中州國際融資有限公司
CENTRAL CHINA INTERNATIONAL CAPITAL LIMITED

6 May 2021 **BY EMAIL (ECM_DCM_consultation@sfc.hk)**

The Securities and Futures Commission
54/F, One Island East
18 Westlands Road
Quarry Bay
Hong Kong

Dear Sirs,

Re: Consultation Paper on (i) the Proposed Code of Conduct on Bookbuilding and Placing Activities in Equity Capital Market and Debt Capital Market Transactions and (ii) the "Sponsor Coupling" Proposal (the "Consultation Paper")

INTRODUCTION

With reference to the Consultation Paper, which was published by the Commission on 8 February 2021, we set out in the table below our replies to each of the 24 questions in the Consultation Paper for your consideration. Unless otherwise indicated, the abbreviations used in our replies follow that in the Consultation Paper and bear the same meanings.

REPLY TABLE

No.	Contents	
1.	Do you consider the definitions of "bookbuilding activities" and "placing activities" to be clear and sufficient to cover key capital raising activities? If not, please explain.	
	Ans:	We consider that the definitions of "bookbuilding activities" and "placing activities" proposed in paragraphs 42-44 of the Consultation Paper to be clear and consistent with market understanding of these two phrases. The definitions are also sufficiently broad to cover almost all of the key capital raising activities and thus obviate the need for any future amendments to the definitions unless the evidence is so strong to justify any revisions.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

No.	Contents	
2.	Do you agree with the proposed scope of coverage for both ECM and DCM activities?	
	Ans:	Agree. The proposed scope of coverage for both ECM and DCM activities in paragraphs 46-49 of the Consultation Paper is in line with market understanding of the scope of such activities and is sufficiently broad.
3.	Do you consider the role of an OC to be properly defined? If not, please explain.	
	Ans:	We consider that the role of an OC as described in paragraph 53 of the Consultation Paper to be sufficiently broad to cover almost all of the activities carried out by an OC in a share offering and a debt offering. Accordingly, we believe that the OC's role is properly defined in the Consultation Paper.
4.	Do you agree that the appointments of OCs and other CMIs and the determination of their roles, responsibilities, and fee arrangements, should all take place at an early stage? If not, please explain.	
	Ans:	Agree in principle, but in practice, market conditions and sentiment change rapidly, and the OC and syndicate structure should remain as flexible as possible in order to cope with changing conditions.
5.	Do you agree that an OC should provide advice to the issuer on: (i) syndicate membership and fee arrangements; (ii) marketing strategy; and (iii) pricing and allocation? If not, please explain. What else should the OC advise the issuer about?	
	Ans:	Agree, for the reasons cited in paragraphs 70-75 of the Consultation Paper. We are also of the view that an OC should advise the issuer of all legal and regulatory requirements in relation to an offering.
6.	Do you agree that a private bank should not pass on to investor clients any rebates provided by the issuer? If not, please explain.	
	Ans:	Agree, for the reasons stated in paragraphs 32, 83 of the Consultation Paper, namely, prevention of some investors paying in effect a lower price to participate in an offering, resulting in unfair treatment to other investors.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

7.	Do you agree that an OC should provide relevant information to CMIs to enable them to identify investor clients which are Restricted Investors in share offerings or have associations with the issuer in debt offerings? If not, please explain.	
	Ans:	Agree, for the reasons set out in paragraphs 86-88 of the Consultation Paper.
8.	Do you agree that information about the underlying investors should be provided to an OC by CMIs placing orders on an omnibus basis when they place orders in the order book? If not, please explain.	
	Ans:	Agree, for the reasons cited in paragraphs 91- 92 of the Consultation Paper, namely, to reduce concerns on "poaching" of clients expressed by some CMIs and to ensure that an OC would be able to identify duplicated orders.
9.	Do you think there would be difficulties in a large IPO or debt offering for OCs to remove duplicated orders and identify irregular or unusual orders in the order book? If so, please provide examples.	
	Ans:	To ensure fair allocation of orders to investors free of the types of conflicts of interest described in paragraph 96 of the Consultation Paper, OCs are duty-bound to remove duplicated orders and identify irregular or unusual orders in the order book notwithstanding any difficulties that OCs might encounter in doing so.
10.	Do you agree that OCs and CMIs should not accept knowingly inflated orders? If not, please explain.	
	Ans:	Agree. Knowingly inflated orders undermine the price discovery process and the placement of them by CMIs could mislead investors and, depending on the sufficiency of the evidence, might indicate possible fraud committed by CMIs and the creation of a false market on the shares in contravention of the Listing Rules. That said, the CFO of a Chinese real estate company was quoted by a financial industry publication as saying that "some investors tend to inflate orders to secure their expected allocation when the market or order book is strong … it is kind of showing respect to the issuer".[1] In fact, according to that industry publication, over-inflation is less common in difficult markets as investors do not want to be over-allocated.[2]

