Client Alert
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Launch of the Shanghai-London Stock Connect – Joint announcement made by CSRC and FCA

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On 17 June 2019, the China Securities Regulatory Commission (CSRC) and the Financial Conduct Authority of the United Kingdom (FCA) released a joint announcement of their approval in principle of the establishment of the Shanghai-London Stock Connect. On the same day, the London Stock Exchange (LSE) held the launch ceremony for the westbound business of Shanghai-London Stock Connect and the listing of global depositary receipts (GDRs) issued by Huatai Securities Co., Ltd. ("**Huatai**"), a company listed on both Shanghai Stock Exchange (SSE) and Hong Kong Stock Exchange (SEHK). Huatai is the first A+H share company issuing GDRs on the LSE.

1. What is Shanghai-London Stock Connect?

Shanghai-London Stock Connect is a mechanism that connects the LSE and the SSE. Eligible companies listed on the two stock exchanges can issue, list and trade depositary receipts on the counterpart's stock market in accordance with the corresponding laws and regulations.

The Shanghai-London Stock Connect is a two-way mechanism with westbound and eastbound business.

A. Westbound business

Under the westbound business, eligible companies listed on the SSE ("**SSE Listed Companies**") can issue GDRs and apply for their listing on the Main Market of the LSE.

B. Eastbound business

Under the eastbound business, eligible companies listed on the LSE ("**LSE Listed Companies**") can issue Chinese Depositary Receipts (CDRs) in China and apply for their listing on the Main Board of SSE. (For the purposes of this article, "China" does not include Hong Kong Special Administrative Region, Macau Special Administrative Region or Taiwan.)

2. Significance of Shanghai-London Stock Connect to Issuers and Investors

- **Issuers can improve their reputation in the counterpart's stock market.**

  In addition, SSE Listed Companies can (a) issue GDRs representing both existing and newly issued shares under the westbound business to raise capital, and (b) keep the capital raised in foreign countries and use it directly for foreign investment.

In the early stage of eastbound business, LSE Listed Companies can only use their existing issued shares (but not newly issued shares) as underlying shares to issue CDRs. Therefore, LSE Listed Companies cannot use the Shanghai-London Stock Connect as a tool to raise fresh capital in China's domestic market.

- **From the perspectives of local investors, Shanghai-London Stock Connect is a tool to invest in the counterpart's listed companies.**

3. Differences between Shanghai-London Stock Connect and Shanghai-Hong Kong Stock Connect

Both Shanghai-London Stock Connect and Shanghai-Hong Kong Stock Connect are stock connect mechanisms, but they differ significantly in several ways.

	A. Market mechanism
Shanghai-Hong Kong Stock Connect	Shanghai-Hong Kong Stock Connect is a secondary market trading scheme. Investors in one market can purchase shares of listed companies in the counterpart's market through the stock connect.
Shanghai-London Stock Connect	Shanghai-London Stock Connect is a scheme that covers both primary market and secondary market. Investors can trade the depositary receipts in the secondary market. For westbound business, SSE Listed Companies can use newly issued shares for the issue of GDRs to achieve primary market security issuance.

	B. Trading targets
Shanghai-Hong Kong Stock Connect	The trading targets under the Shanghai-Hong Kong Stock Connect are shares listed on the counterpart's market. Chinese domestic investors appoint the SSE's exchange services company in Hong Kong to purchase the shares of the companies listed on SEHK ("**SEHK Listed Companies**"). The trading targets are the shares of SEHK Listed Companies registered under the name of the SSE's exchange services company on behalf of the Chinese domestic investors. Similarly, Hong Kong investors appoint SEHK's exchange services company in Shanghai to purchase the shares of SSE Listed Companies. The trading targets are the shares of SSE Listed Companies registered under the name of SEHK's exchange services company on behalf of Hong Kong investors.
Shanghai-London Stock Connect	The trading targets under the Shanghai-London Stock Connect are depositary receipts listed on the local stock exchange. The underlying shares of the CDRs are listed on the LSE, but the issue of CDRs occurs in China. Depositaries stationed in China issue CDRs to Chinese investors, who can trade the CDRs with other investors in China. The issuance and trading of CDRs occur in China.

	The underlying shares of GDRs are listed on the SSE, but GDRs are securities issued outside China. Foreign depositaries issue GDRs to foreign investors, who can exchange GDRs with other foreign investors. The issuance and trading of GDRs occur outside China.

	C. Scope of investment
Shanghai-Hong Kong Stock Connect	The regulatory bodies of the Shanghai-Hong Kong Stock Connect decide the scope of shares eligible for investment. Eligible shares can be traded automatically under the Shanghai-Hong Kong Stock Connect. Eligible SSE securities include all the constituent stocks of the SSE 180 Index, SSE 380 Index and all the SSE-listed A shares that have corresponding H shares listed on SEHK. Hong Kong and overseas investors can trade the shares of SSE Listed Companies via the Shanghai-Hong Kong Stock Connect without those companies applying to be included in the scope of the Shanghai-Hong Kong Stock Connect. The same mechanism applies for SEHK Listed Companies.
Shanghai-London Stock Connect	The regulatory bodies of the Shanghai-London Stock Connect decide the scope of the underlying shares of companies listed in the counterpart's stock exchange for the purpose of issuing the corresponding depositary receipts, but those eligible shares do not automatically fall into the trading system of the Shanghai-London Stock Connect. The issuance and listing of depositary receipts are subject to the voluntary applications of the eligible companies and the approval of the regulatory bodies in London and Shanghai. Currently, the GDRs issued by Huatai are the only depositary receipts available for trading under the Shanghai-London Stock Connect. International investors remain unable to invest in other SSE Listed Companies and Chinese domestic investors are also unable to invest in LSE Listed Companies under the Shanghai-London Stock Connect.

