



Hong Kong

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HONG KONG STOCK EXCHANGE ISSUES A CONSULTATION PAPER ON DELISTING AND OTHER RULE AMENDMENTS

Introduction

On 22 September 2017, the Stock Exchange of Hong Kong Limited (the **Exchange**) published a Consultation Paper¹ on Delisting and Other Rule Amendments.

The consultation paper proposes improvements to the effectiveness of the delisting framework under the Main Board Listing Rules and the Rules for the Growth Enterprise Market (**GEM Listing Rules**), in order to address the issue of prolonged suspension of trading in issuers' listed securities. The Exchange proposes the following amendments to the delisting framework:

1. Under the Main Board Listing Rules:
 - Add a separate delisting criterion under new Main Board Listing Rule 6.01A which would allow the Exchange to delist an issuer after its continuous suspension for a prescribed fixed period (either 12, 18 or 24 months);
 - Stipulate a new delisting process under Main Board Listing Rule 6.10 which would apply to the delisting criteria in Main Board Listing Rule 6.01: the Exchange would be able to (i) publish a delisting notice and give the issuer a period of time to remedy the relevant matters to avoid delisting, or (ii) delist an issuer immediately; and

- Remove Practice Note 17 (Sufficiency of Operations and Delisting Procedures), since the new delisting process would apply to issuers that do not have sufficient operations or assets.
2. Under the GEM Listing Rules: add a separate delisting criterion so as to enable the Exchange to delist an issuer after its continuous suspension for a prescribed period (either 6 or 12 months); and
 3. Provide transitional arrangements for Main Board/GEM issuers whose securities are under suspension immediately prior to the effective date of the above proposed framework.

Current Framework

Main Board

Pursuant to Main Board Listing Rule 6.01, the Exchange may at any time cancel the listing of any securities to protect investors and maintain an orderly market. At present, the Exchange may cancel a listing where an issuer (a) is in material breach of the Main Board Listing Rules; (b) fails to maintain sufficient public float; (c) fails to maintain sufficient operations or assets; and (d) is no longer suitable for listing. The Exchange has considerable discretion in delisting an issuer on the ground that it is "no longer suitable for listing". The Listing Committee is the body responsible for making the decision to delist an issuer.

¹ <https://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2017091.pdf>

The Main Board Listing Rules provide for delisting procedures in two specific circumstances:

1. For issuers that do not have sufficient operations or assets (**PN17 companies**), Practice Note 17 provides for a three stage delisting procedure, with each stage having a duration of at least six months. At the end of each stage, the Exchange determines whether proceeding to the next stage is appropriate, and this depends on whether the issuer has submitted a viable resumption proposal to the Exchange; and
2. For issuers that are no longer suitable for listing, the Exchange may, pursuant to Main Board Listing Rule 6.10, publish a delisting notice stipulating a period within which the issuers must remedy the issues to avoid delisting.

The current delisting Listing Rules emphasise the requirement that issuers must take steps to resume trading, instead of facilitating delisting. This requirement takes into consideration that if there is a delisting, minority shareholders might end up holding shares in an unlisted company with no exit. The Exchange has however faced difficulties in delisting issuers in a timely manner under the existing delisting framework:

- a) Under the current Rules there is no clear benchmark to support a delisting decision in circumstances where an issuer is suspended for a prolonged period but is taking steps to remedy issues giving rise to the suspension. Listing Rule 6.04 of the Main Board does not define the meaning of the phrases “prolonged period” or “adequate action. This may mean that issuers that have committed material breaches of the Main Board Listing Rules may not have strong enough incentives to take active steps to rectify matters.
- b) Under the delisting criteria in Main Board Listing Rule 6.01, the Exchange may have insufficient grounds to support a delisting decision. If an issuer fails to publish financial results due to allegations concerning accounting or other corporate irregularities, the Exchange is unlikely to have evidence to conclude whether the issuer is unsuitable for continued listing prior to the outcome of the investigation. Such investigation is likely to last a considerable period of time.

- c) For PN17 companies, in many cases the three-stage delisting procedure takes more than 18 months because the commencement of each stage is a decision of the Exchange that requires an assessment of the viability of any resumption proposal submitted by the issuer. Each decision of the Exchange has to undergo two levels of review and, therefore, the delisting process is further prolonged if a PN17 company decides to review the Exchange’s decision to put it into each of the three delisting stages.

