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**LISTING RUSSIAN COMPANIES IN HONG KONG**

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## INTRODUCTION

On 16 February 2015, Russia signed the International Organisation of Securities Commissions' Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (the **IOSCO MMoU**)<sup>1</sup> which paves the way for Russian companies to list on Hong Kong's Stock Exchange (the **Exchange**).

With a market capitalisation of US\$3,233 billion at the end of 2014, the Exchange is currently the world's 7<sup>th</sup> largest stock exchange by market capitalisation, and the third largest in Asia after Japan and Shanghai. In terms of IPO funds raised, however, Hong Kong ranked second (after New York) among the world's exchanges in 2014, continuing a trend that has placed it in the world's top five for the past 13 years.

The Hong Kong Stock Exchange is a leading international stock exchange which allows full access to foreign investors wishing to trade on its markets and offers a listing venue to foreign companies which are able to meet its requirements. The key advantage of Hong Kong and its stock exchange is its strategic position as the gateway between Mainland China and the rest of the world. Hong Kong has long been the preferred international listing venue for mainland Chinese companies looking to raise funds in the international capital markets and there are currently 876 Chinese companies listed on the Exchange which account for 60% of the total market capitalisation.

The Exchange has also been keen to list more international companies, and recent years have seen an increasing number of international companies listing in Hong Kong.

There were 1,752 companies listed on the Exchange as at 31 December 2014, of which 1,548 were listed on the Exchange's Main Board. A key factor attracting foreign companies to Hong Kong market is the depth of liquidity in both its primary and secondary markets.

There were 115 new listings<sup>2</sup> on the Exchange in 2014 which raised US\$ 29.4 billion (up 33% from 2013). The ease of raising funds post-listing is also attractive to foreign companies. In 2014, listed companies raised US\$91.3 billion post listing, an increase of 238% on 2013.

Hong Kong currently ranks as Asia's top international financial centre. Among the benefits of listing on the Hong Kong stock exchange is that this provides overseas companies with access to investors in Mainland China, currently under the Qualified Domestic Institutional Investor (QDII) programme. This allows Mainland Chinese financial institutions to raise funds in the domestic Chinese market and to invest US\$76.79 billion in offshore securities markets. The importance of Mainland Chinese investors is expected to grow and the Exchange is now positioning itself as the vehicle through which Mainland Chinese investors can invest internationally.

A first step in that process was the launch in November 2014 of the Shanghai-Hong Kong Stock Connect pilot programme which allows certain Mainland Chinese investors to invest directly in Hong Kong listed stocks for the first time. Although currently restricted to Hang Seng Index companies, it is likely that the programme will be expanded to include other

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<sup>1</sup> The current list of signatories to the IOSCO MMoU is available at:

[http://www.iosco.org/library/index.cfm?section=mou\\_siglist](http://www.iosco.org/library/index.cfm?section=mou_siglist)

<sup>2</sup> Excluding 7 companies which transferred their listings from GEM to the Main Board. HKEx. "Market Statistics 2014" at page 2 available at <http://www.hkex.com.hk/eng/newsconsul/hkexnews/2015/Documents/150108news.pdf>

stocks in the future. If this is the case, a Hong Kong listing will offer international companies even greater access to Mainland China's investors.

Launched in November 2014, the pilot programme allows investors in Hong Kong and China to trade eligible shares listed on the other market through the exchange and clearing house in their local market.

Under the so-called Southbound Trading Link, Mainland investors can trade the constituent stocks of the Hang Seng Composite LargeCap and MidCap Indexes, and all H-shares with corresponding A shares listed on the Shanghai Stock Exchange.

Trading is subject to aggregate and daily quotas. The northbound trading link has an aggregate trading quota of RMB300 billion and a daily trading quota of RMB13 billion, while the southbound trading link has an aggregate trading quota of RMB250 billion and a daily trading quota of RMB10.5 billion. It is not however possible to purchase IPO shares through Stock Connect.

The quotas apply on a "net buy" basis, meaning investors can always sell their cross-boundary securities regardless of the quota balance. Mainland investors are restricted to institutional investors and individuals holding RMB500,000 in cash & securities, whereas all Hong Kong and overseas investors are eligible for North-bound trading.

A similar scheme to allow the mutual trading of shares between the Shenzhen Stock Exchange and the Hong Kong Stock Exchange is expected to be launched in the second half of 2015.

## **BENEFITS OF LISTING IN HONG KONG**

Key advantages of Hong Kong as a listing venue are its established legal system based on English common law and its regulatory framework which is on a par with those in other international finance centres, which give investors confidence in the Hong Kong stock market. It also offers many tax advantages, currency convertibility, free transferability of securities and no restrictions on capital flow.

In addition to fund raising opportunities, Hong Kong offers foreign companies the chance to raise their profile and visibility in China and the rest of the Asia-Pacific region. This has proved particularly attractive to companies in the luxury goods sector and high profile companies such as Prada, Coach, L'Occitane and Samsonite have listed in Hong Kong in recent years.

China's position as a major consumer of energy, minerals and metals has also attracted a number of mining and natural resource companies to list in Hong Kong. These include Swiss commodities giant Glencore International AG, Russia-based United Company Rusal PLC, Kazakhstan copper miner Kazakhmys PLC and Brazilian metals and mining company Vale S.A. Vale S.A. was also the first company to list on the Exchange in the form of depositary receipts (**HDRs**). The Exchange's Listing Rules allow overseas companies to list on the Exchange's Main Board (but not on its Growth Enterprise Market) in the form of HDRs rather than ordinary shares. This is intended to allow the Hong Kong listing of companies from jurisdictions which restrict the movement of shares abroad or prohibit an overseas share register or splitting of the share register.

