

The introduction of the AMS/3⁹⁵ and internet initial public offering (“iIPO”) also made it easier for investors to invest through the internet, freeing them from geographical restriction. In the last quarter of 2000, SEHK launched AMS/3⁹⁶ and it was implemented in several phases. The AMS/3 introduced three major features: multi-workstation system (“MWS”); open gateway (“OG”); and order routing system.⁹⁷ In January 2010, HKEx introduced AMS/3.5 which has doubled the order processing capacity to 3,000 per second, with the average latency reduced to 0.15 second.⁹⁸

The order routing system will enable investors to trade Hong Kong stocks from anywhere in the world using computers or mobile phones through the internet⁹⁹ and it was implemented in February 2001. The iIPO service was also introduced in 2000 to allow individual investors to submit applications for initial public offering through an electronic mechanism.¹⁰⁰ Investors can directly access the iIPO service over the internet without using a CCASS terminal.¹⁰¹

On 1 January 2010, the free real-time basic market prices website service (or free prices website service) was officially launched to expand dissemination of Hong Kong securities market information and raise the Hong Kong securities market’s profile in the PRC.¹⁰² It was later re-packaged into basic market prices service (“BMP Service”), a standard market data service under the vendor licensing regime for all interested information vendors beginning 1 April 2011.¹⁰³

The trading, clearing, and settlement system is constantly improving with the advent of technology.

¶1-057 Free Market

With zero capital flow restrictions, tax advantages, currency convertibility, and free transferability of securities, Hong Kong provides an attractive market for both investors and issuers.

of the Hong Kong Securities and Futures Market Economy, Note, Room Document 8 of Fourth Round Table on Capital Market Reform in Asia in Tokyo organised by Organization For Economic Cooperation and Development, 9-10 April 2002, note 4).

⁹⁵ The Automatic Order Matching and Execution System (AMS) was first launched in Nov. 1993. HKEx, *Fact Book 1999*. AMS/3 is the third generation of AMS.

⁹⁶ HKEx, *HKEx Fact Book 2000*.

⁹⁷ Id.

⁹⁸ HKEx, *HKEx Fact Book, 2010*.

⁹⁹ Id.

¹⁰⁰ Id.

¹⁰¹ Id.

¹⁰² HKEx, *HKEx Fact Book 2009*.

¹⁰³ HKEx, *HKEx Fact Book 2010*.

¶1-058 Hong Kong as an Investment Window to the World

In order to establish Hong Kong as an international financial centre, HKEx has tried vigorously to forge alliances with stock exchanges all over the world through signing memoranda of understanding.¹⁰⁴

HKEx also began negotiating on a cooperative plan of global equity market partnership with nine Equity Exchanges in 2000 under the global equity market partnership¹⁰⁵ and explored with NYSE in 2001 a possible linkage between NYSE, HKEx, and the Toronto Stock Exchange.¹⁰⁶ Such link-up will create greater global liquidity, facilitate global price recovery, and provide investors with better access to global stocks.

In May 2000, SEHK introduced a pilot programme for trading US securities. Based on this programme, NASDAQ and the SEHK signed an agreement on exchange of regulatory information. Seven established securities listed on NASDAQ were quoted on SEHK.¹⁰⁷

In 2000, GEM was recognised by the US Securities and Exchange Commission as a designated offshore securities market. Consequently, all GEM listed shares may generally be resold without restriction to US and non-US persons in and outside the US.¹⁰⁸

In the same year, HKFE also obtained the approval of the US Commodity Futures Trading Commission to place HKATS terminals and automated order routing systems connected to HKATS in the US.¹⁰⁹ This would expand the trading network of HKFE’s product to the US market.¹¹⁰ Futures exchange participants can provide online trading to their customers and in August 2001, SFC approved investors outside Hong Kong the direct access to its derivatives market.¹¹¹

¹⁰⁴ Recent examples include signing a Memorandum of Understanding with the Australian Stock Exchange to exchange market surveillance information in 2000 (See HKEx, *HKEx Fact Book 2000*), entering into a strategic initiative with the Sydney Futures Exchange to explore development of a range of new derivatives trading and clearing services for the Asia exchange-traded and OTC market places in 2001 and separately signing with the Stock Exchange of Thailand and the Kuala Lumpur Stock Exchange on the exchange of market information. (See HKEx, *HKEx Fact Book 2001*)

¹⁰⁵ HKEx News Release, *Ten Leading Equity Exchanges Jointly Announce Global Equity Market Partnership Talks*, 7 June 2000 at <http://www.hkex.com.hk/eng/newsconsul/hkexnews/2000/0607news.htm> and NYSE, *US Regulation of The International Securities and Derivative Markets (9th ed., Edward F. Greene et al eds., Aspen Publishers, 2006) Volume One §10.03[3]* although none of the linkages between the NYSE and the foreign exchanges is currently in operation. The nine equity Exchanges are New York, Tokyo, Australia, Euronext (including Amsterdam, Brussels and Paris), Toronto, Mexico and Sao Paulo. The ten exchanges (including Hong Kong) participating in this plan are the major securities markets of three time zones of Asia-Pacific (Australia, Tokyo and Hong Kong), Europe (Euronext, the combined Amsterdam, Brussels and Paris exchanges) and America (Sao Paulo, Mexico and Sao Paulo).

¹⁰⁶ HKEx, *HKEx Fact Book 2001*.

¹⁰⁷ HKEx, *HKEx Fact Book 2000*.

¹⁰⁸ Id.

¹⁰⁹ Id.

¹¹⁰ Id.

¹¹¹ HKEx, *HKEx Fact Book 2001*.