GEM

GEM Listing Rule 9.15 provides for a delisting procedure for all existing delisting criteria under GEM Listing Rules 9.01 and 9.04 (which are similar to the criteria under Main Board Listing Rule 6.01). Under this procedure, the Exchange may issue a delisting notice indicating a period (ordinarily, of 6 months) within which the issuer must remedy the matters that gave rise to the Exchange’s proposal to cancel the listing.

As this delisting procedure also applies to issuers that do not have sufficient operations or assets, the GEM Listing Rules do not include an equivalent to the current Main Board Practice Note 17.

Main Board Proposals

Fixed period delisting criterion

The proposed fixed period delisting criterion aims at delisting issuers which fail to resolve the issues that led to their suspensions after continuous suspension for a prescribed fixed period. The fixed period would provide suspended issuers with a precise deadline that would incentivise them to act promptly towards resumption. This would allow the Exchange to delist an issuer where it currently does not have sufficient basis to support such decision under the delisting criteria of Main Board Listing Rule 6.01.

The Exchange proposes a fixed period of either 12, 18 or 24 months, with the view that:

- from their experience, a large majority of issuers would be able to remedy their suspension issues within 24 months;

- a 12 months period would serve as a stronger incentive for early resumption and would contribute to a more robust delisting policy by providing a strong deterrent effect; and
- an 18 months period is a compromise between the two and is broadly aligned with the intention of the three stage delisting process under PN17.

The fixed period should provide minority shareholders with an opportunity to resume trading in the market, as well as incentivise suspended issuers to act diligently and promptly to remedy issues. The fixed period duration should also be sufficiently long enough for issuers to remedy issues, thereby avoiding the need of the Exchange to grant an extension frequently. The Listing Committee is expected to grant an extension only in exceptional circumstances.

Delisting process under Main Board Listing Rule 6.01

The Exchange proposes to amend Main Board Listing Rule 6.10 so that for delisting based on a delisting criterion in Main Board Listing Rule 6.01, the Exchange would either (i) publish a delisting notice and give the issuer a period of time to remedy the relevant matters to avoid delisting, or (ii) delist an issuer immediately. The Exchange would usually specify a remedial period prior to delisting. The power to delist an issuer immediately is expected to be exercised only in exceptional circumstances, where the matters triggering the application of a delisting criterion are fundamental to the general listing principles and are without remedy.

The Exchange's delisting decisions made under Main Board Listing Rule 6.01 may be reviewed under Chapter 2B procedures.

Practice Note 17 removal

The Exchange proposes to remove Practice Note 17. If it is removed, the Exchange would be able to delist issuers that do not have sufficient operations or assets under either the fixed period criterion or the new delisting process of Main Board Listing Rule 6.01. The Exchange would normally apply the fixed period criterion so that issuers would be able to remedy the matters and resume trading. If appropriate, the Exchange would grant a specific remedial period to an issuer under Main Board Listing Rule 6.01.

Extension of time would only be given in exceptional circumstances, such as where the Exchange has approved an A1 application and the issuer needs additional time for implementation. A frequently granted extension of time would create certainty and undermine the incentive to act promptly towards resumption.

Issuers that have questions concerning their resumption proposals may seek the Exchange's non-binding guidance. A guidance letter on the Exchange's expected standard for re-compliance with Main Board Listing Rule 13.24 concerning sufficient operations will be published.

A note will be added to Main Board Listing Rule 13.24, which will set out the characteristics of issuers that are unable to comply with Main Board Listing Rule 13.24, which are now provided in paragraph 2.2 of Practice Note 17.

Material breach of the Main Board Listing Rules as reason for suspension or delisting

The Exchange proposes to remove Main Board Listing Rule 6.01(1), which provides that a material breach of the Main Board Listing Rules is a specific ground for suspension or cancellation of a listing. The suspension or cancellation of a listing due to a Main Board Listing Rules breach is a disciplinary decision of the Listing Committee pursuant to Main Board Listing Rule 2A.09, which is subject to the review procedures in Chapter 2A. Hence, Main Board Listing Rule 6.01(1) may create an ambiguity as to whether a suspension or cancellation decision due to a material breach of the Main Board Listing Rules should be treated as a disciplinary decision under Chapter 2A or as a non-disciplinary decision subject to the Chapter 2B review procedure.