<b>Hong Kong Listings of Overseas Companies</b>					
<b>Issuer</b>	<b>Country of Operations /Headquarters</b>	<b>Country of Incorporation</b>	<b>Sector</b>	<b>Year of Listing</b>	<b>Funds Raised (HK\$ billion)</b>
Glencore International plc	Headquartered in Switzerland	Jersey	Natural Resources	May 2011	77.75
RUSAL	Russia	Jersey	Natural Resources	January 2010	17.39
Mongolian Mining Corporation	Mongolia	Cayman Islands	Natural Resources	October 2010	5.81
PRADA SpA	Italy	Italy	Luxury	June 2011	19.23
Samsonite International SA	Headquartered in United States	Luxembourg	Luxury Goods	June 2011	10.09
L'Occitane	France	Luxembourg	Luxury Goods	May 2010	5.5
Vale SA (HDR Listing)	Brazil	Brazil	Natural Resources	December 2010	
Kazakhmys PLC	Kazakhstan	United Kingdom	Natural Resources	June 2011	
Coach, Inc (HDR Listing)	United States	United States	Luxury Goods	December 2011	

## THE EXCHANGE'S MARKETS

The Exchange operates two markets, the Main Board and the Growth Enterprise Market (**GEM**). The Main Board caters for companies with a profitable operating track record or that are able to meet alternative financial standards. It is designed to give these companies an opportunity to raise further funds from the market in order to finance future growth. GEM, on the other hand, caters for smaller growth companies and has lower admission criteria. GEM also acts as a stepping stone to Main Board listing.

The post-listing obligations of GEM and Main Board listed companies are now broadly similar. The principal remaining difference is that quarterly reporting is mandatory for GEM companies, whilst for Main Board issuers it is a Recommended Best Practice only under the Corporate Governance Code.

## KEY QUALIFICATIONS FOR LISTING ON THE MAIN BOARD

### (a) Suitability for listing

A listing applicant must satisfy the Exchange that the applicant and its business are suitable for listing. The Exchange's [Guidance Letter HKEx-GL68-13](#)<sup>3</sup> provides guidance on factors it takes into account in assessing an applicant's suitability, including: over-reliance on third parties (e.g. connected persons); non-compliance with laws and regulations; concerns as to financial performance and sustainability; and internal controls failings.

### (b) Operating History and Management

A Main Board listing applicant must have a trading record period of at least 3 financial years with:

- (i) management continuity for at least the 3 preceding financial years; and
- (ii) ownership continuity and control for at least the most recent audited financial year.

An exception exists for companies applying to list under the market capitalisation/revenue test (please see below). For these companies, the Exchange may accept a shorter trading record period under substantially the same management if the applicant can demonstrate that:

- (i) its directors and management have sufficient and satisfactory experience of at least 3 years in the line of business and industry of the new applicant; and
- (ii) management continuity for the most recent audited financial year.

### (c) Financial Tests

Main Board listing applicants are required to satisfy one of 3 tests: the Profit Test; the Market Capitalisation/Revenue Test; or the Market Capitalisation/Revenue/Cash Flow Test.

**The Profit Test** (Rule 8.05(1)) requires the applicant or its group to have profits of at least **HK\$20 million** in the most recent financial year and aggregate profits of at least **HK\$30 million** in the two years before that. This profit must exclude any income or loss of the

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<sup>3</sup> Exchange Guidance letter HKEx-GL68-13 "Guidance on suitability for listing" available at <http://www.hkex.com.hk/eng/rulesreg/listrules/listguid/iporq/Documents/gl68-13.pdf>.

applicant (or its group) generated by activities outside the ordinary and usual course of its business.

Applicants listing under the profits test must also have an expected market capitalisation at the time of listing of at least **HK\$200 million**.

Under the **Market Capitalisation/Revenue/Cash Flow Test** there is no profit requirement for a listing applicant which has an expected market capitalisation at the time of listing of at least HK\$2 billion. Instead the applicant must have:

- (i) at least **HK\$500 million** in revenue for the most recent audited financial year; and
- (ii) positive cash flow from operating activities of at least **HK\$100 million** in aggregate for the three preceding financial years.

Under the **Market Capitalisation/Revenue Test**, an applicant with an expected market capitalisation at listing of at least **HK\$4 billion**, will meet the financial requirement for listing if it has revenue of at least HK\$500 million for the most recent audited financial year. This test is for larger listing applicants that are able to generate substantial revenue.

### **Financial Requirement Waivers**

#### Mineral Companies

A new applicant Mineral Company that cannot satisfy the profit test, the market capitalisation/revenue/cash flow test or the market capitalisation/revenue test of Main Board Rule 8.05, may be accepted for listing if it establishes to the Exchange's satisfaction that its directors and senior management, taken together, have a minimum of 5 years' experience relevant to the exploration and/or extraction activity that the Mineral Company is pursuing. Details of such experience must be included in the applicant's listing document.

A Mineral Company is a company for whom exploration for, and/or extraction of, natural resources such as metal ores, mineral concentrates, industrial minerals, mineral oils, natural gases or solid fuels account for 25% or more of the total assets, gross revenue or operating expenses of the company and its subsidiaries.

However, a pre-production stage company seeking a waiver needs to show a clear path to commercial production. The Exchange expects most companies seeking a waiver to be at the development stage, although companies which are in production are not necessarily precluded as they may have junior assets which are yet to be developed. Companies that are in production will however need to be able to show a clear path to profitability in order to be accepted for listing. Pure exploration companies are not considered suitable for listing.