On 3 March 2003, Hong Kong was admitted as a signatory of the IOSCO multilateral memorandum of understanding to enhance a regulatory cooperation and information sharing among signatories. Signatories include the US, the UK, Australia, and Canada.¹¹²

Such global network is very useful for the PRC companies listed on HKSE. Hong Kong also has close cooperation with the PRC. In 1993 and 1995, an agreement concerning regulatory cooperation was signed between SFC and CSRC respectively.¹¹³ In 2001, HKEx signed an agreement with SSE and SZE for mutual exchange of market and listed company information.¹¹⁴ A China Stock Market website was integrated in the existing websites of HKEx, SSE and SZE in November 2001.¹¹⁵ Through this cooperation, all three exchanges will be able to provide investors with comprehensive data on the three securities markets at a centralised location.¹¹⁶

HKEx has a proven record of launching PRC-related securities but it has not yet developed a successful PRC-related derivative product. HKEx has announced the launch of H share index on 8 December 2003.¹¹⁷ The first A share index in Hong Kong, Hang Seng China A Industry Top Index, was launched in September 2009.¹¹⁸ HKSE has also signed an agreement with Shanghai's futures market to develop energy futures.¹¹⁹ Hong Kong provides an important venue to promote and market the PRC and PRC-related securities.

¶1-059 Significant Human Resources in Hong Kong

Human resources are the foundation stone of a knowledge-based economy.¹²⁰ Hong Kong can provide a valuable source of human capital in a range of professions including lawyers, accountants, businessmen, bankers, regulators, and judges.¹²¹

There are eminent people of solid international financial expertise in Hong Kong who have already been spotted internationally and by the Chinese Government. For instance, Anthony Neoh, during his employment as a former Chairman of SFC, had been elected, in September 1996, Chairman of the Technical Committee of IOSCO, a committee that develops uniform regulatory standards for developed markets. He held this post until 1998. He was later invited by Premier Zhu Rongji in late 1998 to serve as

¹¹² HKSFC, *Annual Report 2002-03: New Regulatory Framework, Better Quality of Market: Enforce the Law, Protect Investors*, HKSFC, 2003.

¹¹³ HKSFC, *Annual Report 96/97: A Strategic Outlook for the Future*, HKSFC, 1997.

¹¹⁴ HKEx, *HKEx Fact Book 2001*.

¹¹⁵ Id.

¹¹⁶ Id.

¹¹⁷ Enoch Yiu, *HKEx to Introduce H-share Index Futures*, SCMP, 23 October 2003.

¹¹⁸ HKEx, *HKEx Fact Book, 2009*.

¹¹⁹ Enoch Yiu, *HKEx Snubs International Pacts to Focus on China*, SCMP, 2 June 2003.

¹²⁰ The Financial Secretary, The Hon. Antony Leung, address moving the Second Reading of the Appropriation Bill 2003, para. 32 at <http://www.budget.gov.hk/2003/eng/speech.htm>.

¹²¹ Eric Ng & Hui Yuk-Min, *State-Run Enterprises Seek Executive Overseas*, SCMP, 17 September 2003.

the Chief Adviser of CSRC.¹²² In February 2001, CSRC appointed Laura Cha, former Deputy Chairman of SFC, as Vice-Chairman in charge of corporate governance.¹²³ On 22 November 1999, former Chairman of SFC, Andrew Sheng, was appointed to chair the Financial Stability Forum Task Force on Implementation of Standards to examine ways of fostering the implementation of international standards relevant to the strengthening of financial systems.¹²⁴ Charles Li, the Chief Executive since 2010, was the President of Merrill Lynch China and Chairman of JP Morgan China and has been the Director of the China Entrepreneurs Forum since 2005 and is a consulting member of Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone of Shenzhen. He is familiar with the PRC capital market.

Hong Kong is reinventing itself as a knowledge-based and technology-intensive economy.¹²⁵ As an international financial centre, multinational business activities have also led to the spread of knowledge and advanced technology and the cross-fertilisation of business cultures. The latest figures of the Hong Kong Government show that 13% of the labour force in Hong Kong are employed by multinational companies.¹²⁶

SFC, HKSE, and HKFE have on-going programmes for executives of H share companies on the regulatory system, listing rules, take-over and mergers rules, and investor relations.¹²⁷

¶1-060 Alternative Methods for PRC Companies to be Listed on the Hong Kong Stock Exchange

¶1-061 Red Chip Companies

Other than direct overseas listing by means of H shares on HKSE, PRC companies can raise funds by indirect overseas listing through red chip companies.

As said earlier, the first H shares company was Tsingdao Beer Company Limited listed in June 1993, and the first Red Chip company to be incorporated in Bermuda was Brilliance China Automotive Holdings Ltd ("Brilliance China"), one of the largest automobile manufacturers in Northeast China at the time. It was listed on NASDAQ in 1992.¹²⁸ The company underwent a complicated restructuring for the listing and seeing

¹²² Press Release from Chinese University of Hong Kong at <http://www.cuhk.edu.hk/cpr/pressrelease/Anthony%20Neoh-e.htm>.

¹²³ Jamie Allen & Francois Roy, *Corporate Governance in Greater China: A Comparison between China, Hong Kong and Taiwan in Structuring for Success – The First 10 Years of Capital Markets in China* (Asia Law & Practice ed., Asia Law & Practice, 2001).

¹²⁴ HKSFC, *Annual Report 99/20: Technology and Markets*, HKSFC, 2000.

¹²⁵ The Financial Secretary, The Hon. Donald Tsang, *The 2000-01 Budget: Scaling New Heights*, address moving the Second Reading of the Appropriation Bill 2000, para. 53 (8 March 2000) at <http://www.budget.gov.hk/2000/eindex.htm>.

