

Client Alert

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Shanghai Stock Exchange launches Science and Technology Innovation Board

A quick guide on the key provisions and requirements

Overview

On 1 March 2019, the China Securities Regulatory Commission (**CSRC**) and the Shanghai Stock Exchange (**SSE**) issued a series of immediately effective listing rules and guidance materials of the Science and Technology Innovation Board ("**Innovation Board**"). These documents include:

- Administrative Measures for the Registration of Initial Public Offerings on the Science and Technology Innovation Board (for Trial Implementation) 《科创板首次公开发行股票注册管理办法（试行）》
- Measures for Continuous Regulation of Companies Listed on the Science and Technology Innovation Board (for Trial Implementation) 《科创板上市公司持续监管办法（试行）》
- Special Provisions on the Trading of Shares on the Science and Technology Innovation Board 《上海证券交易所科创板股票交易特别规定》
- Review Rules of Issuance and Listing of Shares on the Science and Technology Innovation Board 《上海证券交易所科创板股票发行上市审核规则》
- Listing Rules of the Shanghai Stock Exchange Science and Technology Innovation Board 《上海证券交易所科创板股票上市规则》
- Implementing Measures for Issuance and Underwriting of Shares on the Science and Technology Innovation Board 《上海证券交易所科创板股票发行与承销实施办法》

On 3 March 2019, based on the immediate needs of issuing, listing and underwriting shares, SSE released the following documents:


- Guidelines for Listing Sponsorship on the Science and Technology Innovation Board 《上海证券交易所科创板企业上市推荐指引》 ("**Sponsorship Guidelines**")
- Questions and Answers on Review of Issuance and Listing of Shares on the Science and Technology Innovation Board 《上海证券交易所科创板股票发行上市审核问答》 ("**Q&A**")

This client alert will discuss the key issues of the Innovation Board in terms of (1) the issuance and listing of shares and (2) post-listing regulatory requirements.

Part One: Issuance and Listing

1. Positioning

The Innovation Board is positioned to encounter the challenges of international technological advancement, economic competitions and significant national needs. Priorities are given to technological and innovative companies that align with national strategies, own core technologies and demonstrate outstanding scientific and technological



capabilities. These companies usually rely on their core technologies to develop their businesses, operate under a stable business model, enjoy a high market acceptance, maintain a reputable social image and possess high developmental potential.

Question: How to grasp the positioning of the Innovation Board?

Answer: Q&A number 9 recommends issuers and sponsors to consider the following factors seriously:

1. Level of alignment between national strategies and the issuer's industry and development trend;
2. Position of the issuer's core technologies in terms of both national and international development;
3. Demonstrations of the issuer's core competitiveness and level of innovative capabilities, such as professional qualifications, significant awards, research skills of core technicians, investment in R&D, progress and achievements in R&D;
4. Mechanism for maintaining a continuous technological advancement; specific arrangements for technological reserves and innovation; and
5. Reliance on core technologies to operate its business.

2. Target Industries

New high-tech industries and strategic emerging industries, including new-generation information technology, high-end equipment, new materials, new energy, energy saving and biomedicine. These industries will foster the manufacturing integration of the Internet, Big Data, cloud computing and artificial intelligence.

Question: What are the highly recommended new technologies?

Answer: Sponsorship Guidelines number 6 highly recommends the following six industrial areas and their corresponding technological services:

1. **New-generation information technology:** such as semiconductors and integrated circuits, electronic information, next-generation information networks, artificial intelligence, big data, cloud computing, emerging software, the Internet, the Internet of Things, and intelligent hardware;
2. **High-end equipment:** such as intelligent manufacturing, aerospace equipment, advanced railway transportation, marine engineering equipment;
3. **New materials:** such as advanced steel materials, advanced non-ferrous metal materials, advanced petrochemical new materials, advanced inorganic non-metallic materials, high-performance composite materials and cutting-edge new materials;
4. **New energy:** such as advanced nuclear power, large-scale wind power, high efficiency photoelectric solar energy, high efficiency energy storage;
5. **Energy saving and environmental protection:** such as energy-efficient products and equipment, advanced environmental protection products, recycling products, new energy vehicles and their key components, power batteries; and
6. **Biomedicine:** such as biological products, high-end chemical drugs, high-end medical equipment and instruments.



3. Target Companies

Domestic companies that satisfy the positioning requirements of the Innovation Board, companies with weighted voting rights ("WVR") structure, pre-revenue companies and red chip companies.