#### Waivers for non-Mineral Companies

The Exchange may also accept a shorter trading record period and/or may vary or waive the financial standards requirements for:

- (i) newly formed "project" companies (for example a company formed to construct a major infrastructure project); or
- (ii) in exceptional circumstances, if the applicant or its group has a trading record of at least two financial years and the Exchange is satisfied that the applicant's listing is in the interests of the applicant and its investors.

### Calculation of revenue

For both the Market Capitalisation/Revenue Test and the Market Capitalisation/Revenue/Cashflow Test, only revenue arising from the applicant's principal activities and not items of revenue or gains arising incidentally will be recognised. Revenue from "book transactions" is disregarded.

### **(d) Shares in Public Hands**

There must be an open market in the securities for which listing is sought. In general, this means that not less than 25% of the listing applicant's total issued share capital having an expected market capitalisation at the time of listing of at least HK\$50 million, must be held by the public, i.e. owned by persons who are not "core connected persons" of the issuer, persons whose securities have been financed by a core connected person, or who are accustomed to take instructions from a core connected person in relation to their shares. "Core connected persons" include directors, chief executives or substantial shareholders (i.e. holders of 10% of the voting power at general meetings) of a company or any of its subsidiaries or a close associate of any of them.

Where a listing applicant has more than one class of securities, the total securities of the listing applicant held by the public (on all regulated markets including the Hong Kong Stock Exchange) must be at least 25% of the issuer's total issued share capital. However, the class of securities for which listing is sought must not be less than 15% of the issuer's total issued share capital, and have an expected market capitalisation at the time of listing of not less than HK\$50 million.

### Exchange's Discretion to Accept Lower Public Float

For large companies, with an expected market capitalisation in excess of HK\$10 billion, the percentage required to be in public hands, may, at the Exchange's discretion, be lower (but not lower than 15%) provided that:

- (i) the Exchange is satisfied that the number of securities and their distribution will enable the market to operate properly with a lower percentage;
- (ii) the issuer makes appropriate disclosure of the lower prescribed percentage of public float in the listing document;
- (iii) the issuer confirms the sufficiency of public float in successive annual reports after listing; and
- (iv) a sufficient proportion (to be agreed in advance with the Exchange) of any securities to be marketed contemporaneously in and outside Hong Kong, must normally be offered in Hong Kong.

This public float waiver is available only on initial listing. It cannot be applied for post-listing if the issuer subsequently satisfies the HK\$10 billion market capitalisation requirement.

### **(e) Minimum Number of Shareholders at Time of Listing**

Securities new to listing must have an adequate spread of shareholders. The number will depend on the size and nature of the issue, but there must be a minimum of 300 holders.

In addition, not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders.

After listing, there is no requirement for a minimum number of shareholders. The issuer must however continue to comply with the minimum public float requirement.

#### **(f) Market Capitalisation**

The expected market capitalisation at the time of listing of a new applicant must be at least HK\$200 million and the expected market capitalisation of the securities held by the public must be at least HK\$50 million. If a listing applicant lists under the Market Capitalisation/Revenue/Cash Flow Test or Market Capitalisation/Revenue Test, it must have an expected market capitalisation at the time of listing of HK\$2 billion or HK\$4 billion, respectively. Most companies at the time of initial flotation have a market capitalisation of around HK\$200 million. Further issues of securities of a class already listed are not subject to this limit, and, in exceptional cases, a lower expected initial market capitalisation may be acceptable, although the Exchange will have to be satisfied as to the marketability of the securities.

#### **(g) Working Capital Sufficiency**

A listing applicant must have sufficient working capital for the group's present requirements, that is for at least the next 12 months from the date of publication of the listing document.

#### Mineral Companies

A new applicant Mineral Company is required to demonstrate that it has sufficient working capital for 125% of the group's requirements for the next 12 months including general, administrative and operating costs, property holding costs and the cost of any proposed exploration and/or development.

### **GEM LISTING**

The key requirements for listing on GEM are summarised below.

#### **(a) Suitability for Listing**

Both the issuer and its business must, in the opinion of the Exchange, be suitable for listing.

#### **(b) Operating History and Management**

A GEM listing applicant must have:

- (i) management continuity for at least 2 completed financial years; and
- (ii) ownership continuity and control for at least 1 completed financial year,

immediately before the issue of the listing document. In both cases, continuity must continue until the date of listing.

The Exchange may accept a trading record period of less than 2 financial years and waive or vary the ownership and management requirements for:

- (i) newly formed project companies; (for example a company formed for the purpose of a major infrastructure project);
- (ii) mineral companies where the directors and senior management have more than 5 years' relevant experience; and
- (iii) in exceptional circumstances under which the Exchange considers it desirable to accept a shorter period.

Where the Exchange accepts a shorter period, the applicant must nevertheless meet the cash flow requirement of HK\$20 million for that shorter trading record period.

#### **(c) Cash Flow Requirement**

A GEM listing applicant must have a positive cashflow from operating activities in the ordinary and usual course of business of at least HK\$20 million in total for the 2 financial years immediately preceding the issue of the listing document.

#### **(d) Market Capitalisation**

The expected market capitalisation of a new listing applicant at the time of listing must be at least HK\$100 million.

#### **(e) Public Float**

The minimum public float requirement is in line with the Main Board requirement, that is 25% or, in the Exchange's discretion, between 15% and 25% for companies with a market capitalisation of more than HK\$10 billion. Shares held by the public must have a market capitalisation of at least HK\$30 million at the time of listing. If the issuer has more than one class of shares, the total shares in public hands (on all regulated market(s) including the Exchange) at the time of listing must be at least 25% of the issuer's total issued share capital and the shares for which listing is sought must be at least 15% of the total issued share capital with an expected market capitalisation of HK\$30 million at the time of listing.