¹²⁶ The Financial Secretary, The Hon. Donald Tsang, *The 2000-01 Budget: Scaling New Heights*, address moving the Second Reading of the Appropriation Bill 2000, para. 60 (8 March 2000) at <http://www.budget.gov.hk/2000/eindex.htm>.

¹²⁷ Id.

¹²⁸ Brilliance China Automotive Holdings Ltd was also later listed on HKSE by introduction in October 1999.

such a structure enabled the company to list successfully, many other SOEs followed suit. Soon after the public offering and listing by Brilliance China, the red chip phenomenon exploded.¹²⁹ It is a way for China's entrepreneurs to raise capital through public offering of the shares of an overseas holding company created to hold assets and business operations based exclusively within the PRC.

Red chip companies are predominately diversified conglomerates which have grown rapidly due to the asset injection from parent companies in the PRC. They include China Mobile Limited ("China Mobile"), Beijing Enterprises Holdings Ltd, China Everbright Limited, Shanghai Industrial Holdings Limited, China Resources Enterprise, and "window-companies" or "International Trust and Investment Corporations ("ITICs")" of provincial governments. They are incorporated outside the PRC but their businesses are based in the PRC and controlled directly or indirectly by the central, municipal, or provincial governments of the PRC.

The list of red chip companies on the Main Board provided by HKSE can be dated back to 1972, with CITIC 21CN Co Ltd being the earliest listed on 6 July 1972, to be followed by Shenzhen International Holdings Limited listed later in the same year.¹³⁰ However, most of the larger red chip companies in terms of market capitalisation listed after 1992. In terms of market capitalisation, China Mobile is at the top of the list with HK\$1,628,173,240,200 as at 30 June 2013 and it was also the first red chip company that returned home and issued A share listed on a Mainland stock market after registering and listing aboard.

Strictly speaking, red chip companies did not fall within the jurisdiction of the PRC authorities. However, in June 1997, CSRC in conjunction with the State Council introduced the Notice Concerning Further Strengthening Administration of Share Offering and Listing Overseas ("国务院关于进一步加强对在境外发行股票和上市管理的通知", commonly known as "Red Chips Guidelines")¹³¹ to prevent the dissipation of State assets. The PRC Government was worried that State assets would be injected into red chip companies and that they might be sold off indirectly to overseas investors at a discount. The Red Chip Guidelines provide more stringent requirements for reporting to, and obtaining approval from, the Chinese authorities. Chinese shareholders who control foreign listed companies or Chinese shareholders who intend to inject assets to red chip companies are either required to report to CSRC or alternatively required to obtain consent from their local provincial governments or relevant department of the State Council depending on their circumstances.¹³²

¹²⁹ Anthony Neoh, *How China's Companies Use International Regulation* (CUHK Business School) at <http://www.baf.cuhk.edu.hk/program/article.aspx?id=C336566F590F>.

¹³⁰ HKEx, List of Red Chip Companies (Main Board) at http://www.hkex.com.hk/eng/stat/smstat/chidimen/cd_rcmb.htm (updated: 30/06/2013).

¹³¹ Notice promulgated by State Council Concerning Further Strengthening Administration of Share Offering and Listing Overseas [*Guanyu Jinyibu Jiajiang zai Jingwai Faxing Gupiao he Shengshi Guanli de Tongzhi*] (20 June 1997 *Guofa* [1997], effective as of the same day).

¹³² Red Chip Guidelines, paras. 1, 2 & 3.

Backdoor Listing

A red chip company can be formed by means of backdoor listing.¹³³ In the early stage of the development, a number of PRC companies bypassed the official listing channels through reverse take-over or commonly known as "backdoor listing."¹³⁴ Backdoor listing is the acquisition of a listed company (typically a company which is no longer profitable with little or no activity) as a shell company by an unlisted company to gain a listing on the securities exchange. It happens where a listed company acquires a non-listed company's assets or shares, and the value of the acquired assets, based on the criteria set by each stock exchange, is larger than the acquirer's original assets, resulting in a change in the control of the listed company to major shareholders of the non-listed company. As a result, it allows companies that may not be able to meet the listing requirements of HKSE to be listed on it and it will also enable the private companies to be listed on HKSE much faster than the one who has to go through the listing procedures formally.

On 30 January 2004, HKEx announced a number of changes to the Main Board Rules which came into effect on 31 March 2004. Among them, reverse takeovers have been added as a new category of notifiable transactions, making it more difficult to achieve backdoor listings.¹³⁵ Such notifiable transaction requires notification and approval from HKEx, approval from the shareholders, an accountant's report on the preceding three financial years on the business or companies acquired, publication on the newspaper and circular to the shareholders.¹³⁶ With the new amendments, backdoor listing or reverse takeovers will be treated as new listing.¹³⁷

Rule 14.06(6) defines "reverse takeover" as:

"[a]n acquisition or a series of acquisitions of assets by an issuer which, in the opinion of the Exchange, constitutes, or is part of a transaction or arrangement or series of transactions or arrangements which constitute, an attempt to achieve a listing of the assets to be acquired and a means to circumvent the requirements for new applicants set out in Chapter 8 of the Exchange Listing Rules."

A "reverse takeover" normally refers to:

- "an acquisition or a series of acquisitions (aggregated under Rules 14.22 and 14.23)¹³⁸ of assets constituting a very substantial acquisition where there is, or

¹³³ Dongwei Su, *Chinese Stock Markets – A Research Handbook* 54 (World Scientific, 2003).

¹³⁴ See HKEx Listing Rules, rule 14.06(6) for a detailed definition of "reverse takeover."

¹³⁵ HKEx, *Note to Subscribers for the Amendments to the Rules Governing the Listing of Securities – Update No. 80* (31 March 2004).

¹³⁶ Main Board Rule 14.33.

