February 2, 2012

Hong Kong Capital Market Developments

A. Property valuation and disclosure regime streamlined

Simplified regime for property valuation in an IPO took effect on 1 January 2012

Following the Consultation Conclusions on Proposed Changes to Property Valuation Requirements jointly issued by The Hong Kong Securities and Futures Commission ("SFC") and the Hong Kong Stock Exchange ("HKEx") in October last year, the relevant new rules took effect on 1 January 2012.

For many years, listing applicants and listed companies have been required to include in their prospectuses and transaction documents an independent property valuation report. Based on the hair-trigger concept of "interests in land or buildings", companies could be unpleasantly surprised to find themselves being compelled to commission a full-fledged property valuation report for such property interests as office space owned for use by the business, or retail premises held under a license.

The SFC and HKEx has for years worked to rationalize the process. Under the new regime, relaxations to the property valuation and relevant disclosure requirements are available to companies, based on whether the property in question is material, and (in the case of listing applicants) whether the interest is held for a "property activity" or "non-property activity".

For a listing applicant, if an interest is held for "non-property activities" – which basically means that the property is not held as an investment to produce rental income or capital gain – the disclosure requirements are now less onerous as a full valuation report is required to be included in the prospectus only for any such interest which individually has a carrying amount of 15% or more of the company's total assets. On the other hand, if the interest is held for "property activities", a full valuation report must be prepared and be disclosed in the prospectus, subject to a de minimis exemption. Under this exemption, if the carrying value of an individual property interest accounts for less than 1% of the company's total assets, no valuation is required until a 10% cap is reached. The regime is further simplified so that for any property interest with a market value of less than 5% of the company's total property interests, the full valuation report still has to be prepared but need not be disclosed in full in the prospectus. In this case, only summary disclosure is required and the full valuation report should be made available for inspection.

For companies already listed, similar simplifications have been made to the valuation report requirements under the rules for sizeable property businesses acquired or disposed of by the listed group.

B. Significant regulatory updates from the last quarter

Amendments to corporate governance provisions

October 2011 – After more than a year's work, HKEx published the consultation conclusions to the corporate governance provisions of the Listing Rules. Most of the proposed changes will be adopted, subject to certain modifications.

Most of the amendments to the Listing Rules took effect on 1 January 2012. The implementation dates for other amendments are as follows:

- Code on Corporate Governance Practices – 1 April 2012
- Listing Rule 3.10A requiring independent non-executive director to comprise 1/3 of the board – 31 December 2012
- training for company secretary – staggered implementation according to date of appointment

- other amendments to the Listing Rules – 1 April 2012

For more details, please see full text of the rule changes in English and the implementation dates and relevant FAQs.

HKEx introduces streamlined Main Board "professionals-only" debt listings

November 2011 – The new rules in the Consultation Conclusions on Proposed Changes to Requirements for the Listing of Debt Issues to Professional Investors Only issued by HKEx became effective on 11 November 2011. The purpose of the new rules is to remove requirements that HKEx considers, after consultation with law firms, accounting firms and other professional bodies, as inapplicable to offers of debt securities which are only made to professional investors.

HKEx aims to streamline and clarify the HK listing process under the new rules which provide, among other things:

- **Faster approval process**: The listing of debt marketed to professionals (excluding high net worth individuals) can be approved by the Listing Division, an executive department within HKEx itself, as opposed to the Listing Committee which only meets once a week.
- **Simpler disclosure obligations**: The detailed disclosure requirements for listing documents have been replaced with a simple obligation to include information that is "customary for offers of debt securities to professionals".
- **Streamlined vetting of listing document**: There will be no substantive vetting of the listing document. Vetting is only required for (i) listing eligibility criteria, (ii) standard disclaimers and (iii) responsibility statements in the listing document.

The streamlined procedure is expected to make HKEx debt listings more attractive to Asian market issuers executing cross-border debt offerings.

Additional requirements for structured contracts listing applications

December 2011 – HKEx revised its 2005 Listing Decision 43-3 (LD43-3), regarding the circumstances in which a company operated under structured contracts or variable interest entity ("VIE") arrangements may be accepted for listing in Hong Kong. The requirements stated in the original decision remain unchanged.

The additional materials (appearing in paragraph 16 onwards in the revised decision) set out a number of additional points following relevant statements by the Listing Committee in November 2011. The additional requirements for the listing applicant and the sponsor include:

- providing reasons for the contracts
- unwinding the contracts as soon as the law allows the business to be operated without them
- inserting certain mandatory provisions into the contracts (*e.g.,* a power of attorney giving the applicant's directors the power to exercise the rights of the operating company's shareholders)

HKEx consults public on environmental, social and governance reporting

December 2011 – HKEx issued a new consultation on rules to encourage listed companies to improve their environmental, social and governance (ESG) reporting. The proposal is to introduce a user-friendly ESG Guide to raise awareness on the following issues: workplace quality, environmental protection, operating practices and community involvement.

The proposed ESG Guide will not impose mandatory measures but will only recommend best practices for listed companies. Listed companies may commence ESG reporting at any time (which is encouraged by HKEx) but once an issuer has commenced reporting, it will be expected to continue to do so regularly.

The consultation in ESG reporting will close on 9 April 2012.

C. Recent HKEx listing decisions and guidelines

In the 4th quarter in 2011, HKEx issued a number of important listing decisions and guidelines. Set out below are some highlights.

Listing decision on fund manager as connected persons

In LD22-2011 HKEx examined the circumstances in which a fund manager holding shares in a listed company would not be considered as a connected person of that company.

Listing decision on restoring the public float

In LD23-2011 HKEx said that a listed company was required to restore its public float to at least 25% before resumption of trading. This was the case even though Listing Rule 13.32 states that HKEx will normally only require suspension of trading when the public float falls below 15%.

Guideline on restaurant-operating listing applicants

HKEx has issued a new guideline (GL28-12) on prospectus disclosure where the issuer is a food and beverage restauranteur. The guidelines spell out a number of items that HKEx believes should be disclosed in detail in the prospectus to the extent they are material for the business.

New guide on drafting “summary” section in a prospectus

HKEx has issued a new guideline (GL27-12) on drafting the “Summary and Highlights” section in a prospectus. The guidance letter makes it clear that the summary section should not include cut and pasted paragraphs from elsewhere in the prospectus and sets out certain things that should not appear in the summary section (*e.g.,* detailed financials).

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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