#### **(f) Minimum Number of Shareholders**

The equity securities in the hands of the public should, as at the time of listing, be held among at least 100 persons (including those whose equity securities are held through CCASS).

In addition, not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders.

### **ELIGIBILITY OF OVERSEAS LISTING APPLICANTS**

The Listing Rules provide for the listing of companies incorporated in Hong Kong, the PRC, the Cayman Islands and Bermuda (**Recognised Jurisdictions**). The Exchange has also accepted companies from twenty-one other jurisdictions (referred to as **Acceptable Jurisdictions**) for listing. These are:

Australia, Brazil, the British Virgin Islands, Canada (Alberta), Canada (British Columbia), Canada (Ontario), Cyprus, France, Germany, Guernsey, the Isle of Man, Italy, Japan, Jersey, the Republic of Korea, Labuan, Luxembourg, Singapore, the United Kingdom and the states of California and Delaware in the United States of America.

The Exchange's policy requirements for accepting overseas listing applicants are set out in the Joint Policy Statement Regarding the Listing of Overseas Companies (**Joint Policy Statement**) published by the Exchange and the Securities and Futures Commission (**SFC**) which was updated in September 2013. The key requirements relate to: (i) the standards of shareholder protection available to shareholders of the overseas listing applicant; and (ii) the regulatory cooperation arrangement in place between the statutory securities regulator(s) in the applicant's jurisdiction of incorporation and its place of central management and control (if different) and Hong Kong's Securities and Futures Commission (the **SFC**).

In relation to shareholder protection standards, the Exchange requires that the listing applicant must be able to demonstrate that the laws and regulations of its country of incorporation, **and** the provisions of its constitutional documents, together provide standards of shareholder protection which are equivalent to those provided under Hong Kong law. The key standards of shareholder protection are set out in the Joint Policy Statement and relate to:

- (a) the matters which require approval by a super-majority of shareholders' votes (e.g. material changes to the company's constitutive documents or the voluntary winding-up of the company);
- (b) a requirement that any change to the company's constitutional document to increase an existing shareholder's liability to the company must be agreed by the shareholder in writing;
- (c) the appointment, removal and remuneration of auditors must be approved by a majority of shareholders or another body that is independent of the board; and
- (d) proceedings at general meetings.

A listing applicant which is incorporated in a jurisdiction already accepted as an Acceptable Jurisdiction can refer to the Exchange's Country Guide for that jurisdiction. If it adopts the arrangements set out in that Country Guide, it will not need to provide a detailed explanation of how it meets the key shareholder protection standards.

Listing applicants incorporated in a jurisdiction new to listing need to demonstrate to the Exchange how the laws and regulations of their country of incorporation, their constitutional documents and the arrangements they adopt as a whole meet the key shareholder protection standards set out in the Joint Policy Statement. In doing so, they can refer for guidance to the methods used to show equivalent shareholder protection standards specified in a Country Guide for an Acceptable Jurisdiction or methods used by those incorporated in one of the four Recognised Jurisdictions.

As regards regulatory cooperation arrangements, the Exchange requires that the statutory securities regulator in the listing applicant's: (a) jurisdiction of incorporation; and (b) place of central management and control (if different), must:

- (i) be a full signatory of the IOSCO MMoU; **or**
- (ii) have entered into an appropriate bi-lateral agreement with the SFC which provides adequate arrangements with the SFC for mutual assistance and exchange of

information for the purpose of enforcing and securing compliance with the laws and regulations of that jurisdiction and Hong Kong.<sup>4</sup>

Russia signed the IOSCO MMoU on 16 February 2015, paving the way for its acceptance as an “acceptable jurisdiction” of incorporation for the purposes of listing in Hong Kong. Russia was previously prevented from becoming an Acceptable Jurisdiction because it had not signed the IOSCO MMoU and there was no bi-lateral arrangement on regulatory cooperation between Hong Kong and Russia. This was the reason why Lukoil, Russia’s second largest oil producer, suspended preparations to list in Hong Kong in 2013.

There are currently only two Russian-based companies listed in Hong Kong: Rusal and IRC Limited. However, neither company is incorporated in Russia. Rusal is incorporated in Jersey which was approved as an Acceptable Jurisdiction in connection with the company’s listing. There was no requirement at the time of Rusal’s listing for the securities regulator of an overseas applicant’s place of central management and control to be either a signatory to the IOSCO MMoU or a party to a bi-lateral arrangement on regulatory cooperation with the SFC. The requirements for regulatory cooperation arrangements do not apply to the 4 recognised jurisdictions of incorporation (Hong Kong, Bermuda, the Cayman Islands and the People’s Republic of China).

The Rusal listing was also unusual in that it is the only Hong Kong IPO ever to have been restricted to institutional and professional investors or other investors ordering at least HK\$1 million of shares each. The barriers to retail participation were insisted upon by the SFC mainly due to concerns regarding Rusal’s high debt levels.

Gazprom is another Russian company which was reported to be considering a Hong Kong listing in 2014 following its listing of American Depositary Receipts (ADRs) on the Singapore Stock Exchange in June 2014.

## **LISTING HONG KONG DEPOSITARY RECEIPTS**

Companies can list on the Main Board of the Exchange either in the form of ordinary shares or depositary receipts (**HDRs**) representing a given number of underlying shares. However, HDRs cannot be listed on the Growth Enterprise Market (**GEM**) and companies must list ordinary shares.