¹³⁷ Main Board Rules 14.54 – 57.

¹³⁸ Referring to the Main Board Rules.

- HKEx no longer requires title certificates for Mainland properties for other issuers, irrespective of their place of incorporation. Instead, HKEx expects the issuers to disclose the risks to their operations of not having Title Certificates for Mainland properties in their listing document, and it will consider each case based on the guidance and circumstances of each case.²⁹⁰

The 2010 guidance letter is a relaxation of the rule laid down by the Clarification on Requirements for Land Use Title of Properties Situated in the Mainland of the People's Republic of China dated 25 March 1998, which requires issuers which are not infrastructure project companies or property companies to produce title certificates for Mainland properties that are crucial to their operations.²⁹¹ Since other markets also allow issuers to disclose, as a risk factor in their listing document, that they do not have long-term title certificates, HKEx, does not, therefore, insist on the production of such title certificates for issuers which are not infrastructure project or property companies. Practice Note 12 of the Main Board Rules also provides that where the issue of a land use right certificate is pending, a properly approved land grant or land transfer contract in writing, together with a PRC legal opinion as to the validity of the approval may be acceptable as evidence of a transferee's pending title to the land to be granted or transferred.

Non-Competition (Main Board Rules 8.10 & 19A.14)

In accordance with the Main Board Rules 8.10 and 19A.14, where a new applicant has a controlling shareholder²⁹² with an interest in a business apart from the applicant's business, which competes or is likely to compete, either directly or indirectly, with the applicant's business, full disclosure is required. Directors should also be reminded that they have their common law duties of not having any conflict of interests with the company, whether it is real or potential.

State-run enterprises were all owned by the State and after the open door policy and the restructuring of SOEs, many of such enterprises became more independent and commercially oriented. Enterprises operated by Government departments will then become competitive. HKSE will normally not consider a PRC Government body as a controlling shareholder of a PRC issuer. A PRC Government body is defined in the Listing Rules of HKSE as the PRC Central Government, PRC provincial-level governments, and PRC local governments immediately under the PRC provincial-level governments.²⁹³ However, entities under the PRC Government that are engaging in

²⁹⁰ HKEx Guidance Letter (HKEx-GL19-10 (July 2010)).

²⁹¹ See also Listing Decision HKEx-LD10-3.

²⁹² "Controlling Shareholder" means any shareholder or other person or group of persons together entitled to exercise, or control the exercise of 30% (or such other amount as may from time to time be specified in the applicable PRC law as being the level for triggering a mandatory general offer or for otherwise establishing legal or management control over a business enterprise) or more of the voting power at general meetings of the issuer or who is in a position to control the composition of a majority of the board of directors of the issuer. See Main Board Rule 19A.14.

²⁹³ Main Board Rule 19A.14.

commercial business or operating another commercial entity will be excluded from this definition.

Full disclosure requires disclosing facts to demonstrate that the applicant is capable of carrying on its business independently, and at arm's length from the competing business. Under such circumstances, for competitive commercial businesses under the same government department, non-competition agreement may be signed to show that the businesses are not competing with each other (either because their target customers or the products provided are different), and are operated at arm's length. Moreover, in terms of provision of raw materials, production or sales assistance, the controlling shareholder will treat the listed company fairly and reasonably, as its other subsidiaries which are not included in the listed company.

Special Companies: Project and Mineral Companies (Main Board Rule 8.05(B))

There is a specific regime for listing newly formed "project" companies, like infrastructure project companies or mineral companies. For these companies, some listing criteria may be relaxed (eg a shorter trading record period can be accepted), while additional requirements are imposed for disclosure and technical reporting.

Project (Infrastructure Project) Companies (Main Board Rule 8.05(B)(2))

A shorter trading record, and/or variations or waivers the profit or other financial standards requirement for infrastructure project companies is only allowed if the following is complied with:

- the applicant company, either directly or through subsidiaries or joint venture companies, is a party to, and has the right to build and operate or participate in the results from the operation of a particular infrastructure project(s);
- at the time of listing, it is not engaged in any businesses other than those stipulated in the infrastructure project mandate(s) or contract(s);
- the infrastructure project(s) must be carried out under a long-term concession or mandate, normally with at least fifteen years remaining in each of them at the time of listing, which is awarded by the Government; it should be of a substantial size, and the applicant company's share of total capital cost of the projects should normally be at least HK\$1 billion;
- where it is involved in more than one project, the majority of its projects are in the pre-construction or construction stage;
- the bulk of the proceeds of the offering will be used to finance the construction of the project(s), and not principally to repay indebtedness or to acquire other non-infrastructure assets;
- it will not, and will procure its subsidiaries or joint venture companies from acquiring any other type of assets or engage in such activities that would result in a change of business from those stipulated in the infrastructure project mandate(s) or contract(s) in the first three years after listing;

- its substantial shareholders and management have the necessary experience, technical expertise, track record and financial strength to carry out the project(s), to complete and operate them thereafter. In particular, its directors and management must have sufficient and satisfactory experience of at least three years in the line of business and industry of the new applicant. Details of such expertise and experience must be disclosed in the listing document of the new applicant; and
- additional disclosure of matters and documents required by HKEx at its discretion, including business valuations, feasibility studies, sensitivity analyses, and cash flow projections will be included in the document(s) of the new applicant.

