

CHARLTONS
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HKEX CONSULTATION PAPER ON GEM LISTING REFORMS

INTRODUCTION AND OVERVIEW OF THE PROPOSED GEM LISTING REFORMS

Key proposals of HKEX's Consultation Paper published on 26 September 2023

New alternative financial listing eligibility test

Streamlined transfer mechanism

Removal of mandatory quarterly reporting requirement

Aligning certain GEM Listing Rules with those of Main Board

BACKGROUND TO CURRENT GEM MARKET

History of GEM reforms

- 1999 - Launch of HK Growth Enterprise Market as capital-raising platform for emerging growth companies
- Lower admission criteria than the Main Board: 2 years of active business pursuits, but no financial tests
- Adopted “buyer beware”, light touch regulation based on “enhanced disclosure”
- GEM administered separately from Main Board: separate Listing Rules and GEM Listing Committee
- Benefitted from “dot com” boom of 1999 and 2000 + listings of Mainland companies unable to meet “4-5-6” rule for listing Mainland companies on overseas main markets
- In 2000 + 2001, GEM listed more companies than the Main Board
- 12 GEM-listed companies transferred to the Main Board between 1999 + 2005
- GEM listings declined when dot com boom ended



BACKGROUND TO CURRENT GEM MARKET

History of GEM reforms

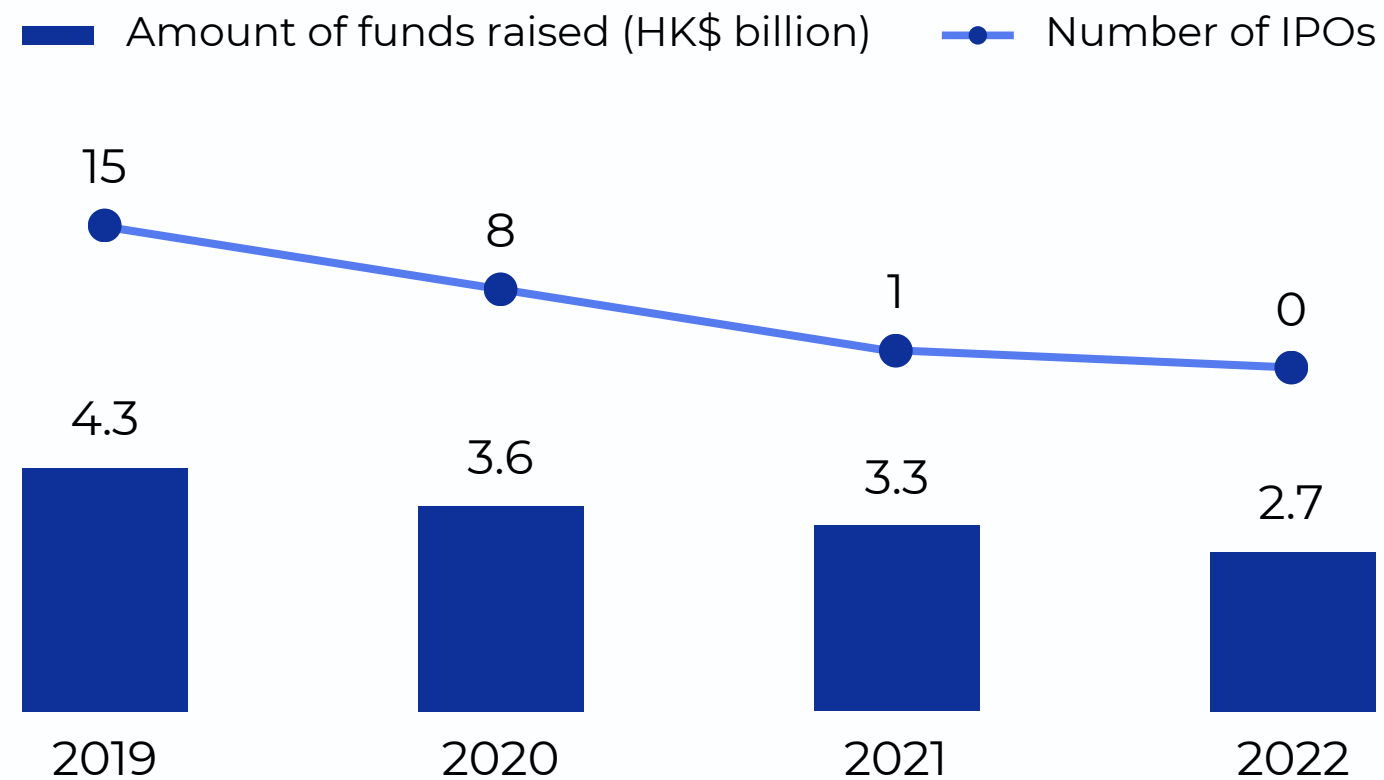
- In 2006, GEM Discussion Paper set out 3 options for GEM - respondents' preferred option was a new, light touch market modeled on London's AIM market
- July 2008, HKEX repositioned GEM as a stepping stone to Main Board listing with higher GEM admission requirements: HK\$20 mln cash flow over 2 financial years before listing and expected market cap. of HK\$100 mln at listing
- July 2008 repositioning introduced streamlined process for transferring to the Main Board removing need to appoint a sponsor or publish "prospectus standard" listing document
- February 2018, GEM repositioned as a stand-alone board for small + mid-sized companies
- Repositioning raised GEM admission criteria to HK\$30 mln cash flow + HK\$150 mln expected market cap. at listing
- Streamlined transfer process removed + new requirement for public offering of 10% of offer shares
- 2020 market consultation on raising the Main Board profit requirement - respondents raised concerns re. GEM's viability as a listing venue for SMEs