The framework for listing HDRs was introduced in July 2008 as part of the Exchange’s initiative to encourage the listing of more foreign companies on the Exchange. Prior to 2008, the Listing Rules required companies to list in the form of ordinary shares and to maintain a share register or a branch of their share register in Hong Kong. These requirements effectively barred the listing of companies from jurisdictions which prohibit the issue of shares overseas or the maintenance of an overseas share register. The HDR regime was therefore introduced as a solution to this problem and was aimed in particular at encouraging the listing of companies from Russia, India, Taiwan, Kazakhstan, Mongolia and Vietnam.

However, to date, only three companies have listed HDRs on the Exchange and these were all secondary listings. These are: (i) Brazilian mining company, Vale which listed in Hong Kong in December 2010 – it is also listed on the stock exchanges of São Paulo, New York, Paris, and Madrid; (ii) American luxury handbag and accessories brand, Coach Inc. which listed in Hong Kong in December 2011 – its primary listing is on the New York Stock Exchange; and (iii) Japanese retail clothing business, Fast Retail-DRS whose

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<sup>4</sup> Details of the SFC’s cooperative arrangements with overseas regulators are available at <http://www.sfc.hk/web/EN/about-the-sfc/collaboration/overseas/>.

primary listing is on the Tokyo Stock Exchange and which listed in Hong Kong in March 2014.

### **Listing Requirements for HDR Issuers**

The listing requirements for HDR issuers are essentially the same as for issuers of shares – i.e. they must satisfy the listing criteria set out in Chapter 8 of the Listing Rules. There is no requirement for the issuer to be already listed on an overseas exchange. Additional requirements specific to HDRs must also be complied with and these are set out in Chapter 19B of the Main Board Listing Rules. The additional requirements that must be met by HDR issuers are as follows:

#### **(a) Public Float**

HDR issuers must comply with the public float requirement that at least 25% of the issuer's total issued share capital must be held by the public at all times. In the case of companies with an expected market capitalisation at the time of listing of HK\$10 billion or more, the Exchange has a discretion to accept a lower public float of between 15% and 25%.

Where the HDRs listed in Hong Kong are fungible with the underlying shares, the total shares and shares represented by HDRs of the issuer held by the public on both the Exchange and any relevant overseas market(s) will count towards the 25% (Rule 19B.08).

#### **(b) HDR Requirements**

The HDRs must be freely transferable and the securities which the HDRs represent must be fully paid and free from all liens and restriction on the right of transfer to the depositary. HDRs may be issued in respect of newly issued shares and/or in respect of shares placed with a depositary by existing shareholders provided that the issuer applies to be the issuer of such depositary receipts and assumes the obligations and duties imposed on an issuer by the Listing Rules.

#### **(c) Register of HDRs**

An approved share registrar is required to maintain in Hong Kong a register of HDR holders and the transfers of the HDRs. Only HDRs registered in Hong Kong are permitted to be traded on the Exchange.

#### **(d) Depositary**

The depositary must: (a) be duly incorporated and operate in conformity with its constitutional documents; (b) be a suitably authorised and regulated financial institution acceptable to the Exchange; and (c) have adequate experience in issuing and managing DR programmes in Hong Kong or overseas. Depositaries do not require a depositary licence.

#### **(e) Deposit Agreement**

Issuers are required to enter into a Deposit Agreement with the depositary, which acts as the agent of the issuer for the benefit of the HDR holders. The Deposit Agreement is required to stipulate the rights, duties and obligations of the depositary, issuer, HDR holders, and custodian and to set out the fee structure of the depositary.

The Deposit Agreement must also define the procedures for the replacement or removal of the depositary and/or the custodian and should specify the procedures for amending the

agreement. The governing law of the Deposit Agreement is required to be Hong Kong law or any other law that is generally used in accordance with international practice.

**(f) Number of Authorised HDRs**

HDRs seeking to list on the Main Board can represent any number of shares. To allow for future conversions of the underlying shares into HDRs, the issuer may apply to list a greater number of HDRs than will be issued for capital raising (i.e. it may apply for "headroom"). Any combination of HDRs issued for capital raising or issued as a result of conversion of underlying shares will be permitted and listing approvals will be given for specific purposes and amounts.

No further application for listing HDRs is required for the creation of listed HDRs resulting from the conversion of shares into HDRs. Likewise, no further listing of HDRs is needed for any further issue of shares, provided that the original amount of listed HDRs is not exceeded. The depositary will monitor the level of outstanding HDRs on a day-to-day basis and will not permit shares to be converted into HDRs if this would cause the number of authorised HDRs to be exceeded. Listing must be sought for all further issues of HDRs in excess of the amount of HDRs already listed.

**(g) Rights of HDR Holders**

The rights of HDR holders are broadly equivalent, but not identical, to those of the underlying shareholders. The rights of HDR holders are contractual and arise from the deposit agreement, whereas the rights of shareholders are reinforced by statute in the issuer's jurisdiction of incorporation. The local laws may prohibit foreign investors from holding shares directly: no such restriction will however apply to the HDRs. Subject to compliance with local laws and regulations, HDR holders who want to enforce their rights as shareholders may choose to convert their HDRs into shares of the issuer.

As regards voting rights, the depositary will send information on resolutions and voting procedures to the HDR holders and will pass the HDR holders' voting instructions back to the issuer.

**LISTING MINING AND NATURAL RESOURCES COMPANIES**

The particular advantage of qualifying as a Mineral Company for a company seeking a Main Board listing is the opportunity to obtain a waiver from the requirement to meet the financial tests of Main Board Rule 8.05. A Mineral Company is a company whose Major Activities (whether directly or through a subsidiary company) include exploration for, and/or extraction of, natural resources such as minerals or petroleum. A Major Activity is one representing 25% or more of the total assets, gross revenue or operating expenses of the applicant and its subsidiaries.