[1] Jonathan Breen & Morgan Davis, "HK SFC Plans Overhaul of ECM, DCM Syndicates" <https://www.globalcapital.com/article/b1qhzhkqq899kh/hk-sfc-plans-overhaul-of-ecm-dcm-syndicates>
[2] Ibid.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

11.	Do you agree that OCs should ensure the transparency of the order book? If not, please explain.	
	Ans:	Agree. As the head of syndicate which is responsible for the overall management of an offering, coordination of bookbuilding or placing activities conducted by the syndicate and the provision of advice to the issuer, OC should be the party to ensure the transparency and accuracy of the order book.
12.	Do you agree that "X-orders" should be prohibited? If not, please explain.	
	Ans:	Agree, for the reasons cited by the Commission in paragraphs 28-29, 91 of the Consultation Paper. In addition, bankers claim that X orders are often misleading, with some of such orders being placed to receive a favourable allocation by implying that they came from an important investor, while others may conceal that they are proprietary or come from a related party, such as a bank's asset management arm.[3] An Asian DCM syndicate head was quoted by a financial industry publication as saying that "[X order] creates an incentive in terms of allocations which is not in the interests of the market. If I am B&D [billing and delivery] bank, it's my responsibility to judge the quality of the book, and I can't do it if there are X orders".[4] So by ruling out "X-orders", the Commission can be seen as encouraging more transparency in order books, facilitating the heads of syndicate to assess real demand or identify unusual or irregular orders and ensuring the right of issuers to know their shareholders is respected.
13.	Do you agree that OCs and CMIs should be required to establish and implement allocation policies? If not, please explain.	
	Ans:	Agree. We believe that allocation policies should set out principles and rules for OCs and CMIs to follow, and that OCs need to communicate allocation policies to issuer after books are open. Allocation policies should allow some flexibility for OCs and CMIs to make judgement calls based on their own knowledge and experience.
14.	Do you agree that client orders must have priority over proprietary orders at all times? If not, please explain.	

[3] Daniel Stanton & Fiona Lau, "Hong Kong Outlines Syndicate Shakeup" <https://www.ifre.com/story/2730289/hong-kong-outlines-syndicate-shakeup-v84vjwyp6l>.
[4] Ibid.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

	Ans:	Agree. This is consistent with the requirements of paragraph 9.1 of the *Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission* ("Code of Conduct") regarding priority for clients orders.
15.	Do you agree that proprietary orders can only be price takers? If not, please explain.	
	Ans:	Agree, for the purpose of reducing the possibility that the proprietary orders might impact on the price discovery process and mitigating the effect of the consequent conflicts of interest if CMIs exercise control over bookbuilding and making pricing or allocation recommendations to issuers.
16.	Do you agree that a CMI's proprietary orders and those of its Group Companies should also include orders placed on behalf of funds and portfolios in which a CMI or its Group Companies have a substantial interest? If not, please explain.	
	Ans:	Agree, but need further information on what constitutes substantial interest as referred to in the question.
17.	Orders received and entries placed in the order book are subject to constant amendments and updates throughout the bookbuilding process. Do you think it is feasible for the OC and CMIs to maintain records which evidence every change? If not, please explain.	
	Ans:	Keeping a reliable and complete audit trail of orders received for regulatory review or inspection by regulators is part of the responsibilities of a licensed intermediary. Such records may be saved in either the CMI's excel files or Dealogic. In this connection, CMIs and OCs should be required to review existing policies and procedures to determine if they are already fit for purpose, and consider if any enhancements to existing internal control procedures would be necessary and if so, implementation plans.
18.	Do you agree with the scope of fee-related advice to be provided by an OC to an issuer? If not, please explain.	
	Ans:	Agree. However, it seems that the proposed scope of fee-related advice is already reflected in current market practice.
19.	Would you envisage substantial practical difficulties in an issuer determining the syndicate membership, the ratio between the fixed and discretionary portions of the fees to be paid to all syndicate CMIs and fixed fees allocation four clear business days before the Listing Committee Hearing? If yes, please cite examples.	