BACKGROUND TO CURRENT GEM MARKET

RECENT GEM LISTING PERFORMANCE

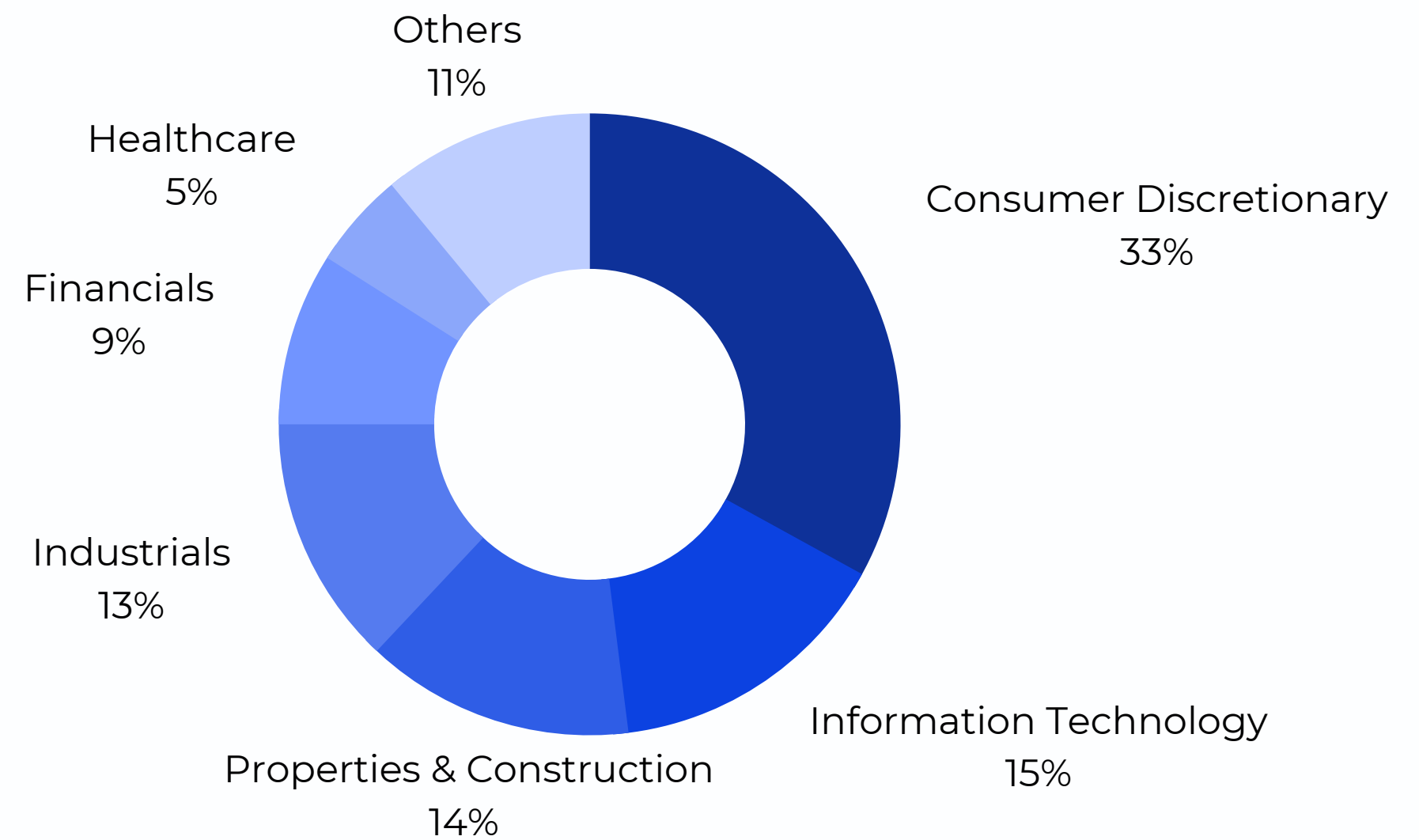
Number of IPOs and funds raised (IPO and post-IPO) on GEM since 2019