As mentioned above, a Mineral Company will qualify for a waiver of the financial test requirements if it establishes to the Exchange's satisfaction that its directors and senior management, taken together, have a minimum of 5 years' experience relevant to the exploration and/or extraction activity that the Mineral Company is pursuing (Main Board Rule 18.04). Details of such experience must be included in the applicant's listing document. Other key requirements that must be satisfied by a new applicant Mineral Company are set out below.

## **Portfolio of Indicated Resources or Contingent Resources Requirement**

A new applicant Mineral Company is required to have at least a portfolio of Indicated Resources (in the case of minerals) or Contingent Resources (in the case of petroleum) that are identifiable under one of the accepted reporting standards and substantiated in the report of an independent expert (a **Competent Person**). The definition of Indicated Resources is based on the one in the 2004 edition of the Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves (**JORC Code**). The definition of Contingent Resources is based on the one in the Petroleum Resources Management System of September 2007 (**PRMS**). The portfolio is also required to be meaningful and of sufficient substance to justify a listing. We have been told informally that this requirement will be satisfied in the case of a Main Board listing applicant if the HK\$200 million market capitalisation requirement will be met at the time of listing. Early stage exploration companies are thus not eligible for listing.

## **Rights of Active Participation**

A new applicant Mineral Company must also be able to demonstrate that it has the right to actively participate in the exploration for and/or extraction of resources either through:

- control over a majority (by value) of the assets in which it has invested together with adequate rights over the exploration for and/or extraction of resources. This will normally be interpreted as an interest of more than 50%. Companies must also disclose full details of their exploration and/or extraction rights; or
- adequate rights arising under arrangements acceptable to the Exchange, which give it sufficient influence in decisions over the exploration for and/or extraction of the resources. Arrangements which may be acceptable include joint ventures, production sharing contracts or specific government mandates. The Exchange has stated that it will adopt a purposive approach to determining what is appropriate in specific circumstances and places the onus on applicants to demonstrate the adequacy of their rights and sufficiency of influence.

## **SECONDARY LISTING BY WAY OF INTRODUCTION**

Companies that are already primary listed on certain stock markets recognised by the Exchange can apply for a secondary listing by way of introduction on Hong Kong's Main Board. The Exchange's key criteria for accepting a company for secondary listing is that the company is primary listed on an exchange where the standards of shareholder protection are equivalent to those available in Hong Kong. The Moscow Stock Exchange has not yet been recognised as an exchange providing the required shareholder protection standards.<sup>5</sup> Before a Russian company can be secondary listed in Hong Kong, it will be necessary to satisfy the Hong Kong Exchange as to the equivalence of its shareholder protection standards which will require a line-by-line analysis of Russian standards against those available in Hong Kong.

## **RESTRICTIONS FOLLOWING A NEW LISTING**

### **(a) Moratorium on Disposal of Shares by Controlling Shareholders**

The Listing Rules contain restrictions on the disposal of securities by controlling shareholders following a company's new listing. A "controlling shareholder" is a person (or

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<sup>5</sup> These are listed at paragraph 91 of the HKEx/SFC Joint Policy Statement Regarding the Listing of Overseas Companies.

group of persons) who can control: (a) the exercise of 30% or more of the votes at general meetings of the company; or (b) the composition of a majority of the company's board of directors. Any person shown to be a controlling shareholder by the company's listing document must not:

- (i) dispose of, or enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of the shares which the listing document shows to be beneficially owned by him during the period commencing on the date by reference to which disclosure of the shareholding of the controlling shareholder is made in the listing document and ending on the date which is 6 months from the date on which dealings in the applicant's securities commence on the Exchange; or
- (ii) dispose of, or enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of the shares which the listing document shows to be beneficially owned by him, if such disposal or the exercise or enforcement of such options, rights, interests or encumbrances, would result in him ceasing to be a controlling shareholder in the period of 6 months commencing on the date on which the period referred to in (i) above expires.

Offers for sale contained in a listing document are not subject to the above restrictions.

A controlling shareholder is allowed to purchase additional shares and to dispose of such shares during the relevant periods, provided that the minimum public shareholding requirement with respect to the issuer's shares can be met.

#### **(b) No further Issues of Shares within 6 Months of Listing**

The Listing Rules prohibit further issues of shares or securities convertible into shares of a listed issuer or the entering into of any agreement for such an issue within 6 months from the date on which dealings in the issuer's shares commence on the Exchange (whether or not such issue of shares or securities will be completed within 6 months from the commencement of dealings). There are exceptions for:

- (i) the issue of shares pursuant to a share option scheme under Chapter 17 of the Listing Rules;
- (ii) the exercise of conversion rights attaching to warrants issued as part of the IPO;
- (iii) any capitalisation issue, capital reduction or consolidation or sub-division of shares; and
- (iv) the issue of shares or securities pursuant to an agreement entered into before the commencement of dealing and disclosed in the issuer's listing document.

#### **(c) Restriction on Fundamental Change in the Nature of Business**

In the 12 months following listing, an issuer may not effect any acquisition, disposal or other transaction or arrangement (or series thereof) which would result in a fundamental change in the principal business activities of the listed issuer as described in its listing document. The Exchange may however grant a waiver from this restriction if the circumstances are exceptional and the transaction is approved by a resolution of the issuer's independent shareholders (any controlling shareholder, or if none any chief executive or directors, and their associates must abstain from voting in favour).

