
A newsletter to help market participants better understand
the Dual Filing arrangements

Cases handled

In the six months ended March 2009, the SFC received, via The Stock Exchange of Hong Kong Ltd, 21 listing applications. They include three applications by companies listed on the Growth Enterprise Market (GEM) to transfer to the Main Board.

Of the 21 applications, the SFC commented on 11 cases, and deferred raising comments on four others until substantial improvements had been made to rectify the serious deficiencies in the documents submitted. The average response time was six working days.

From April to September 2008, the SFC received 66 listing applications and commented on 43 cases¹.

Conduct of sponsors

The SFC noted with concern various deficiencies in the initial draft prospectus, which suggested that the sponsors might not have exercised due care in advising on the preparation of the initial listing applications.

In an application by a Mainland property developer, piecemeal information on its key property development projects was found scattered over different parts of the initial draft prospectus. The prospectus also omitted the applicant's long history of regulatory breaches, which had exposed it to severe penalties and potential disruption of operations, and various legal proceedings relating to the timeliness and quality of the properties it developed. The applicant was in a net current liabilities position but the prospectus failed to demonstrate whether it could manage to continue to finance its operations.

These issues are relevant to enable investors to assess the business conduct of the applicant and the risks of investing in it. The extent of deficiencies in the listing application raised doubts as to whether the sponsors had critically assessed the applicant's business viability and ensured the disclosure of sufficient relevant information for investors to make such an assessment.

In some other cases, inaccuracies that the sponsors claimed to be clerical or inadvertent could have been severely misleading had they not been identified by the regulators and subsequently rectified.

In one of the cases reviewed, the listing applicant claimed to be a leader in the market, but this was found to be related to only a segment of the market. In a similar case, the statements in relation to the competitive strengths of the listing applicant were not supported by facts nor relevant to its business at all.

In another case, the initial draft prospectus disclosed that the listing applicant has no controlling shareholders, but following enquiries by the regulators, the sponsor submitted that two shareholders, including one previously described as a passive investor, were at all material times acting in concert and should have been disclosed as the controlling shareholders throughout the track record period.

¹ Please see press release dated 3 December 2008 for background statistics.

Sponsors should examine with professional scepticism the information given to them by listing applicants or other parties in the course of their due diligence. In one case, the sponsor submitted information provided by the listing applicant in response to certain serious allegations raised in a complaint lodged by an insider, but the information was found to be incomplete and inadequate.

Compliance with laws and regulations in relevant jurisdictions

Listing applicants are often subject to rules and regulations specific to the industry and country in which they operate. Complete and accurate disclosure is important for an informed understanding of the regulatory environment in which the listing applicants operate and the legality of their businesses.

In one case, the listing applicant operates its principal business in an overseas jurisdiction, which prohibits foreign controlling ownership in that business. However, the applicant claimed to have control because of an arrangement with a local employee from that jurisdiction. The listing application made no disclosure about the fact that the relevant law explicitly prohibits “nominee” arrangements and that there have been a number of investigations against companies suspected of breaching the relevant law.

This piece of key information was only revealed following persistent enquiries by the regulators about inconsistent explanations from the sponsor and successive revisions of the legal opinions by the applicant’s legal advisers on the laws of the foreign jurisdiction. It also transpired that certain key elements of the arrangement might not be legally enforceable. The potential result could be the listing applicant losing control over its principal business, the very basis on which the listing was sought. The application was formally withdrawn leaving these issues unresolved.

Legal and regulatory compliance issues can be complicated and subject to legal uncertainties that only legal experts can opine on. It is important that complicated or unfamiliar legal issues, in particular any key aspects which are subject to interpretation, are clearly identified and brought to the attention of potential investors. Listing a company with an untenable corporate structure is contrary to the interests of potential investors.

The Dual Filing Update is available under ‘Speeches, Publications & Consultations’ – ‘Publications’ of the SFC website at <http://www.sfc.hk>.

Feedback and comments are welcomed and can be sent to dualfiling@sfc.hk.

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