Source: HKEX

Note: The amount of funds raised included IPO financing raised by way of subscription, sales and placing, and post-IPO fundraising.

GEM industry distribution as at 31 December 2022

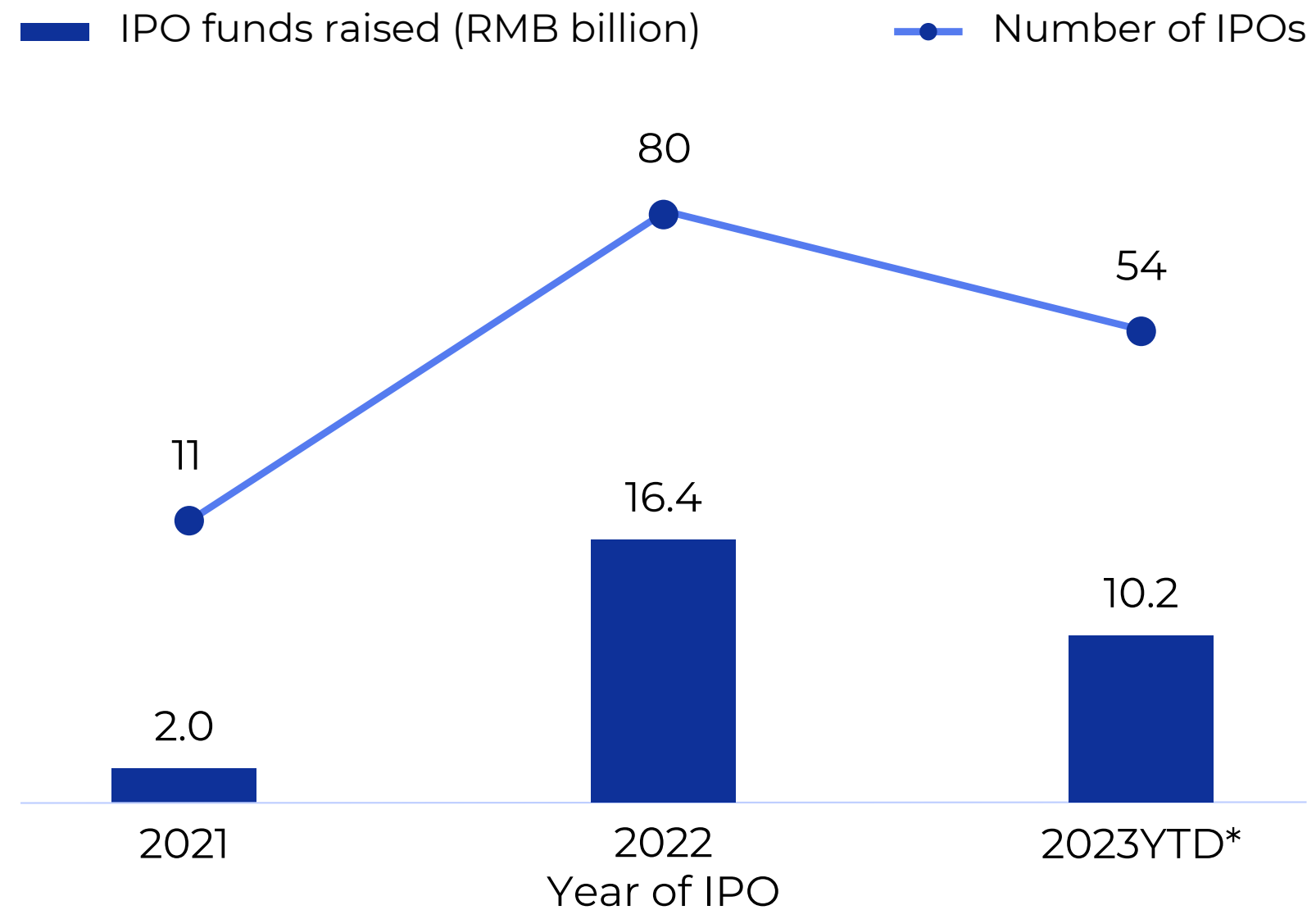


Source: HKEX and Hang Seng Indexes Company Limited

Note: Based on the industry classification of GEM issuers under the Hang Seng Industry Classification System as at 31 December 2022.

BACKGROUND TO CURRENT GEM MARKET

HKEX attributes decline in GEM listings to impact of COVID-19 + greater choice of listing venues for Mainland SMEs



Source: BSE website and WIND (as August 2023)

Note: Excluding transfers from the NEEQ Select Market at the BSE's launch.

* Up to 31 August 2023.