## THE LISTING PROCESS

### (a) Appointment of a Sponsor

A company applying to list on the Exchange must appoint one or more sponsors to assist it. Only corporate finance advisers licensed by the SFC to conduct sponsor work are permitted to act as sponsors. The sponsor must also be independent of the applicant from the date of submission of the listing application until the date of listing and must comply strictly with the Listing Rules relating to sponsors.

The sponsor is responsible for preparing the issuer for listing, the submission of the application for listing and for dealing with the Exchange on all matters concerning the application.

Additionally, the sponsor must be satisfied that the new issuer is suitable to be listed, that the information contained in the prospectus is complete and accurate in all material respects and that the issuer's directors will be able to honour their obligations under the Listing Rules post-listing.

### (b) Applying to List

The sponsor will submit to the Exchange the listing application form (Form A1), a draft of the listing document which is substantially complete except in relation to information which can only be incorporated at a later date (the **Application Proof**), all supporting documents and the listing application fee. A listing application must be submitted at least 2 months after the signing of the sponsor engagement letter, and if there is more than one sponsor, two months after the date the last sponsor to be appointed signed the engagement letter.

On applying to list, the Application Proof of the listing document is required to be published on the website of the Exchange. The information contained in the Application Proof, the Form A1 and other documents submitted with Form A1, is required to be substantially complete, except for information that, by its nature, can only be finalised and included at a later date.

If the Exchange does not consider the information to be substantially complete, it will return the listing application and all other documents to the sponsor. If an application is returned, the Exchange will publish on its website the names of the listing applicant and its sponsor(s) and the date of its decision to return the listing application (**Return Decision**). It will also refund the initial listing fee unless it returns the listing application after issuing its first comment letter, in which case the initial listing fee will be forfeited. The applicant can resubmit the Form A1 and a new Application Proof, but cannot do so until 8 weeks after the date of the Return Decision to return the listing application.

The requirement for the Application Proof to be substantially complete when it is submitted to the Exchange with the listing application means that the sponsor's due diligence process has to be front loaded, in that it should be completed before the submission of the listing application. The directors of the listing applicant are responsible for ensuring that the information in the Application Proof (and the final form listing document) is accurate and complete in all material respects and is not misleading or deceptive.

### (c) Conduct of Due Diligence

The directors of a listing applicant are primarily responsible for ensuring that the information included in the company's listing document is accurate and complete in all material respects and not misleading. Where the information contained in a listing

prospectus is untrue or misleading in a material respect, any person who authorised its issue is criminally liable unless he can prove that he had reasonable grounds to believe that the information was true. The directors of the listing applicant are potentially liable as “persons who authorise” the issue of the listing prospectus and the SFC also considers that the sponsor is within the category of persons who may be liable. The company directors may also be liable to compensate any person who suffers loss by reason of relying on an untrue statement.

The Listing Rules and Paragraph 17 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (**Paragraph 17**) also impose obligations on the listing applicant’s sponsor or sponsors to conduct due diligence on the listing applicant’s group in order to satisfy itself that the information in the listing prospectus is true and complete in all material respects.

Paragraph 17.4(a) of the Code of Conduct requires sponsors to perform all reasonable due diligence before submitting a listing application except in relation to matters that by their nature can only be dealt with at a later date. Sponsors must also ensure that all material information as a result of due diligence on the listing applicant has been included in the Application Proof.

“Matters that by their nature can only be dealt with at a later date” refer to those matters which cannot be ascertained, finalised or fulfilled at the time a listing application is submitted. Examples of such matters given by the SFC include:

- determination of the size and structure of an offering;
- preparation of an indebtedness statement or a working capital forecast; and
- a change in financial position since the most recent reporting period and changes in circumstances and developments or events arising subsequent to the submission of the application.

The Listing Rules contain a number of specific steps which sponsors should take when conducting due diligence on a new listing applicant which are set out in Practice Note 21 to the Listing Rules. Further obligations are imposed by Paragraph 17 of the Code of Conduct.

The scope of sponsors’ due diligence obligations depends on whether the information is included in an “expert section” of the listing document – i.e. any report, valuation or opinion made by an expert (e.g. accountants, property valuers or lawyers) who have consented to the inclusion of their report, valuation or opinion in the listing document. In respect of “expert sections” the requirement is that sponsors conduct due diligence so that, at the time of issue of the listing document, the sponsor (as a non-expert) has no reasonable grounds to believe and does not believe that the information in the expert report is untrue, misleading or contains any material omissions.

The main emphasis in relation to experts reports is that sponsors cannot take them at face value. In order to rely on an expert report, the sponsor must perform due diligence on the report in four key areas:

- (i) the expert’s qualification, experience and independence;
- (ii) the expert’s scope of work;
- (iii) the bases and assumptions underlying the report; and
- (iv) a review of the expert report in the light of all other information known to the sponsor to identify any inconsistency or irregularity.

Non-expert sections are, as the name suggests, all sections of the listing document which

do not comprise expert reports. The standard required of the sponsor is that it should “have reasonable grounds to believe and should believe that:

- (i) the information in the non-expert sections of the listing document is true, accurate and complete in all material respects and not misleading or deceptive in any material respect;
- (ii) there are no matters or facts the omission of which would make any information in the non-expert sections of a listing document or any other part of the listing document misleading in a material respect”.

Sponsors must approach due diligence with professional scepticism and a questioning mind. The sponsor must also undertake independent verification of all material information, including documents provided, and statements and representations made, by the listing applicant and its directors.

In respect of each listing assignment, a sponsor is required to keep records, including relevant supporting documents and correspondence, within its control relating to matters such as:

- (i) the transaction team and any subsequent variations within the transaction team;
- (ii) a due diligence record including the due diligence plan and changes to the due diligence plan and reasons for them;
- (iii) the bases for the opinions, assurances and conclusions required under paragraph 17 of the Code of Conduct;
- (iv) the results of due diligence performed together with its assessment of these results.