Question: How should issuers choose the suitable listing requirements:

Answer: There are several sets of listing requirements based on market capitalization and financial indicators such as net profit, operating income, R&D investment and operating cash flow. In addition to the general financial requirements (see the listing conditions in sub-section 4 below), specific types of companies have the following listing requirements:

1. Red chip companies

- (a) Red chip companies that satisfy the requirements prescribed in "Several Opinions on Launching the Pilot Program of Innovative Companies Issuing Shares or Depository Receipts in China - issued by CSRC and forwarded by the General Office of the State Council" (《国务院办公厅转发证监会关于开展创新企业境内发行股票或存托凭证试点若干意见的通知》); or
- (b) Red chip companies that (i) have not listed outside China, (ii) maintain a rapid growth in operating income, (iii) possess independent R&D capabilities, internationally leading technologies and comparative advantages, and (iv) satisfy at least one of the following financial indicators: (A) minimum expected market capitalization of CNY 10 billion; or (B) minimum expected market capitalization of CNY 5 billion and at least CNY 500 million operating income for the most recent year.

2. Companies with WVR structure: (i) Minimum expected market capitalization of CNY 10 billion; or (ii) Minimum expected market capitalization of CNY 5 billion and at least CNY 500 million operating income for the most recent year.

3. Pre-revenue companies: (i) Minimum expected market capitalization of CNY 1.5 billion, (ii) at least CNY 200 million operating income for the most recent year; and (iii) the proportion of R&D investment for the recent three years accounted for not less than 15% of the operating income during the same period; or other applicable market capitalization standards.

4. Listing Requirements

Listing requirements in terms of the issuer's qualification, actual controllers, compliance, directors, executives, core technicians, industry competition and connected transaction, the Innovation Board's requirements are similar to those in "*The Management of the Initial Public Offering of Shares*" (《首次公开发行股票并上市管理办法》). Separately, SSE will announce the rules in relation to employees' share option scheme, futures and options incentive schemes and accumulated unrecovered losses before change and other relevant matters.

Listing applicants are required to satisfy at least one of the following five sets of market capitalisation standards (SSE may adjust the following standards according to market conditions and subject to the approval of CSRC):



	Estimated market capitalisation ¹	Net Profit	Operating income
1. Market capitalisation/ Net Profit Test	Not less than CNY 1 billion	Net profit for the recent two years is positive, and the accumulated net profit was not less than CNY 50 million; or The net profit for the most recent year was positive.	Not Applicable The operating income was not less than CNY 100 million.
2. Market capitalisation/ Income Test A	Not less than CNY 1.5 billion	Not Applicable	The operating income for the most recent year was not less than CNY 200 million, and the proportion of R&D investment for the recent three years accounted for not less than 15% of the operating income.
3. Market capitalisation/ Income Test B	Not less than CNY 2 billion	Not Applicable	The operating income for the most recent year was not less than CNY 300 million, and the net cash flow generated from operating activities in the most recent three years was not less than CNY 100 million.
4. Market capitalisation/ Income Test C	Not less than CNY 3 billion	Not Applicable	The operating income for the most recent year was not less than CNY 300 million.
5. Market capitalisation/ Business Test	Not less than CNY 4 billion	Not Applicable	Not Applicable Major businesses or products should have received approvals from relevant national authorities, possessed large market potential and achieved phased results. Pharmaceutical companies must have at least one core product that was approved to commence Phase 2 clinical trials. Other eligible companies must possess substantial technological advantages and satisfy the relevant conditions of the Innovation Board.

5. Review and Registration Mechanism

- **Registration System:** A registration system is adopted and the SSE is responsible for the substantive review. SSE will submit its review approval to the CSRC to complete the registration process.
- **Organizational Structure of the Review Board:** The SSE will establish the Innovation Board Share Listing Committee to review and determine the suitability of the listing applicant. When necessary,

¹ Estimated market capitalisation means the total value of the issuer's shares calculated by multiplying the total number of issued shares and the issued price.



the newly established Science and Technology Consultation Committee will provide opinion.

- **Review Method:** By way of Q&A electronically and categorized review by industries. Based on the positioning of the Innovation Board, SSE will access the applicant's listing and issuance requirements, and information disclosure requirements.
- **Time Limit of the Review:** The SSE shall form a review opinion within 3 months after receiving the application materials. The 3 months period exclude the time for the issuer to modify the registration application materials, the intermediaries to answer SSE's enquiries, conduct on-site verification or suspend listing review. The CSRC will decide whether to approve the registration within 20 working days.
- **Time Limit for Issuance:** An issuer shall issue the shares in any time within 1 year starting from the date of CSRC's registration approval.

6. Market-based Issuance Underwriting Mechanism

- Direct pricing is cancelled (the so-called "23 times price earning ratio" limit is no longer applicable). Instead, a market-based price setting mechanism is adopted. The share issuance price shall be determined by way of interactions with registered offline professional investors².
- Lowering the placing requirements for strategic investors and introducing subscription arrangements for senior management and core employees.
- Allowing listing applicants and lead underwriters to adopt over-allotment options to promote share price stability after listing.

