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[online version](http://www.charltonslaw.com/hkex-publishes-consultation-paper-on-proposed-reduction-of-required-minimum-number-of-shareholders-for-the-market-capitalisation-revenue-test/)

# HKEx Publishes Consultation Paper On Proposed Reduction Of Required Minimum Number Of Shareholders For The Market Capitalisation/Revenue Test

## Introduction

The Stock Exchange of Hong Kong ("**HKEx**") has published a consultation paper on a proposed change to the minimum number of shareholders required for applicants listing under the Market Capitalisation/Revenue Test ("**MCR Test**") ("**Consultation Paper**"). The public is invited to provide written comments on this proposal.

HKEx proposes to lower the minimum shareholder requirement for the MCR Test from 1,000 shareholders to 300 shareholders (the "**Proposal**"). This would bring the MCR Test in line with the minimum shareholder requirements for the other two eligibility tests: the Profit Test and the Market Capitalisation/Revenue/Cash Flow Test ("**MCRCF Test**").

The purpose of this note is to provide a summary of the Proposal, the reasons behind it and how to respond to the consultation.

The Consultation Paper is available on [the HKEx website](http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2010092.pdf).

Parties that wish to respond to the consultation should complete and submit the corresponding questionnaire to HKEx no later than 12 November 2010. The questionnaire is available at [here](http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2010092q.doc).

## Background

Currently, the Listing Rules require companies applying to be listed on the Main Board to choose one of three eligibility tests to satisfy:

* The Profit Test under Rule 8.05(1);
* The MCRCF Test under Rule 8.05(2); or
* The MCR Test under Rule 8.05(3).

The Profit Test and the MCRCF Test require the applicant to distribute shares to a minimum of 300 shareholders. However, the MCR Test requires the applicant to distribute shares to a minimum of 1,000 shareholders. The rationale for the MCR Test's higher requirement when it was first introduced was that large market capitalisation applicants that are able to generate substantial revenues for the most recent financial year should be able to attract greater market support to justify their listing.

However, an advantage of using the MCR Test over the other two tests is the possibility of using the waiver under Rule 8.05A to list with a shorter trading record period than three years if directors and management have sufficient experience. Additionally, applicants using the MCR Test are not required to be profitable or meet a minimum cash flow requirement.

## Reasons For The Proposed Amendment

One reason for the Proposal was to respond to market comments that the current minimum shareholder requirement for the MCR Test is too demanding. Applicants using this test must generate significant interest from both retail and institutional investors, but this may not be appropriate because such companies may be riskier investments; they do not have to be profitable or have a minimum cash flow and can have a track record of less than three years.

Another reason for the Proposal is that HKEx considers the current "public float" requirement under Rule 8.08(1)(a) to be enough to ensure an open market and retail investor participation. Under this requirement, at least 25% of an issuer's total issued share capital must normally be held by the public at all times. Since the market capitalisation requirement for the MCR Test is HK$4 billion, the corresponding "public float" market capitalisation requirement is HK$1 billion. If this is sufficient to ensure an open market and retail participation, as the HKEx believes, it may not be necessary to maintain a higher minimum shareholder requirement than for other eligibility tests.

Further evidence supporting the Proposal can be found in some statistics regarding the MCR Test. Between 2004 and 2009, only 10 companies out of 352 (3%) listed under the MCR Test. Also, 126 companies out of the 337 (37.4%) that listed in the same period under the Profit Test would have met the requirements of the MCR Test. This may suggest that applicants are discouraged from using the MCR Test due to its higher minimum shareholder requirement.

## How To Respond To The Consultation

HKEx proposes to remove Rule 8.05(3)(f) and to make a consequential amendment to Rule 8.08(2), as well as to simplify the wording of both rules. Appendix II of the Consultation Paper shows the exact proposed changes to the Listing Rules. These changes will not affect the listing criteria of the Profit Test and the MCRCF Test. The Consultation Paper asks two questions regarding these changes, included in the Appendix to this note, for the public to answer. Parties can respond by using the consultation questionnaire, which is available on [the HKEx's website](http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2010092q.doc).

Completed questionnaires should be submitted to HKEx no later than 12 November 2010 by one of the following methods:

By mail or hand delivery to:

Corporate Communications Department Hong Kong Exchanges and Clearing Limited 12th Floor, One International Finance Centre 1 Harbour View Street Central Hong Kong Re: Consultation Paper on Proposed Change to Minimum Number of Shareholders for Market Capitalisation/Revenue Test

By tax to:

(852) 2524-0149

By e-mail to:

response@hkex.com.hk Re: CP on Minimum Number of Shareholders

## Appendix - Consultation Questions

Question 1: Should the Exchange remove MB Listing Rule 8.05(3)(f) and make a consequential amendment to MB Listing Rule 8.08(2) to require a minimum number of 300 shareholders for the Market Capitalisation/Revenue Test? Please give reasons for your answer.

Question 2: If your answer to Question 1 is "Yes", do you agree that the MB Listing Rule amendments in Appendix II will implement the proposal? If your answer is "No", please provide reasons and alternate views.

*This note constitutes a summary only of HKEx's Consultation Paper on Proposed Change To Minimum Number of Shareholders For The Market Capitalisation/Revenue Test, which can be viewed on* [*the HKEx's website*](http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2010092.pdf)*.*

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