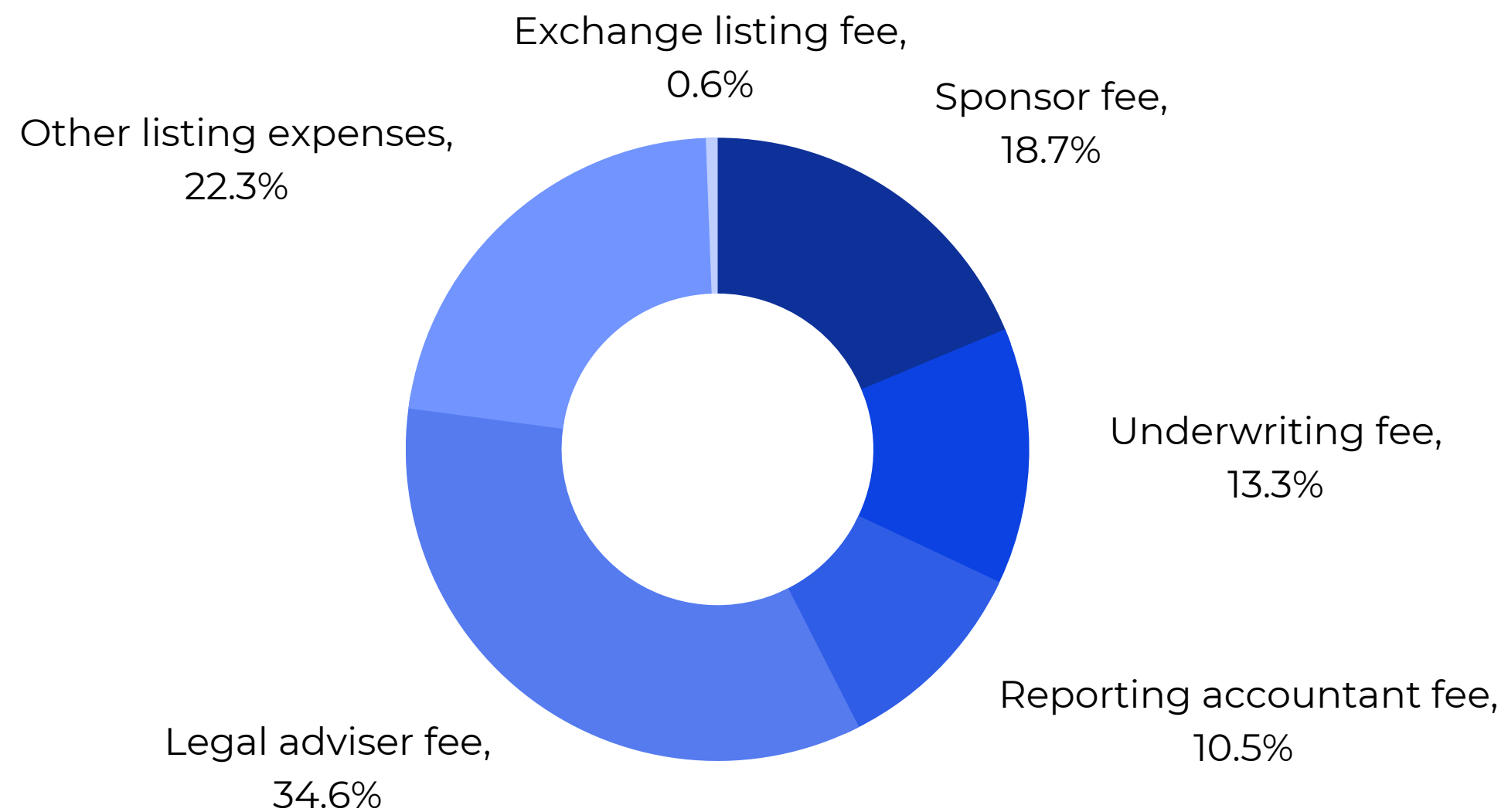
STAKEHOLDER FEEDBACK

- In the 2020 MB profit consultation, concerns were raised about GEM's viability as a listing platform for SMEs and traditional companies.
- Stakeholder engagement: Industry associations, professional bodies, + industry practitioners (law firms, sponsor firms, and investment managers in Hong Kong)
- Feedback also sought from Mainland institutional SME investors
- Key issues raised:
 - existing eligibility requirements
 - alternative eligibility requirements
 - continuing obligations
 - transfers to the Main Board
 - cost of listing



STAKEHOLDER FEEDBACK

Average listing expenses of GEM listing applicants between 2018 and 2022



Source: HKEX's internal analysis of GEM listing applicants' submissions to the Exchange



OVERVIEW OF THE HKEX GEM LISTING RULE AMENDMENTS AND GEM REFORMS

Initial listing requirements

Continuing obligations

Transfers to the Main Board



INITIAL LISTING REQUIREMENTS

Proposed new alternative financial eligibility test for GEM listing

Current GEM listing requirements	Proposed alternative financial eligibility test (the Market Capitalisation / Revenue / R&D Test)
<p>A GEM listing applicant is required to have:</p> <ul style="list-style-type: none">• an expected market capitalisation of at least HK\$150 million at the time of listing +• positive cash flow generated from operating activities of at least HK\$30 million in aggregate for the 2 financial years prior to listing	<p>A GEM listing applicant under the new test is required to have:</p> <ul style="list-style-type: none">• market capitalisation of at least HK\$250 million at the time of listing• an adequate trading record of at least 2 financial years• revenue of at least HK\$100 million in aggregate for the 2 financial years immediately preceding the issue of the listing document, + year-on-year revenue growth over the 2 financial years;• expenditure on R&D of at least HK\$30 million in aggregate for the 2 financial years immediately preceding the issue of the listing document; and• expenditure on R&D to be at least 15% of its total operating expenditure for each of the 2 financial years immediately preceding the issue of the listing document

INITIAL LISTING REQUIREMENTS

Proposed reduction of post-IPO lock-up period for controlling shareholders

Purpose of current pre-IPO 24 month lock-up period was to address shell activities and to require controlling shareholders to demonstrate a stronger commitment to the GEM issuer