Mineral Companies (Main Board Rule 8.05B(1), Chapter 18, & Guidance Note 7)

A mineral company applying for listing must satisfy the following requirements before HKSE may accept a shorter trading record, and/or waive or vary the financial standards and management continuity:

- the mineral company must have discovered at least a portfolio of indicated resources or contingent resources (in the case of petroleum companies) of sufficient substance, identifiable under an accepted reporting standard and substantiated in a competent person's report;
- where the mineral company has not yet begun production, the company must disclose its plans to proceed its production with indicative dates and costs supported by at least a scoping study (a preliminary evaluation of a mineral project), and substantiated by the opinion of a competent person;
- there is sufficient working capital for 125% of present requirements, for at least twelve months from the date of the listing document;
- where a mineral company seeks a waiver from the financial standards requirements (see Main Board Rule 8.05 & GEM Board Rule 11.12A), it must establish that its directors and senior managers, taken together, have sufficient experience relevant to the exploration and/or extraction activity that the Company is pursuing. The individuals being relied on must have a minimum of five years relevant industry experience; and
- the company must include a report on its reserves and resources, prepared by a competent person, in its listing document. Competent persons must be independent of issuers (see Main Board Rules 18.03 to 18.08).

The mineral reporting standard (see Main Board Rules 18.28 to 18.33) is as follows:

- a mineral company must disclose information on mineral resources, reserves, and/or exploration results under the JORC Code NI 43-101, or the SAMREC Code. Information presented under other reporting standards must be reconciled to one of these codes. Valuation reports must conform to the VALMIN, CIMVAL or SAMVAL Code. (see Main Board Rules 18.28 to 18.33).

Guidance Note 7 of the Main Board Rule provides a suggested risk assessment for mineral companies which are particularly useful for risk factor disclosure and expert reports in the listing document.

Other Equities

Depository Receipts (Main Board Rule 8.09(2))

Mainland Chinese companies can issue H shares on the Hong Kong stock markets, so they do not need to resort to depository receipts for listing in Hong Kong; but it can be useful for companies in certain overseas jurisdictions to list in Hong Kong, which will not be able to list there if not for the use of depository receipts.

Depository receipts are issued by the depository bank on the back of the issuer's ordinary shares, which in practice, means the issuer's shares do not necessarily need to leave its home country. Hong Kong depository receipts ("HDR") in particular suit companies that come from countries with home-jurisdiction regulations prohibiting overseas issuance of shares, or restrictions against the maintenance of an overseas shares register. It also assists companies coming from dematerialised jurisdictions, where shares are held in book entry form, which is problematic in Hong Kong as the market demands both local share register and physical issuance. Countries such as Japan, France and Italy are governed by dematerialised jurisdictions, while Brazil and Japan are subject to restrictions around share registrations. For HDRs, the depository bank maintains the depository receipt register in Hong Kong.

Market capitalisation of a new applicant must be at least HK\$200 million (ie US\$26 million) at the time of listing. Market capitalisation at the time of listing is determined by multiplying the number of issued shares by the expected issue price. In the case of depository receipts, the depository receipts and the underlying shares will be taken into account when calculating the market capitalisation, provided that such depository receipts and the underlying shares are fungible.

Options, Warrants or Similar Rights (Main Board Rule 8.09(4))

Market capitalisation of HK\$10 million at the time of listing is required.

¶2-025 Conclusion

The Main Board Rules are strict, and in line with international standards in order to protect the investing public. As discussed above, some listing requirements can be modified for large companies²⁹⁴ and specific industries.²⁹⁵ The stringent international

²⁹⁴ HKSE may accept a shorter trading record period under the market capitalisation/revenue test, if the applicant can demonstrate that its directors and management have sufficient and satisfactory experience of at least three years in the line of business and industry, and there is management continuity for the most recent audited financial year. In order to qualify for the capitalisation/revenue test, companies need to have a large market capitalisation of at least HK\$4 billion at the time of listing, and revenue of at least HK\$500 million for the most recent audited financial year.

HKSE will also accept a lower percentage of public float between 15% and 25%, instead of 25% for issuers with an expected market capitalisation of over HK\$10 billion at the time of listing.

Both the reporting accountants and the sponsor are required to issue, for inclusion in the prospectus, a comfort letter to the issuer as regards any profit forecast made in the prospectus.

The reporting accountants also need to verify the indebtedness statement and the net tangible assets statement to be included in the listing document and issue a comfort letter to the company confirming that the work undertaken supports the figures contained in the prospectus.

In a global offering that will involve international offering, the reporting accountants may be required to participate in due diligence meetings in relation to the relevant international tranche and will be required to issue a comfort letter in the style of U.S. Auditing Standard AU 634, aligning standards for both the Hong Kong and relevant international portions of the offering.⁴¹⁴

Prospectus

Reporting accountants also assist with the preparation of the prospectus, particularly sections on “key statistics”, “share capital”, “indebtedness”, “trading record”, “profit and dividend forecast”, “working capital” and “adjusted net tangible assets” and any area which his professional competence is relevant. Reporting accountants would generally not comment on anything to do with management’s business judgment including any causes of change not within their knowledge and expertise or comment on management’s explanation of such changes. The accountants’ report is typically included in the prospectus as Appendix I.

¶6-017 Property Valuers (“Valuers”)

The role of a property value is to prepare an independent valuation report on property interests held by the group for the inclusion in the prospectus.

If the issuer has interests in any land or buildings over the specified threshold imposed by the Listing Rules,⁴¹⁵ the Listing Rules require valuations of such interests to be included in the prospectus. It is highly unlikely that a listing applicant has not obtained some interest in land and so a property valuer is usually involved in the IPO working party.

The property interests are generally held either for property activities or non-property activities. Property activities mean holding, developing or purchasing properties for subsequent sale, letting or investment and it does not include holding properties for its own use.

Valuation Reports

Valuation reports must contain all material details on the basis of valuation in accordance with the HKIS Valuation Standards (2012 edition) issued by the Hong Kong

⁴¹⁴ Paragraph 66 of the HKSIR 400.

⁴¹⁵ Main Board Rules 5.01A to 5.01C.

