launched a consultation which sought to address concerns about abusive fundraisings by some listed companies as well as a separate consultation on proposals to streamline the delisting procedures for suspended stocks.



Mr Brian Ho, Executive Director, Corporate Finance speaking at the Conference on Business Ethics for Listed Companies 2017

In response to market feedback to SEHK's June 2017 New Board Concept Paper, SEHK announced a proposal in December 2017 to expand the existing listing regime by allowing the listing on the Main Board of companies from emerging and innovative sectors. In February 2018, SEHK issued a consultation paper on proposals and draft rules to introduce a new listing regime for companies with weighted voting rights structures, biotechnology companies not meeting the financial eligibility tests under the current listing rules and overseas-listed companies seeking a secondary listing in Hong Kong. The new listing regime was implemented on 30 April 2018.

As of 3 July 2017, disclosure of interests notices must be submitted via Hong Kong Exchanges and Clearing Limited's new electronic filing system<sup>5</sup>. A three-month transition period was provided.

<sup>4</sup> Formerly known as the Growth Enterprise Market.

<sup>5</sup> The Disclosure of Interests Online System. This requirement follows the commencement of mandatory electronic filing provisions under Part XV of the SFO.

## New listing applications

	2017/18	2016/17	2015/16
Total listing applications <sup>a</sup>	309	245	218
Cases lapsed/withdrawn/rejected during the year	27	38	26
Cases returned	3	5	3
New listings <sup>b</sup>	203	148	131

<sup>a</sup> Including applications for transfer from GEM to the Main Board (2017/18: 22; 2016/17: 18; 2015/16: 12).

<sup>b</sup> Including successful transfers from GEM to the Main Board (2017/18: 17; 2016/17: 6; 2015/16: 12).

## IPO applications

We vet listing applications and raise enquiries on the basis of insufficient or inadequate disclosures, and object to a listing if it appears to us that it would not be in the interest of the investing public or in the public interest for the securities to be listed.

We received 309 listing applications via SEHK during the year, up 26% from 245 last year. We shared with SEHK our comments or concerns on 299 of them. Three listing applications were returned by SEHK, and an eight-week moratorium<sup>6</sup> was imposed because the application proofs or related documents were not substantially complete.

To tackle serious disclosure and public interest issues, we issued seven LOMs to listing applicants directly during the year (see sidebar on page 51). Subsequently, we issued final decision notices to object to two of these applicants because their responses failed to address our concerns<sup>7</sup>. Of the other five, two were withdrawn, two lapsed<sup>8</sup> and one was still being vetted at the end of the reporting period.

## Corporate conduct

We monitor company announcements on a daily basis to identify corporate misconduct and irregularities in disclosures, including failure to disclose information in a timely manner and false or misleading disclosures. We also focus on transactions and corporate actions which are potentially detrimental to shareholders, paying particular attention to serious misbehaviour.

We use our information gathering power under section 179<sup>9</sup> to raise enquires with listed companies and, where our concerns are not addressed satisfactorily, intervene directly.

## Takeovers matters

In Hong Kong, takeovers, mergers, privatisations and share buy-backs affecting public companies are regulated by the Codes on Takeovers and Mergers and Share Buy-backs, which aim to afford equal treatment of shareholders, to mandate disclosure of timely and adequate information to enable shareholders to make informed decisions as well as to ensure a fair and informed market.

<sup>6</sup> The respective applicants can only submit a new listing application with a new application proof more than eight weeks after the return.

<sup>7</sup> After our objection, one of these applicants resubmitted a listing application and was subsequently listed after addressing our concerns.

<sup>8</sup> After a lapse, one applicant resubmitted a listing application and was subsequently listed after addressing our concerns.

<sup>9</sup> Section 179 of the SFO gives the SFC the power to compel the production of records and documents from persons related to a listed company in relation to fraud or other misconduct.

## Listings and takeovers

### Takeovers and Mergers Panel rulings

The Takeovers and Mergers Panel met in April 2017 to consider the application by Television Broadcasts Limited (TVB) for a whitewash waiver in relation to a share buy-back offer it announced in January 2017. The panel ruled that full disclosure should be made of the shareholding and ownership structure of Young Lion Holdings Limited<sup>10</sup>. It also ruled on how the shareholders' resolution to approve the whitewash waiver should be voted<sup>11</sup>.

In May 2017, TVB applied to the High Court of Hong Kong to commence a judicial review of the panel's April decision on how shareholder votes should be counted, which the High Court quashed following a September 2017 hearing. Other aspects of the panel's ruling, including full disclosure of Young Lion's shareholding and ownership structure, were not part of the judicial review and remain valid.

### ICE

This year, the SFC cross-divisional unit designated ICE (Intermediaries, Corporates, Enforcement)<sup>a</sup> recorded significant progress in tackling problems affecting the quality of our markets.

One major issue was the unusual price volatility in GEM stocks. The average first day price gain for GEM stocks which listed by way of placing was 743% in 2015 and 530% in 2016. Mobilising ICE, we issued two statements in January 2017 to remind listed companies and sponsors of their obligations to ensure compliance with the GEM Listing Rules, including that conditions exist for an open, orderly and informed market at the time of listing.