Current post-IPO lock-up period on controlling shareholders	Proposed post-IPO lock-up period on controlling shareholders
<p>Controlling shareholders are prohibited from:</p> <ul style="list-style-type: none">• disposing of any shares within the first 12 months after listing +• disposing of shares that would result in them ceasing to be the controlling shareholders within the second 12 months after listing	<p>Controlling shareholders will be prohibited from:</p> <ul style="list-style-type: none">• disposing of any shares within the first 6 months after listing +• disposing of shares that would result in them ceasing to be the controlling shareholders within the second 6 months after listing

CONTINUING OBLIGATIONS

Proposed removal of requirement for a compliance officer

Proposal to shorten period of engagement of compliance adviser +
to remove certain existing responsibilities

CONTINUING OBLIGATIONS

Amendments to the periodic reporting requirements

Current requirement	Proposed requirement
<p>GEM issuers are required to publish:</p> <ul style="list-style-type: none"> • annual reports not later than 3 months after the end of each financial year • half-year reports not later than 45 days after the end of the first 6 months of each financial year + • quarterly reports not later than 45 days after the end of a quarter <p>GEM issuers are required to publish preliminary announcement of results:</p> <ul style="list-style-type: none"> • for the financial year, not later than 3 months • for the first 6 months of each financial year, not later than 45 days + • for each of the first 3-month and 9-month periods of each financial year, not later than 45 days, after the date on which the financial period ended. 	<p>GEM listed companies will be required to publish:</p> <ul style="list-style-type: none"> • annual reports not later than 4 months after the end of each financial year + • interim reports not later than 3 months after the end of the first 6 months of each financial year <p>No quarterly financial reporting will be required, but this may be done on a voluntary basis and would be a recommended best practice under GEM's Corporate Governance Code</p> <p>GEM-listed companies will be required to publish preliminary announcement of results:</p> <ul style="list-style-type: none"> • for the financial year, not later than 3 months + • for the first 6 months of each financial year, not later than 2 months, after the date on which the financial period ended.

CONTINUING OBLIGATIONS

Possible amendments to ESG-related requirements

- Current ESG reporting requirements are the same for both GEM issuers and Main Board issuers
- HKEx considers that limited resources may limit GEM issuers' ability to meet ESG reporting requirements
- HKEx will take a measured approach in implementing ESG-related requirements for GEM issuers that are proportionate to their circumstances
- HKEx will further update the market on this topic in due course



TRANSFERS TO THE MAIN BOARD

Proposed new streamlined transfer mechanism

Proposed removal of requirement to appoint a sponsor to carry out due diligence

Proposed removal of requirement for a “prospectus-standard” listing document



TRANSFERS TO THE MAIN BOARD

Proposed removal of requirement for a “prospectus-standard” listing document

Under the proposal, GEM issuers will no longer be required to produce a “prospectus-standard” listing document. Instead, they will be required to submit at least the following documents:

- a formal application for listing
- a Long-Form Announcement to be pre-vetted by HKEx +
- a working capital sufficiency statement with relevant supporting information

Contents of the Long-Form Announcement include:

- | | |
|--|--|
| (a) a prescribed form disclaimer statement; | (f) a statement that the requisite approval has been granted by the HKEx; |
| (b) directors' responsibility statement; | (g) issuer's stock codes on GEM + the Main Board; |
| (c) confirmation of fulfilment of all pre-conditions to transfer of listing; | (h) a statement of CCASS eligibility; |
| (d) reasons for the transfer of listing; | (i) if applicable, a statement of any listing of options, warrants etc., that will be transferred together with the underlying securities; |
| (e) a statement that various documents are displayed on the HKEx's website and the issuer's website; | (j) names of the directors; and |
| | (k) such information as may be directed by the HKEx. |



TRANSFERS TO THE MAIN BOARD

Proposed daily turnover test

The Stock Exchange proposes that the daily turnover of a transfer applicant must have reached a minimum threshold on at least 50% of the trading days over the 250 trading days immediately preceding the transfer application (“**Minimum Daily Turnover Threshold**”) and until the commencement of dealings in its securities on the Main Board (“**Reference Period**”)