Institute of Surveyors. The disclosure in the prospectus should also be made in accordance with Chapter 5 and Practice 12 of the Main Board Rules and Checklist I.F. Among other things, the following substantial information should be included in such a report.⁴¹⁶

- detailed description of each property;
- classification of the property according to the purpose for which it is held;
- the name, address and professional qualifications of the valuer;
- the effective date as at which the property was valued and the date of the valuation. The effective date must not be more than three months before the date of the prospectus;⁴¹⁷ and
- such other information as HKSE may require under Practice Note 12 of the Main Board Rules.

To establish titles for the PRC property interests, a PRC legal opinion is normally required. A PRC legal opinion is also required to ascertain property titles and interests held by joint venture entity. Such legal opinions have to be submitted to the valuer and the valuer will explain whether and if so how he has taken account of the content of such opinion in the valuation of the relevant property.⁴¹⁸

Valuers’ Qualifications

All valuations of properties must be prepared by an independent qualified valuer. A valuer is not independent if he is either an employee or proposed director of the issuer, its group or its associated company. It would also not be independent if any director or employee of the valuation firm has such a relationship with the issuer or the valuation firm is a company within the issuer’s group.⁴¹⁹

For the valuation of properties in Hong Kong, the valuer must be a Fellow or Associate of the Royal Institution of Chartered Surveyors or the Hong Kong Institute of Surveyors and carries on the business of valuing properties in Hong Kong.⁴²⁰ For the valuation of properties situated outside Hong Kong, the valuer must have the appropriate professional qualifications and experience of valuing properties in the same location and category and such valuer should also comply with other requirements and procedures required in the jurisdiction where the property is situated, in addition to the requirements set out in the HKIS Valuation Standards.

⁴¹⁶ Main Board Rule 5.06.

⁴¹⁷ Main Board Rule 5.07.

⁴¹⁸ Paragraph 7 of the Practice Note 12 of the Main Board Rules.

⁴¹⁹ Main Board Rule 5.08(1).

⁴²⁰ Main Board Rule 5.08(2).

¶6-018 Competent Person (for Mineral Companies Only) (“Competent Person”)

A competent person is required to preparing competent person reports for inclusion in mineral companies’ prospectus.

A “competent person” must (1) have a minimum of five years’ experience relevant to the style of mineralisation and type of deposit under consideration or to the type of petroleum exploration, reserve estimate (as appropriate), and to the activity which the issuer is undertaking; (2) be professionally qualified, and be a member in good standing of a relevant self-regulatory recognised professional organisation, in a jurisdiction where the statutory securities regulator has satisfactory arrangements with SFC for mutual assistance and exchange of information for enforcing and securing compliance; and (3) take overall responsibility for the competent person’s report to be included in the prospectus in accordance with a recognised reporting standard acceptable to HKSE.⁴²¹

A competent person must be independent of the issuer, its directors, senior management and advisers. Specifically the competent person retained must:⁴²²

- have no economic or beneficial interest (present or contingent) in any of the assets being reported on;
- not be remunerated with a fee dependent on the findings of the competent person’s report;
- in the case of an individual, not be an officer, proposed officer or employee of the issuer or its group or associated company of the issuer; and
- in the case of a firm, not within the issuer’s group or associated company of the issuer. Any of the firm’s partners or officers must not be officers or proposed officers of any group or associated company of the issuer.

¶6-019 Placing Agents

A placing agent acts as an intermediary between the issuer and prospective investors who may be interested in the issuer and procures placees to purchase or subscribe for shares of the issuer.

Placing agents are typically the brokerage and securities firms that specialise in the buying and selling of shares and with a dedicated sales and trading team, they will sell shares to institutional investors and high net worth individuals whom they have strong relationship to. Either the underwriters sell directly to the investors or they can use the expertise of placing agents to sell the issuer’s shares. In practice, they are another distribution venue for the issuer’s shares. Being broker-dealers who are not part of the underwriting syndicate, they assist in the sale of shares and are allowed to purchase the issuer’s shares at a discount from the offering price.

⁴²¹ Main Board Rule 18.21.

⁴²² Main Board Rule 18.22.

¶6-020 Research Analysts

Research analysts are very familiar with the issuer’s business and write reports about the company and its shares, providing earnings estimates, and making investment recommendations. With their expertise, they can draw inferences and derive insights from publicly available information.

After receiving the post-hearing letter, the issuer and the sponsor will start the “pre-marketing” or “investor education” stage of offering. The company will meet separately and/or collectively research analysts employed by the underwriters to help them understand the company’s business model and develop their own forecasts of the company’s future results. In turn, the research analysts will draft detailed reports and send them to professional and institutional investors to educate them about the company and the offering prior to the roadshows.

Research analysts are prohibited from soliciting underwriting business or participating in IPO roadshows, but they may communicate with prospective investors if underwriters and company management are not present, and they are allowed to express their views.

¶6-021 Investor Relations Firm (“PR Company”)

Public Relations Consultants groom the directors and help to publicise the issuer. However due to the IPO publicity restrictions, they have to be careful what they can or cannot do. Their role is described directly below –

- before the IPO:
 - attending to the details of the presentations to be made by the company to analysts and fund managers;
 - preparing corporate brochures and video tapes and helping the company to effectively liaise with the press;
 - assisting the roadshows and presenting the company to the target audience in a professional manner;
 - assisting the setting up of the investor relations section of the company’s website that will go live after the IPO is priced; and
 - assisting in the relevant artwork and design of the prospectus.
- after the IPO, an investor relations firm can provide professional assistance in developing the company’s ongoing investor communications programs and assisting the company to announce important corporate events, such as acquisitions, in a way that can further market the company.