4. Approval process for Shanghai-London Stock Connect in China

A. Westbound business

For westbound business, SSE Listed Companies that use their existing or newly issued shares as underlying shares to issue and list GDRs overseas must (a) comply with the Chinese Securities Law ("**Securities Law**"), the Special Provisions of the State Council on the Overseas Offering and Listing of Shares of Joint Stock Companies ("**Special Provisions**"), other laws and regulations and other relevant CSRC provisions on the overseas offering or listing of securities by domestic Chinese companies; and (b) obtain the approval from the CSRC.

B. Eastbound business

For eastbound business, LSE Listed Companies that use their existing issued shares as underlying shares to issue CDRs should (a) comply with the Securities Law, Several Opinions on Conducting the Pilot Program of Innovative Enterprises' Offering of Shares or Depositary Receipts within China (the "**CSRC's Several Opinions**") and CSRC's regulations; and (b) submit the application to CSRC. The SSE examines whether the LSE Listed Companies can meet the conditions for the listing of CDRs and other matters in accordance with the SSE business rules. The CSRC accepts the application documents filed by the LSE Listed Companies through the SSE and approves the application of the LSE Listed Companies. The Public Offering Review Committee will not review further.

5. Regulatory requirements of Shanghai-London Stock Connect in China

A. Conditions for westbound business in China

As mentioned in Part 4(A), SSE Listed Companies offering GDRs overseas must comply with the Securities Law, the Special Provisions, other laws and regulations, and other relevant provisions of the CSRC on the overseas offering or listing of securities by domestic Chinese companies.

In addition, a SSE Listed Company shall not use its newly issued shares to issue GDRs under any one of the following situations:

1. The application documents contain false records, misleading statements or material omissions.

2. The rights and interests of the SSE Listed Company are seriously damaged by the controlling shareholders or actual controllers and the damage has not been resolved.

3. The SSE Listed Company or its subsidiary companies provide a guarantee to outsiders in violation of any regulation and the guarantee has not been cancelled.

4. A current director or senior executive has been given an administrative penalty by CSRC in the last 36 months or has been publicly condemned by the SSE in the last 12 months.

5. The SSE Listed Company or any of its directors or senior executives is being investigated by (a) the judicial bodies due to any suspected crime, or (b) the CSRC for any suspected breach of laws or regulations.

6. A certified public accountant has issued an audit report with qualified opinions, adverse opinions, or disclaimer of opinions ("**Qualified Opinions**") on the financial reports for the most recent year and period, except in circumstances where the significant impact of the matters involved in the Qualified Opinions have been resolved or such Qualified Opinions have been made in relation to significant corporate restructuring.

7. Other circumstances which seriously damage the lawful rights and interests of investors or the public.

B. Conditions for eastbound business in China

The business rules of Shanghai-London Stock Connect are established in accordance with CSRC's Several Opinions, but such requirements are not applicable to LSE Listed Companies that use their existing issued shares to issue CDRs in China.

LSE Listed Companies, as overseas securities issuers, have to fulfil the following conditions when they use their underlying shares to issue CDRs in China:

1. The basic conditions set out in items 1 to 3 of Article 13 of the Securities Law, i.e. the company: (1) is a sound operating organization; (2) has profit-making capabilities and good financial conditions; (3) does not have false records in the financial statements in the last three years and no significant violation of law.

2. The company has been established legally and operated continuously for three years or more, and the company's major assets do not have any significant ownership dispute.

3. There has been no change in the actual controller of the company in the last three years; and there is no major ownership dispute over the underlying shares of the company held by the controlling shareholders and shareholders controlled by the controlling shareholders or the actual controller.

4. The company, its controlling shareholder or actual controller have not breached any law that damages the lawful rights and interests of investors or public interest in the past three years.

5. The company has sound fundamental accounting rules and internal control rules.

6. The directors, supervisors and senior executives have good reputation, satisfy the requirements prescribed by the laws of the place of the incorporation of the company and do not have recent record of major violation of law or dishonesty.

7. Any other conditions prescribed by the CSRC.

In addition, LSE Listed Companies have to satisfy the following conditions when they first apply to list CDRs on the SSE:

1. CDR public issuance conditions under the Administrative Measures for the Issuance and Trading of Depositary Receipts (for Trial Implementation) and the Regulatory Provisions of the CSRC on the Interconnection Depositary Receipt Business of the SSE and LSE (for Trial Implementation) and the approval of CSRC to issue CDRs.

2. The average market value of the underlying shares of the overseas issuer calculated based on the average closing price in the 120 trading days prior to the issuance date shall not be less than RMB 20 billion. The value is calculated in accordance with the middle price of the RMB

exchange rate announced by the People's Bank of China one day before the date of issuance.

3. The company has been listed on the LSE for three years and for at least one year on the premium listing segment of the Main Market of the LSE.

4. The number of CDRs to be listed is not less than 50 million and the market value of the underlying shares is not less than RMB 500 million. The value is calculated based on the latest closing price of the underlying shares and the middle price of the RMB exchange rate announced by the People's Bank of China one day before the listing application date.

5. Any other conditions prescribed by the SSE.

The SSE reserves the right to adjust the CDRs listing conditions in response to market conditions.

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