7. Companies with WVR structure

Condition Precedents

1. A WVR structure must be adopted before listing (WVR structure cannot be adopted in any way after listing);
2. The market capitalization and financial indicators of the listing applicant must satisfy at least one of the following standards: (i) minimum expected market capitalization of CNY 10 billion; or (ii) minimum expected market capitalization of CNY 5 billion and at least CNY 500 million operating income for the most recent year.

² Professional investors refer to individual and institutional investors who satisfy the requirements of investing experience, credit records, pricing capabilities and other conditions specified in the "Detailed Rules for the Management of Offline Professional Investors of Shares in Initial Public Offerings" issued by the Securities Association of China in 2018.



Requirements of WVR beneficiaries

1. The beneficiary entity must have a major contribution to the issuer's development or performance growth; before and after listing, the beneficiary entity must be a director or a controlling shareholder of such entity; and
2. WVR beneficiaries must collectively own at least 10% of the issuer's total issued voting shares.

Limitations


1. **Proportional Restrictions:** The number of voting rights for each WVR share shall be identical. The voting rights of each WVR share must not exceed 10 times of the voting rights of each ordinary share.
2. **Issue Restrictions:** After listing, except for a pro rata issue of securities and conversion of capital reserve, the issuer must not issue WVR shares onshore or offshore, and must not increase the proportion of WVR shares. If the proportion of WVR shares increases due to a share repurchase or other corporate actions, the issuer must take appropriate actions to reduce the number of their WVR shares proportionately (such as through conversion of certain WVR shares into ordinary shares) so that the proportion of WVR shares will not be higher than the original level.
3. **Trading Restrictions:** WVR shares must not be traded in the secondary market, but WVR shares can be transferred in accordance with relevant regulations; under specific circumstances, WVR shares can be permanently converted into ordinary shares on a one to one ratio.
4. **Restrictions on important corporate matters:** When an issuer needs to vote on certain important corporate matters, such as changes to the articles of association or changing the number of voting rights, the voting rights of each WVR share shall be identical to the voting rights of each ordinary share.

Protection of non-WVR Shareholders

1. The proportion of voting rights of ordinary shares shall not be less than 10%.
2. Shareholders individually or in aggregate holding more than 10% of the issuer's voting shares can convene an extraordinary general meeting.
3. Shareholders individually or in aggregate holding more than 3% of the issuer's voting shares can propose a resolution at a general meeting.

8. Red Chip Companies

- **Issuer's qualification:**
 - Red chip companies that satisfy the requirements prescribed in "Several Opinions on Launching the Pilot Program of Innovative Companies Issuing Shares or Depositary Receipts in China - issued by CSRC and forwarded by the General Office of the State Council" (《国务院办公厅转发证监会关于开展创新企业境内发行股票或存托凭证试点若干意见的通知》); or

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- Red chip companies that (i) have not listed outside China, (ii) maintain a rapid growth in operating income, (iii) possess independent R&D capabilities, internationally leading technologies and comparative advantages, and (iv) satisfy at least one of the following financial indicators: (A) minimum expected market capitalization of CNY 10 billion; or (B) minimum expected market capitalization of CNY 5 billion and at least CNY 500 million operating income for the most recent year.
 - **Protection of onshore depository receipts holders:** For Red Chip Companies which are listed on the Innovation Board by issuing shares or depository receipts, their shareholding structure, corporate governance, operational regulation and other features should comply with the company law, rules and regulations of their place of incorporation. Red Chip Companies' investor protection standards should not be lower than the requirements of domestic PRC laws and CSRC regulations. Shareholders' protection include dividend distribution, participation in major decisions, residual property distribution and other rights. Issuers must ensure that the actual rights of onshore depository receipts holders are identical to the rights of offshore shareholders.
 - **VIE structure³:** Red Chip Companies that have a VIE structure or similar contractual arrangements should fully disclose the implementation and change of VIE structure, and the implementation of measures to protect the legitimate rights of domestic investors under the VIE structure.

9. Spin-off

A sizeable issuer can spin-off independent subsidiaries that can satisfy the requirements of the Innovation Board according to the laws, rules and regulations of CSRC and SSE.

Part Two: Post-listing compliance requirements

According to the relevant rules of the Innovation Board, SSE has imposed the following post-listing compliance requirements:

1. Selling Restriction Mechanism:

- **Selling restrictions of the controlling shareholders and actual controllers:** Within 36 months after the listing date, the controlling shareholders and the actual controllers shall not (i) transfer or authorize others to manage their directly-owned or indirectly-owned pre-IPO shares, nor (ii) request the issuer to repurchase those pre-IPO shares.
- **Selling restrictions of core technicians:** (i) Within 12 months after the listing date and within 6 months after resignation, a core technician cannot transfer any pre-IPO shares; (ii) within 4 years after the expiry date of the said selling restriction, the total number of pre-IPO shares transferred each year shall not exceed 25% of the pre-IPO shares at the time of listing. The reduction ratio can be used on a cumulative basis.