It is proposed to clarify Main Board Listing Rule 2B.07(5), so that decisions concerning cancellation of listing under Main Board Listing Rule 6.01 are to be made and reviewed under the procedures for non-disciplinary matters set out in Chapter 2B, notwithstanding that the reasons for the cancellation include or amount to a breach of the Main Board Listing Rules by the listed issuer.

Quarterly updates by suspended issuers

It is proposed to include in the Main Board Listing Rules a requirement that suspended issuers announce quarterly updates regarding developments and progress on satisfying

resumption conditions. A suspended issuer remains obliged to disclose inside information under the Securities and Futures Ordinance (Cap 571) (**SFO**) and the Listing Rules.

Transitional arrangements

It is proposed that for issuers whose securities have been suspended continuously since a date prior the effective date of the fixed period criterion (**Effective Date**):

- a) For issuers subject to Practice Note 17, this Practice Note will continue to apply.
- b) For other issuers, if, as at the Effective Date, trading in an issuer's securities has been continuously suspended:
 - a) for less than 12 months, the fixed period under the fixed period criterion would commence immediately from the Effective Date; or
 - b) for 12 months or more, the fixed period under the fixed period criterion would be deemed to have commenced 12 months before the Effective Date if the fixed period is to be 24 months. If the fixed period is to be 12 or 18 months, it would be deemed to have commenced 6 months before the Effective Date.

GEM Proposals

The Exchange does not propose fundamental amendments to GEM's delisting mechanism.

Fixed period delisting criterion

The Exchange proposes to add a fixed period delisting criterion to allow the Exchange to delist an issuer after its continuous suspension for a prescribed fixed period. The Exchange proposes a fixed period of either 6 months or 12 months. A 6 month period is equivalent to the period that the Exchange will ordinarily specify in a remedial period under GEM Listing Rule 9.15. A 12 month period would on the other hand give additional time for an issuer to identify the underlying issues and prepare its remedial action.

It is proposed that there be a transitional arrangement that for issuers that are suspended as at the effective date of this proposed fixed period criterion, the fixed period would commence from the effective date.

Other amendments

GEM Listing Rule 9.15, which provides that the Exchange may delist an issuer at any time or if the issuer does not remedy the relevant matters within a specified remedial period, is proposed to be aligned with the proposed changes to Main Board Listing Rule 6.10.

The Exchange proposes to remove GEM Listing Rule 9.04(5), which provides that a severe breach of the GEM Listing Rules is a specific ground for suspension and cancellation of listing. It is proposed in respect of GEM Listing Rule 4.07(6) that decisions regarding the cancellation of listing under Chapter 9 are to be made and reviewed under the procedures for non-disciplinary matters set out in Chapter 4.

It is also proposed to include a requirement to announce quarterly updates in the GEM Listing Rules.

Trading suspensions and related matters

Non-publication of notifiable transactions

Under Main Board Listing Rule 13.10A / GEM Listing Rule 17.11, an issuer must apply for a trading halt if it has, or reasonably believes that it has, inside information that is required to be disclosed under Part XIVA of the SFO.

Further, the Listing Rules provide for specific suspension requirements concerning the disclosure of information, including where an issuer has not announced an agreement regarding a share or a major (or higher) transaction under Main Board Listing Rule 14.37(1) / GEM Listing Rule 19.37 (1). The Exchange proposes to remove Main Board Listing Rule 14.37(1) / GEM Listing Rule 19.37 (1) which in effect assume that such transactions are inside information.

The Exchange also proposes to delete Main Board Listing Rule 14.37(2) / GEM Listing Rule 19.37(2), which provide that an issuer who signed an agreement in respect of a notifiable transaction (which it reasonably believes would require disclosure pursuant to Part XIVA of the SFO) must immediately apply for a trading halt or suspension pending announcement of the agreement.

Resumption of trading at the direction of the Exchange

Currently, pursuant to Main Board Listing Rule 6.07 / GEM Listing Rule 9.12, the Exchange has the power to direct the resumption of trading, however under Rule 6.08 / GEM

Listing Rule 9.13, this power cannot be exercised without first giving the issuer an opportunity of being heard by the Listing Committee. The Exchange proposes to delegate the authority of directing resumption of trading to the Listing Department, and to expedite review procedures. This will include measures such as requiring any review application to be submitted by the issuer within 2 days of a decision to direct resumption. An issuer will continue to have two levels of review.

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