¶6-022 Receiving Banks (“Receiving Bankers”)

Being an agent for the issuer, the receiving banks receive and process application under the Hong Kong public offering tranche of the international offering.

They distribute prospectuses (together with application forms), process applications and deal with acceptance and rejection. They also hold the application moneys pending release to the company and the unsuccessful or partially successful applicants.

A Receiving Bankers Agreement is entered into between the receiving bankers, the issuer, the sponsor and underwriters and more about the receiving bankers agreement can be found in Chapter 8.

¶6-023 Share Registrar and Transfer Office (“Registrar”)

A share registrar’s main roles are: processing and balloting public offer applications; dispatching share certificates to successful applicants; and sending refund cheques to partly successful and unsuccessful applicants.

Upon listing, the share registrar will be in charge of the register of members in Hong Kong and will process and record transfers of shares of the company. The registrars are typically involved in the dispatch of all circulars to shareholders as well as cheques or certificates for dividends declared by the company.

A Registrar’s Agreement is entered into between the registrar, the issuer [and the sponsor] and please refer to Chapter 8 for more details.

¶6-024 Financial Printer (“Printer”/“Translation Company”)

For a global offering, printers must be engaged to print both the red herring and the actual prospectus. A good financial printer should meet high standard of timeliness, quality, accuracy and confidentiality. They should be able to provide high quality proofreading and copywriting services.

The financial printer also coordinates the translation of the document into Chinese. Where there is a Chinese translation of the prospectus, the translator should certify that the Chinese translation is true and accurate and the sponsor has to certify that the translator is competent.

The night before the bulk print, the working parties will all gather at the financial printer to proofread the prospectus and may stay overnight there, so the financial printer should be easily assessable with spacious conference room plus catering facilities. After the bulk print, they will arrange for the relevant number of copies of the prospectus to be distributed to the sponsor, the receiving bankers, HKSE, and other relevant parties.

¶6-025 Compliance Adviser (“Compliance Adviser”)

The issuer must appoint a compliance adviser commencing on the date of the IPO and ending with the publication of its financial results for the first full year financial year after the IPO. The HKSE may direct the listed issuer to appoint a compliance adviser after the above period. To ensure an effective relationship between a PRC issuer and its compliance adviser, HKSE requires the two parties to enter into an agreement setting out

the requirements of Main Board Rules 19A.05 and 19A.06. In respect of the issuer it should:

- provide the compliance adviser with access at all times to its authorised representatives, directors and other officers and procure that such persons promptly supply such information and assistance as the compliance adviser may need or reasonably request to perform its duties; and
- ensure that there are adequate and efficient means of communication between itself, its authorised representatives, directors and other officers and the compliance adviser; and should keep the compliance adviser fully informed of all communications and dealings between itself and HKSE.

The compliance adviser needs to give an undertaking to HKSE to comply with the Listing Rules and cooperate with the Listing Division and/or the Listing Committee of HKSE for any investigation.

The compliance adviser has both reactive and proactive duties.

During its appointment, the issuer should consult and seek advice from the compliance adviser in the following situations:

- before publication of any regulatory announcement, circular or financial report;
- before carrying out any possible notifiable or connected transaction including share issues and share repurchases;
- when the issue proposes a change of the use of IPO proceeds from what stated in the prospectus; and
- when HKSE make enquiries concerning usual movements in the price or trading volume of the issuer’s shares, the possible development of a false market in its shares or any other matters.

The compliance adviser is an intermediary between HKSE and the issuer regarding the above issues. The compliance adviser also needs to ensure that it:

- provides advice to the issuer on the continuing requirements under the Listing Rules and the applicable laws and regulations and make sure every new appointees to the board also understand their responsibilities and fiduciary duties as a director of the listed issuer; and
- informs the issuer on a timely basis of any amendment or supplement to the Listing Rules and any new or amended law, regulation or code in Hong Kong applicable to the issuer.

Due to the importance of the compliance adviser’s role, the issuer should not terminate the role of its compliance adviser until it has appointed a replacement. If HKSE is not satisfied that the compliance adviser is fulfilling its responsibilities, HKSE may require the issuer to terminate the compliance adviser’s appointment and appoint a replacement as soon as possible.

each of the sponsors who will act as the sponsors' contact with HKSE and the company; and

- observing the guidelines set out in the Code of Conduct, Sponsor Guidelines, Internal Control Guidelines, CFA Code issued by SFC to the extent possible.

Obligations of the company should, among other things, include:

- responding to any request for advice from the sponsors in a timely manner so as to allow each of the sponsors reasonably sufficient time to advise the company, particularly in relation to any provisions of the Main Board Rules compliance with which is subject to any time limit or in relation to any matters in which timing is a material consideration or has a material significance;
- ensuring that each of the sponsors shall have all necessary access at all times to its directors, other officers and the authorised representatives;
- ensuring that its directors, other officers and the authorised representatives will provide such assistance and information as each of the sponsors may reasonably request in connection with the performance of its duties under the Main Board Rules;
- ensuring that there is adequate and efficient means of communication between each of the sponsors, the authorised representatives, the directors and other officers of the company;
- using its best endeavour to ensure that any public disclosure of information to be made by the company in Hong Kong and/or the People's Republic of China and/or any other relevant country in accordance with the requirements of any laws, regulations and codes in Hong Kong and/or the People's Republic of China and/or any such relevant country will be properly coordinated and made in a timely and orderly manner;
- not, without the prior knowledge of each of the sponsors, communicate with HKSE other than through the authorised representatives or any alternate for the authorised representatives appointed pursuant to Main Board Rule 3.06(2) and ensuring that each of the sponsors is kept fully informed on all communications between the authorised representatives and HKSE, and will use its best endeavours to ensure that there is no inconsistency or contradiction between such communications and communications between the sponsors jointly and HKSE;
- not during its appointment, appoint any other sponsors except with the prior written consent of each of the sponsors; and
- ensuring that it complies with the Main Board Rules and the laws and regulations in Hong Kong.