³ VIE structure means contract-based arrangements or structures commonly used by red chip companies to indirectly own and control onshore business.



- **Holding period of strategic investors' placing shares:** Not less than 12 months after the listing date.
- **Pre-revenue companies at the time of listing:**

	Before realising profits	After realising profits
Controlling shareholders and actual controllers	In the first 3 full financial years after listing, no disposal of pre-IPO shares is allowed. In the 4th and 5th financial years after listing, the annual reduction of pre-IPO shares shall not exceed 2% of the total number of the shares and comply with other SSE share reduction regulations.	On the second day after the current annual report is disclosed, shareholders can dispose their pre-IPO shares and comply with other relevant share reduction regulations.
Directors, supervisors, executives and core technicians	In the first 3 full financial years after listing, no disposal of pre-IPO shares is allowed; those who resign from their positions are bound by the same selling restrictions.	

- **Other selling restrictions:** shareholders can transfer their pre-IPO shares by way of private transfer and placing; SSE will release separate rules on the transfer method, procedure, price, proportion, subsequent transfer and non-public offering of shares.

2. Share Incentive Regime

- **Share incentive limit:** A listed company can implement several share incentive schemes simultaneously. The total number of shares eligible for all share incentive schemes within the effective period is increased to 20%.
- **Scope of targets:** Shareholders who individually or collectively hold more than 5% of the shares of the issuer, actual controllers and their spouses, parents, children and foreign employees, and persons who act as directors, senior management, core technicians or core business personnel of the issuer after listing.
- **Price limit:** Cease to impose price limit on the restricted shares. If the share price is lower than 50% of the market reference price, the independent financial adviser is required to opine on the reasonableness of the pricing assumption and pricing mechanism, and whether the share price is determined at the best interest of the issuer.

3. Special Rules for Secondary Market Transactions

- **Individual investor's eligibility:** An eligible individual investor must have (i) a portfolio of an average daily balance of at least CNY 500,000 in its securities account and cash account within 20 trading days before the account opening; and (ii) at least 24 months' experience in securities transactions. Investors who do not meet the



eligibility requirements can participate in the Innovation Board by purchasing public funds.

- **Share price fluctuation limits:** In the first 5 trading days after listing, there will be no price fluctuation limit. Starting from the sixth trading days and afterwards, the daily upper and lower price fluctuation threshold will be expanded to 20%.
- **Quantity requirement of a single order:** The maximum number of a single market order is 50,000 shares; the maximum number of a single restricted price order is 100,000 shares.

4. Information Disclosure Regime

- On the ground of the general information disclosure requirements, the annual report should focus on disclosing the issuer's industrial characteristics, core technology, R&D expenses, developmental phrases or results of research products or projects, operational risk and other information that can assist investors to make informed decisions.

5. Delisting Regime

The standard and procedure of the delisting regime of the Innovation Board are more stringent.

- **Procedure-wise:** Direct delisting. The Innovation Board cancels the procedures for trading halt and resumption of trading. An unsuitable issuer would be delisted directly.
- **Standard-wise:** The Innovation Board will no longer use continuous loss as a single delisting standard. Mandatory delisting standard includes but not limited to the following circumstances:
 - **Material violation of the law:** An issuer would be delisted mandatorily if it issues shares fraudulently, discloses major information illegally, violates public safety rule or conducts other major illegal acts that seriously damage the order of the securities market;
 - **Market Indicators:** An issuer would be delisted mandatorily if it fails to meet market indicators such as accumulated trading volume, share price, number of public shareholders and market capitalisation;
 - **Financial requirements:** An issuer would be delisted mandatorily if it shows stagnant or extremely low level of its principal business activities; inability to maintain normal operation as a result of significant decrease in operating assets; operating income or profit is mainly coming from connected transactions with no commercial substance or trading business unrelated to the issuer's principal business; or other circumstances that show issuer's inability to maintain operations.

An R&D issuer would be delisted mandatorily if (i) its principal business, core product or reliant technology is failed or is



prohibited from being used, and (ii) the issuer does not have other businesses or products that can meet one of the five sets of market capitalization indicators.

- **Compliance requirements:** An issuer would be delisted mandatorily if it cannot satisfy the following requirements within a specified period: (1) rectify the financial accounting report that have major accounting errors or false records, (2) disclose the annual report or the semi-annual report, (3) rectify major defects in disclosure or regulatory operations, (4) resolve share capital issues that results in the issuer not being able to fulfil the listing requirements for 20 consecutive trading days, (5) resolve the issues arising from the most recent financial report that the auditors issued a reserved comment or a negative comment in the audit report.
- Companies that are subject to mandatory delisting as a results of major illegal violations will not be allowed to submit new listing applications. The delisting would be permanent.

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