The Minimum Daily Turnover Threshold is proposed to be set at either HK\$100,000 or HK\$50,000 (subject to views of respondents)

Effect of the Daily Turnover Test on the Exchange’s issuers based on a Minimum Daily Turnover Threshold of HK\$100,000

Cohort	(i) Eligible GEM Issuers	(ii) GEM Transfers		
		Number of issuers	%	%
Pass	3	50%	28	65%
Fail	3	50%	15	35%
TOTAL	6	100%	43	100%

Source: HKEX and S&P Capital IQ (as of 31 August 2023)

Effect of the Daily Turnover Test on the Exchange’s issuers based on a Minimum Daily Turnover Threshold of HK\$50,000

Cohort	(i) Eligible GEM Issuers	(ii) GEM Transfers		
		Number of issuers	%	%
Pass	5	83%	34	79%
Fail	1	17%	9	21%
TOTAL	6	100%	43	100%

Source: HKEX and S&P Capital IQ (as of 31 August 2023)

TRANSFERS TO THE MAIN BOARD

Proposed volume weighted average market capitalisation test

The Stock Exchange proposes that the transfer applicant must have a volume weighted average market capitalisation over the Reference Period that meets the minimum capitalisation requirement for listing on the Main Board.

The volume weighted average market capitalisation test will take into account the number of shares traded on each trading day during the Reference Period in a manner ensuring that the valuation on trading days where trading volume is relatively high will have a more significant contribution to the average market capitalisation than the valuation on trading days where trading volume is relatively low



TRANSFERS TO THE MAIN BOARD

Other matters

The HKEX has also proposed the following:

(a) compliance record: the transfer applicant must have a clean compliance record without serious Listing Rule breaches in the 12 months prior to its transfer application and no ongoing HKEX investigations or disciplinary proceedings for serious Listing Rule breaches

(b) approval authority: the application under the Streamlined Transfer Mechanism will be processed by the HKEX Listing Division and approved by the HKEX Listing Committee +

(c) GEM issuers not qualified for a streamlined transfer: a GEM issuer that does not meet the Streamlined Transfer Mechanism requirements must apply for a transfer under the existing requirements (i.e. which include requirements to appoint a sponsor and to publish a “prospectus-standard” listing document)