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

	Ans:	We would envisage that the issuer might encounter difficulties in determining syndicate membership and fees allocations on at least 2 grounds: (i) market conditions and sentiment change rapidly, so it is difficult and impractical to settle on the ratio between the fixed and discretionary portions of the fees to be paid to all syndicate CMIs participating in the offering and the allocation of fixed fees to syndicate CMIs and submit such information to the Commission four clear business days before the Listing Committee Hearing; and (ii) changes in market conditions and sentiment might necessitate the appointment of new CMIs by the issuer and the syndicate. However, as the listing timetable progresses, the issuer could (i) appoint additional syndicate CMIs (see paragraph 129 of the Consultation Paper); and (ii) make alternations to fee allocations (see paragraph 136 of the Consultation Paper), we believe that the difficulties could be overcome as a result.
20.	Would you envisage substantial difficulties in issuers determining the allocation of discretionary fees and the fee payment schedule no later than listing? If yes, please cite examples.	
	Ans:	No. We do not envisage such difficulties as allocations of the discretionary fees to each syndicate CMI are determined after order allocations are completed, which is the market norm in respect of most IPO transactions.
21.	Do you agree that (i) the syndicate membership (including the names of OCs) should be disclosed at an early stage; (ii) the total fees to be paid to all syndicate CMIs participating in the offering for the international placing tranche should be disclosed in the prospectus; and (iii) the total monetary benefits paid to each syndicate CMI should be disclosed after listing? If not, please explain.	
	Ans:	(i) Agree, for the reasons cited by the Commission in paragraph 139(a) of the Consultation Paper. It seems that ECM bankers generally welcome the Commission's push to determine the roles and fees earlier in the offering.[5] That said, it should be noted that there are circumstances under which the disclosure of membership of the syndicate at an early stage of the offering might be inappropriate, e.g., changes in market conditions and sentiment may necessitate the addition of new CMIs and the naming of new OCs by the issuer and the syndicate.

[5] See Stanton & Lau, above n. 3.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

		(ii) Disagree. We consider that the amount of total fees to be paid to all syndicate CMIs participating in the offering for the international placing tranche should not be disclosed in the prospectus as such fee is fixed at a stage after the printing of the prospectus. We also believe that more flexibility in the fee structure is required to motivate members in the syndicate to successfully complete the offering to the satisfaction of the issuer. The disclosure of such information publicly, e.g. in the prospectus, might fetter the development of a flexible fee structure for syndicate CMIs. (iii) Disagree, as such information should be regarded as a kind of commercial secret and should not therefore be disclosed publicly.
22.	Do you agree with the "sponsor coupling" proposal? If not, please explain.	
	Ans:	Agree in principle. According to the Commission, the objective of the "sponsor coupling" proposal ("Coupling Proposal") is to ensure that Sponsors would be less inclined to compromise their due diligence efforts in large IPOs given that the much higher fees generated from acting as the head of the underwriting syndicate at the same time would compensate for the substantial due diligence costs incurred for the IPO and the onerous legal and regulatory consequences arising from regulatory breaches.[6] Although the appointment of a Sponsor OC might increase the transparency in respect of the offering, which is in the best interests of investors, we have the following reservations over the Coupling Proposal. Firstly, Sponsors are already required by the Code of Conduct to manage the overall offering in the interests of investor clients and issuers. It seems unnecessary to combine the Sponsor role with the OC role to enhance the ability of the Sponsor to discharge responsibilities which it is already required to do by its mandate. This, together with the possibility that many small boutique Sponsor firms without ECM capability might be driven out of the market if the Coupling Proposal were implemented in full, lessens the force of the Commission's case for the Coupling Proposal.