When we also exercised our powers under SMLR to object to GEM placings with a high concentration of shareholders, this had an immediate impact. Some companies delayed sub-standard listing plans and others changed their offerings to include a public offer tranche. In the year following the January statements, the average first-day price gain for GEM stocks was only 23%, and shareholding concentrations in newly-listed GEM companies were also lower.

Another longstanding problem was the use of unrealistic valuations to support suspicious asset disposals or acquisitions by listed companies. In May 2017, ICE coordinated the issuance of a

guidance note on directors' duties, a circular to financial advisers and a statement on the liability of valuers to remind them of their responsibility to uphold shareholders' interests when corporate assets are acquired or disposed.

In June 2017, ICE authorised one of the largest search operations in our history, pulling together over 100 staff to search multiple premises of interrelated companies. These companies comprised one of several groups working in coordination to extract value from unsuspecting investors by conducting apparently legitimate transactions which may not make any business sense beyond a very superficial level. The investigations were based on suspicions that market manipulation and financing transactions designed to defraud minority shareholders could be involved.

In March 2018, ICE issued a circular that identified continued deficiencies in sponsor work and urged licensed corporations to critically review and enhance their systems and controls to comply with the expected standards and the relevant codes, rules and regulations when carrying out sponsor work.

ICE allows us to deploy the full spectrum of our regulatory tools through tighter cross-divisional collaboration, whilst keeping a close watch on market developments to identify emerging problems and formulate strategies to address them proactively at an early stage.

<sup>a</sup> The unit, which pools resources from the Intermediaries, Corporate Finance and Enforcement divisions, was established in 2016 in response to the increasing prevalence of regulatory issues relating to corporate behaviour and conduct.

<sup>10</sup> Young Lion together with its concert parties holds 29.9% of TVB's shares and could hold up to 41.2% following the buy-back.

<sup>11</sup> The panel also ruled that TVB's whitewash waiver should be granted subject to a majority of votes cast in favour of a shareholders' resolution to approve the offer (without adjustment), and the whitewash waiver should not be put before TVB's shareholders for a separate vote.

## Takeovers activities

Investigations and enquiries remained an important focus of our supervision and regulation of takeovers activities. We sanctioned a number of parties for breaching the Takeovers Code during the year:

- In August 2017, we publicly censured and imposed a 24-month cold shoulder order against Yeung Wing Yee for failing to making a general offer after acquiring over 30% of the shares in Union Asia Enterprise Holdings Limited, depriving the company's shareholders of the right to receive an offer.
- In the same month, we also publicly censured China Life Insurance (Overseas) Company Limited for breaching the dealing disclosure requirements during the privatisation of Glorious Property Holdings Limited.
- In September 2017, we publicly censured Chen Chi-Te and Kenneth C.M. Lo (both directors of Taiwan Cement Corporation) for breaching the dealing provisions during the company's proposed privatisation of TCC International Holdings Limited.
- In December 2017, Zhang Qiang was publicly censured for acquiring shares in Feishang Non-metal Materials Technology Limited within six months after the close of an offer at above the offer price.

## Takeovers activities

	2017/18	2016/17	2015/16
General and partial offers under Code on Takeovers and Mergers	59	73	50
Privatisations	11	13	7
Whitewash waiver applications	41	37	51
Other applications under Code on Takeovers and Mergers <sup>^</sup>	289	365	323
Off-market and general offer share buy-backs	1	4	1
Other applications under Code on Share Buy-backs <sup>^</sup>	0	2	3
Total	401	494	435

<sup>^</sup> Including stand-alone applications and those made during the course of a Code-related transaction.  
Note: Also see Table 3 in Breakdown of SFC activity data on pages 163-169 for more details.

- In March 2018, Nomura International (Hong Kong) Limited and Lee Yuen Yee, Annisa were publicly criticised for failure to comply with requirements for research reports and profit forecasts during a possible offer for West China Cement Limited.

## Code amendments

We launched a three-month consultation on proposed amendments to the Codes on Takeovers and Mergers and Share Buy-backs in January 2018. Key proposals enhance investor protection by increasing the voting approval threshold for whitewash waivers to 75% of independent shareholders and empowering the Takeovers and Mergers Panel to require compensation to be paid to shareholders who have suffered as a result of a breach of the codes.

Other proposed amendments clarify the obligations of persons dealing with the Takeovers Executive<sup>12</sup>, the Takeovers and Mergers Panel and the Takeovers Appeal Committee in all codes-related transactions, including their prompt cooperation and assistance and the provision of true, accurate and complete information.

We made changes to the Introduction to the Codes on Takeovers and Mergers and Share Buy-backs to introduce a new section 19.1 in July 2017 to align them with the newly effective Financial Institutions (Resolution) Ordinance as well as a new note to section 4.2 in April 2018 to bring them in line with the new listing regime for companies from emerging and innovative sectors.

<sup>12</sup> Refers to the Executive Director of the SFC's Corporate Finance Division or his delegate.