The records of the bases for the opinions, assurances and conclusions required should include internal discussions and any actions taken prior to these opinions and assurances being given or conclusions being reached.

A complete set of a sponsor’s records in relation to a listing assignment must be retained in Hong Kong for at least 7 years after completion or termination of the relevant transaction.

As part of its due diligence obligations, the sponsor is required to satisfy itself as to matters such as:

- the suitability of the listing applicant and its business for listing. Factors which the Exchange considers in relation to suitability are set out in its Guidance Letter GL68-13;
- that the listing applicant satisfies the criteria for listing;
- that the applicant has established procedures, systems and controls for complying with the Listing Rules;
- that the applicant’s directors collectively and individually have the experience, qualifications and competence required for a director of a Hong Kong listed company.

Paragraph 17 also sets out specific requirements on particular aspects of due diligence. For example, Paragraph 17.6(f) sets out the interview practices that a sponsor is expected to adopt in its interviews of the applicant’s customers, suppliers, franchisees and distributors. For example, Paragraph 17.6(f)(i) requires a sponsor to select interviewees independently based on objective and proportional criteria, for example, those with whom the listing applicant has entered into high value transactions or entities with special or unusual characteristics. Sponsors are required to carry out interviews directly with the person or entity selected with minimal involvement of the listing applicant.

Following an interview, a sponsor is required to follow up on any incomplete or

unsatisfactory responses or outstanding matters and must keep a reasonably accurate and complete record of the interview.

The requirements on due diligence set out a number of standards that sponsors are expected to achieve without much practical guidance as to how those standards are expected to be achieved. For that reason, Charltons acted as the co-ordinating law firm in producing a set of “Hong Kong Due Diligence Guidelines” which set out what is considered to be “good market practice” in the conduct of IPO due diligence for the purposes of meeting the standards imposed by the Listing Rules and Paragraph 17. These were produced by a group of some 50 investment banks, 20 law firms and representatives of the Big 4 accounting firms, all active in the Hong Kong IPO market. The guidelines are available free online at [www.duediligenceguidelines.com](http://www.duediligenceguidelines.com).

## Listing Process for Main Board

The following chart summarises the process for a listing application for shares on the Main Board:

Process	
<b>Appointment of Sponsors</b>	
<ul style="list-style-type: none"> <li>Appointment of a sponsor at least 2 months before submission of an application and to notify the Exchange</li> </ul>	
	
<b>Submission of the Listing Application</b>	
<ul style="list-style-type: none"> <li>Submit listing application Form A1, Application Proof (AP) and all other relevant documents under Main Board Listing Rules 9.10A(1)</li> <li>Information must be substantially complete</li> </ul>	
	
<b>Accepted</b>	<b>Returned</b>
	
<b>Detailed Vetting</b>	<b>Accelerated review process</b>
<p>Qualitative assessment</p> <ul style="list-style-type: none"> <li>Eligibility</li> <li>Suitability</li> <li>Sustainability</li> <li>Compliance with Listing Rules, Companies (Winding Up and Miscellaneous Provisions) Ordinance and Securities and Futures Ordinance</li> <li>Material disclosure deficiencies</li> </ul> <p>Application may still be returned by SFC or HKEx for not being substantially complete</p> <p><b>Timing of Comments</b></p> <ul style="list-style-type: none"> <li>First round of comments - within <u>10 business days</u> from receipt of application</li> </ul>	<ul style="list-style-type: none"> <li>Available for reviewing the Listing Division's decision to return a listing application</li> <li>Applicant and sponsor(s) has the right to have a Listing Division's decision to return an application and Listing Committee's decision that endorses the Return Decision reviewed</li> </ul> <p>Two levels of review:</p> <ul style="list-style-type: none"> <li>a review of the Return Decision by the Listing Committee</li> <li>a review of a Listing Committee's decision <b>endorsing a Return Decision by the Listing (Review) Committee</b></li> </ul>

<ul style="list-style-type: none"> <li>▪ Second and further rounds of comments (if any) <u>within 10 business days</u> from receipt of reply to previous comment letter</li> <li>▪ Expect replies from sponsor to be full and complete, otherwise the Exchange will not start to vet (e.g. will not accept replies such as “to be provided in due course”)(except updated financial information under Guidance Letter GL6-09A)</li> <li>▪ Competent persons report is reviewed by an external mining consultant selected from a panel. Although nearly all consultants agreed to the streamlined process, there may be cases where some delay may be expected</li> </ul> <p><b>Expected Hearing Timetable</b></p> <p>Depending on the sponsor’s response time and quality of response</p> <ul style="list-style-type: none"> <li>▪ Assumes sponsor takes 5 business days to respond to each of the two rounds of comments, an application can be presented to the Listing Committee in around 40 business days from the date of listing application</li> <li>▪ In the case where only one round of comment is raised and sponsor takes 5 business days to respond, an application can be brought to the Listing Committee in around 25 business days</li> <li>▪ <b>Publication of AP-Publication</b></li> </ul>	
	
<b>Hearing</b>	<b>8 weeks moratorium</b>  <b>(after any accelerated review process)</b>
	

<p><b>Post-Hearing Information Pack (PHIP)</b></p> <ul style="list-style-type: none"> <li>▪ Please view the Guidance on logistical arrangements for publication of Application Proofs, Post Hearing Information Packs and related materials on the Exchange's website for listing applicants</li> </ul>	
	
<p><b>Dealing of Shares Commences</b></p>	

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