[6] See paragraphs 140-143 of the Consultation Paper. As quoted by the Commission in the Consultation Paper, for the 9 months ended 30 September 2020, the sponsor fees for 99 IPOs were on average HK6.3 million whereas the average underwriting fixed fees were HK$43.9 million.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

		Secondly, the proposal that OC should ensure that it or a group company act as the Sponsor might only give the OC or the group company too much bargaining power in respect of the offering without the appropriate check and balance. Combining the OC and Sponsor roles might, it should also be noted, create internal conflicts as the Sponsor could be pressurised to compromise its independence in order to win and hold on to the underwriting mandate.[7] Thirdly, issuer should be entitled to choose the Sponsor it prefers to engage based primarily on the quality and standard of work shown by the proposed Sponsor in past transactions. There is no guarantee that the OC or its group company would be able to attain the standard of Sponsor work required by the issuer. It would work against the best interests of the issuer if issuer were obligated to appoint as Sponsor an intermediary which fails to impress with its work quality and standards but happens to have already been appointed as the OC for the offering. In our view, the appointment of the OC and the Sponsor should be subject to separate considerations. Finally, insofar as the Commission's claim in paragraph 144 of the Consultation Paper is concerned, we are unable to agree as appropriate that the Sponsor OC should submit to the Commission the information discussed in paragraphs 135, 136 and 138 of the Consultation Paper within the prescribed timeframe. It should be noted that the financial market is subject to frequent changes caused by, e.g., prevailing market conditions and sentiment, adjustments in macro-economic factors as well as changes in the intermediary's personnel. It would normally take more than six months for a listing application to reach the Listing Committee Hearing stage after filing, and a 6-month period is in our view a sufficient period, instead of the prescribed time frame, for Sponsor OC and/or the issuer to determine, confirm and submit the information required in paragraphs 135, 136 and 138. We respectfully submit that the prescribed time frame is impractical in the financial services industry and that the requirement to comply with it works against the interests of the syndicate and Sponsor OC.

[7] Peter Guy, "What SFC's Latest Consultation Means for IPO Sponsors" <https://citywireasia.com/news/what-sfcs-latest-consultation-means-for-ipo-sponsors/a1470048>.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

23.	Do you think one Sponsor OC is adequate or should more OCs be required to act as sponsors? For example, should the majority of OCs be required to act as sponsors (i.e., if the issuer appoints three OCs, two must also act as sponsor)? Please explain.	
	Ans:	It depends on the size of the syndicate and deal dynamic. Hence, we do not believe that a compulsory requirement on the number of OCs, as suggested in this question, is required for any offering. The engagement of more Sponsor OCs has benefits in that it may act as a check and balance on the influence of the single Sponsor OC appointed for the offering, but may also cause duplication of work among themselves and result in inefficiency. If it is necessary to appoint more than one Sponsor CO, delineation of work among the Sponsor COs must be clearly spelt out, e.g. who acts as the key contact point to the issuer and the regulators and who leads the overall IPO process amongst the Sponsor COs.
24.	Do you have any comments on the proposed implementation timeline?	
	Ans:	Yes. If the Commission's proposals in the Consultation Paper were fully adopted, players in the financial services industry would in our view find it extremely difficult to comply with the proposed 6-month implementation timeline given the amount of work involved and the associated costs incurred in comprehensively updating their internal control policies and procedures, standard form documentation and workflows to comply with the requirements of the Proposed Code. We respectfully submit that at least a 12-month period instead of the proposed 6-month period would be a more realistic implementation timeline. We further respectfully submit that after the 12-month period has expired, any application for extension of the implementation timeline by industry players, particularly small and medium sized ones, should be considered favourably if applicants could provide valid reasons for seeking to extend the implementation timeline.

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk

CONCLUSION

We are in general support of the suggested measures in the Proposed Code, which, according to the Commission, are aimed at, among others, installing a transparent and robust price discovery process through bookbuilding and ensuring securities are fairly allocated. The achievement of these objectives is critical for the development of a healthy capital market in Hong Kong, and "consistent with the global regulatory trend and expected to help boost overall investor confidence in the market".[8]

However, as expressed in our reply to Question 22, we have certain reservations regarding the Coupling Proposal. We are also concerned with the heavy workload and the associated costs in ensuring compliance with the Proposed Code, which may not work in the best interest of market development (see our reply to Question 24). In the final analysis, we need to strike a balance between the development of a viable and robust capital market on the one hand and the incurrence of onerous compliance costs on the other.

Yours faithfully,
For and on behalf of
Central China International Capital Limited

[8] See Breen & Davis, above n. 1, quoting Frank Bi, a partner at Ashurst Hong Kong

Suites 1505-1508,Two Exchange Square, 8 Connaught Place, Central, Hong Kong
香港中環康樂廣場8號交易廣場二期1505至1508室
Tel 電話: (852) 2500 1375 Fax 傳真: (852) 2250 5581
Website 網址: www.ccnew.com.hk