The indemnity and non-liability section is to ensure that:

“save in respect of any wilful misconduct, or gross negligence on the part of the relevant sponsors, the company will indemnify the sponsors and its officers for any claims against them and for any

losses and damages in connection with the proper performance of its duties under the sponsors' agreement, any breach on the part of the company of any of the provisions of the sponsors' agreement or any default under or breach of any of the provisions of the Main Board Rules by the company except where the company was acting in accordance with and in reliance with the sponsors' advice.”

Confidentiality clause in the sponsors' agreement requires the company and each of the sponsors to procure that:

“their respective directors, officers and agents shall treat as strictly confidential all information received or obtained as a result of entering into or performing the sponsors' agreement unless it is required to be disclosed by applicable law, required by any securities exchange or regulatory or government body, required to vest the full benefit of the sponsors' agreement in such party, disclosed to the professional advisers, auditors, directors, holding and associated companies of such party subject to a binding obligation of confidentiality, the information has come into the public domain through no fault of such party or the other party has given prior written approval to the disclosure.”

The confidentiality clause is typically specified in such a way that it shall survive the termination of any appointment and the termination of the sponsors' agreement.

¶8-012 Due Diligence

Due diligence varies in accordance with the industry and particular business concerned. Due diligence questionnaire should be tailor-made for the industry rather than using templates. The following checklist only intends to give an idea of areas that due diligence should cover and it is far from exhaustive. Terms used below should be adjusted to the particular industry and business the issuer is in:

- corporate organisation and ownership:
 - organisational and ownership charts or similar information relating to the company and its subsidiaries, including all companies, partnerships, joint ventures or other entities or interest groupings in which the company or any subsidiary owns any interest, directly or indirectly and a description of the nature and size of such interest;
 - particulars of the authorised and issued share capital of each of the companies in which an interest is held, confirmation of the registered and beneficial ownership of their respective issued share capitals, and details of any share option, share pledge or similar arrangements affecting the shares of the company or any of the other companies;
 - Memorandum and Articles of Association (or foreign equivalent Charter or organisational documents and by-laws or regulations) including all amendments, of each of the companies, including copies of their respective

- certificates of incorporation and any change of name certificates and any business registration or branch registration certificate;
- registered office address and principal place of business (if different) of each of the companies;
- details of any increases of capital, reductions of capital or other capital reorganisations involving any of the companies that may have occurred since their respective dates of incorporation;
- minutes of directors' and shareholders' meeting of [each of the companies] [the company and its [material] subsidiaries][since [specified date]][for the last [five] years];
- share registers and register of transfers (or equivalent) of the companies;
- agreements between any of the companies and any of their respective shareholders or third parties relating to the voting, disposal or acquisition of shares or securities of such companies;
- details of the other shareholders in companies that are not wholly-owned, and of the partners and co-venturers in other entities, and details of their respective interests;
- [all quarterly, annual and other periodical reports and other communication to the shareholders of [each of the companies][the company and its [material] subsidiaries]];
- a schedule of all jurisdictions in which [each company][the company and its [material] subsidiary] is registered or qualified to do business or is otherwise operating; and
- good standing and tax certificates for [each company][the company and its [material] subsidiaries] in the relevant jurisdictions in which it has offices or does business;
- financial information:
 - balance sheets and profit and loss statements for the last three years [and the first six months of [year]];
 - describe the financial systems, standards and accounting principles adopted, as well as their differences with the international accounting standards;
 - name and address of auditors, all reports and management letters from auditors to the company, and audit representation letters by the company to its auditors and related correspondence, for the last three years [and the first six months of [year]];
 - review of major operational and accounting changes in the last [five] years;
 - internal budgets and projections prepared since [date], including any internal memoranda describing the assumptions used in preparing such budgets and projections;

- data for the operating revenue from the core business for each year for the last three years [and the first six months of [year]] and provide a classification and composition analysis of such operating revenue;
- an analysis of the direct and indirect cost structure of the above-mentioned revenues, including data, classification, structure, wages, maintenance costs, depreciation, interest, taxes, management fees, water, electricity and gas charges, etc;
- data on the revenue from non-core business and provide a classification and composition and analysis of such operating revenue;
- an analysis of the direct and indirect cost structure of the above-mentioned revenues, including data, classification, structure, wages, maintenance costs, depreciation, interest, taxes, management fees, water, electricity and gas charges, etc;
- data on the proportion between the company's revenue from core business and that from non-core business, as well as an analysis thereof. Also provide the amounts and sources of renminbi and foreign exchange revenues;
- describe costs control strategies and methods;
- sources of foreign exchange and renminbi costs;
- please provide total outstanding debts;
- details of all loans made to or by any of the companies, including all loans and indebtedness to directors, [officers], employees or shareholders of any of the companies) or any other companies in which any such director, employee or shareholder is interested;
- a classification and analysis of the debts including the type of debts, currencies in which the debts are denominated, annual debt payment plans, interest rate for each debt, foreign exchange risks and creditors' backgrounds;
- all loan agreements and other debt-related documents;
- any default on loan agreements;
- are all loans subject to mortgage clauses and business restriction clauses?
- all outstanding mortgages, charges (whether registered or not) and other security arrangements and documents relating to or affecting any of the companies;
- details and copies of all guarantees, indemnities, and other contingent obligations given by any of the companies in relation to the obligations of any other person; and given by any other person in respect of the obligations of any of the companies;
- all hire purchase or instalment purchase agreements, finance leases, letters of credit, performance and other bonds and similar documents involving or relating to any of the companies;