TRANSFERS TO THE MAIN BOARD

Costs for transfers of listing

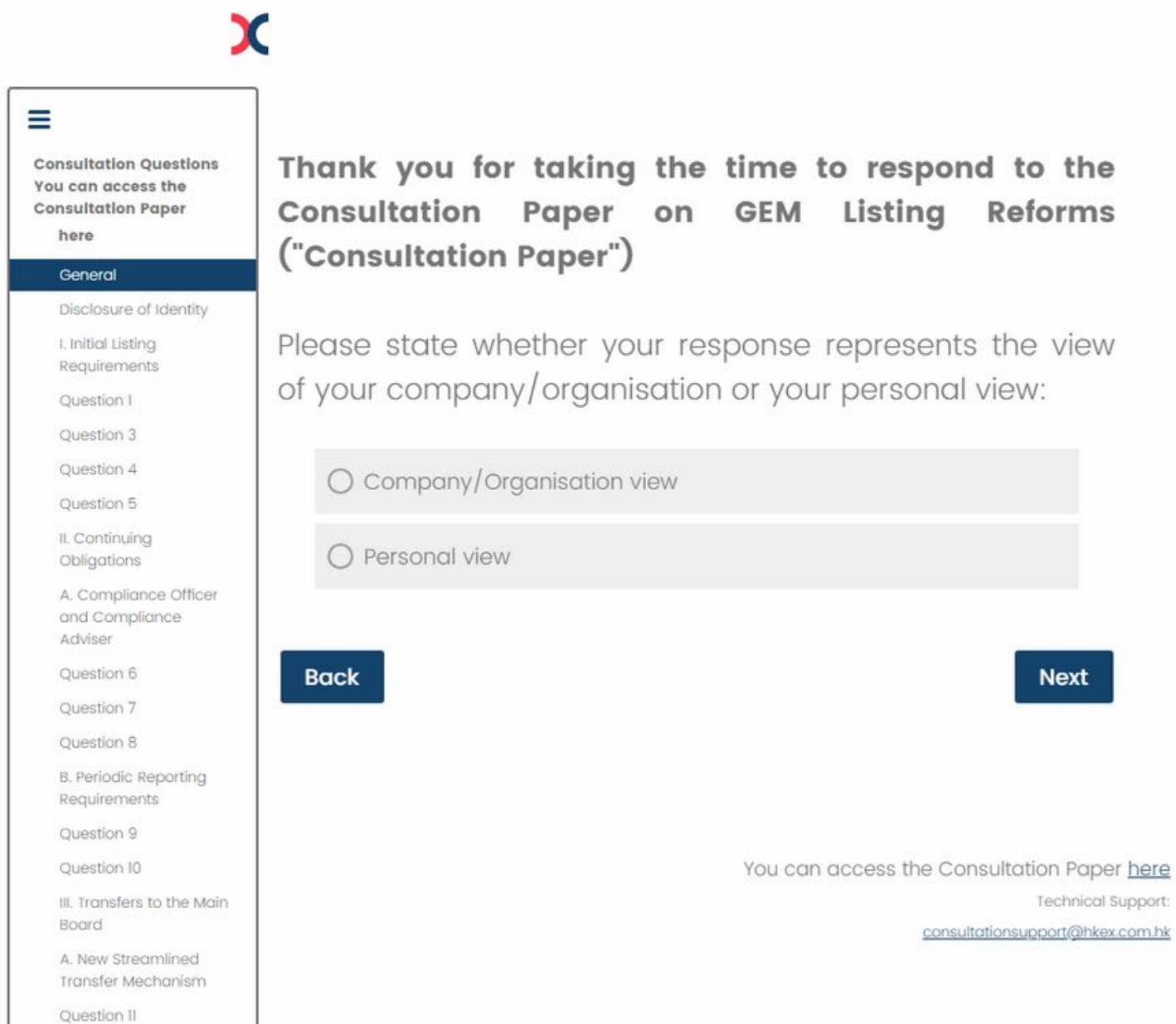
The HKEx proposes to exempt GEM transferees to the Main Board from the Main Board initial listing fee currently required under the Main Board Listing Rules, Appendix 8, paragraph 1.

The proposed fee exemption aims to address stakeholders' concerns regarding listing costs



RESPONDING TO THE HKEX CONSULTATION

Interested parties can respond to the consultation by completing and submitting the questionnaire available on the HKEx's website by **6 November 2023**.



The screenshot shows a web interface for a consultation questionnaire. On the left is a navigation menu with a hamburger icon and a list of sections: 'General', 'I. Initial Listing Requirements' (with sub-items Question 1-5), 'II. Continuing Obligations' (with sub-items A. Compliance Officer and Compliance Adviser, Question 6-8), 'B. Periodic Reporting Requirements' (with Question 9), 'III. Transfers to the Main Board' (with sub-item A. New Streamlined Transfer Mechanism, Question 10), and 'Question 11'. The main content area features the HKEX logo at the top, followed by a thank-you message: 'Thank you for taking the time to respond to the Consultation Paper on GEM Listing Reforms ("Consultation Paper")'. Below this is a prompt: 'Please state whether your response represents the view of your company/organisation or your personal view:'. Two radio button options are provided: 'Company/Organisation view' and 'Personal view'. At the bottom of the main area are 'Back' and 'Next' buttons. At the very bottom, there is a link to the Consultation Paper and technical support contact information: 'Technical Support: consultationsupport@hkex.com.hk'.



OTHER EXCHANGES REFERENCED BY THE HKEX

Beijing Stock Exchange (BSE)



Nasdaq Capital Market



Catalist



AIM



SUMMARY

- Consultation Paper published by HKEx on 26 September 2023
- Third major proposed reform to GEM since launch in 1999
- Proposed GEM listing reforms:
 - alternative test for initial listing
 - revised continuing obligations
 - re-introduction of streamlined transfer process to the Main Board

