



Hong Kong

November 2016

HKEX/SFC JOINT CONSULTATION: PROPOSED ENHANCEMENTS TO THE STOCK EXCHANGE OF HONG KONG LIMITED'S DECISION-MAKING AND GOVERNANCE STRUCTURE FOR LISTING REGULATION

The consultation period for the Joint Consultation Paper published by the Hong Kong Securities and Futures Commission (the **SFC**) and the Stock Exchange of Hong Kong Limited (the **Exchange**) closed on Friday, 18 November. Published in June 2016, the Consultation Paper¹ set out proposals to overhaul Hong Kong's IPO application process and strip the existing 28-man Listing Committee of all of its significant decision-making powers. Instead, the regulators proposed establishing two new super-committees, comprising just six and eight persons respectively, both under its effective control. For a detailed summary of the Joint Consultation Paper's proposals, please see Charltons' June newsletter at <http://www.charltonslaw.com/joint-consultation-paper-issued-on-proposed-changes-to-hong-kong-listing-regulation/>.

Charltons submitted its response to the Consultation Paper on 18 November arguing that the proposals would remove vital checks and balances and threaten to extend the SFC's powers beyond its statutory role as the independent regulator of the Exchange and protector of investors' interests. Charltons' response can be viewed at http://www.charltonslaw.com/newsletters/hong-kong-law/en/2016/349/Response_to_Joint_Consultation16_11-2.pdf.

While Charltons welcomes the regulators' efforts to ensure the quality and efficiency of the Hong Kong market, its response argues this will not be enhanced by the significant regime changes proposed.

Among the key issues identified are:

- The Consultation Paper's stated objectives are achievable under the existing regime
- The case for the proposed reforms has not been made out
- Legislative changes may be needed for the proposed extension of SFC powers
- Lost checks and balances would deprive listing applicants of existing rights of appeal.

The submission highlights, as a key concern, that the proposed extension of the SFC's powers to reject applications for listing on the Exchange will also deprive applicants of the right of appeal to the Securities and Futures Appeals Tribunal, the independent body responsible for ensuring that the SFC's powers are exercised reasonably and fairly.

The submission also says that the SFC's proposed extended powers run counter both to the Exchange's role as the market's front-line regulator and the SFC's role as the independent regulator of the Exchange. Proposals to put SFC executives on the proposed Exchange decision-making committee, the Listing Regulatory Committee, would further create an inherent conflict between the SFC's proposed role in decision-making and its function as regulator of the Exchange.

¹ SFC/HKEX Joint Consultation Paper at <http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201606.pdf>.

Charltons does not see how the proposed reforms would enhance and contribute to continuous market development in response to market demand. While it appreciates the regulators' concerns regarding abusive practices surrounding shell companies, it considers that the regulators should refocus on increasing robust enforcement of existing provisions to curb back-door listings and price manipulation. It also suggests that shell companies may be best dealt with by a more efficient de-listing process to remove them from the market and that this would be a better solution than subjecting all listing applicants, or at least all SME applicants, to the highly subjective process of screening for prospective shells at the listing application stage.

The firm does not consider that the Consultation Paper has adequately established the need for the proposed major reforms. On the contrary, the proposals could stifle market development and undermine the Exchange's competitiveness and risk making the listing application process more complicated and expensive. This must be avoided if the competitiveness of the Exchange as an international fund raising platform is to be maintained and enhanced.

It is essential that the SFC remains operationally independent of the Exchange so that there is no blurring of the lines between the Exchange as decision-maker and the SFC as regulator. Charltons acknowledges the different views as to how the regulators' objectives are best achieved, and considers that whatever the outcome, the market will benefit from the debate.

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