LLINKS Law Offices
通力律师事务所

Shanghai
19F, ONE LUJIAZUI
68 Yin Cheng Road Middle
Shanghai 200120 P.R.China
Tel: (86 21) 3135 8666
Fax:(86 21) 3135 8600

Beijing
Units 902-903
Winland International Finance Centre
No.7 Finance Street, Xicheng District
Beijing 100033 P.R.China
Tel: (86 10) 6655 5050
Fax:(86 10) 6655 5060

上海
上海市银城中路68号
时代金融中心19楼
邮政编码: 200120
电话: (86 21) 3135 8666
传真: (86 21) 3135 8600
www.llinkslaw.com

北京
北京市西城区金融大街7号
英蓝国际金融中心9楼02-03单元
邮政编码: 100033
电话: (86 10) 6655 5050
传真: (86 10) 6655 5060
master@llinkslaw.com

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ChiNext Lifts Its Regulatory Game

By Wayne Chen and Monica Gao

More than 300 listed companies have been trading on ChiNext to date since its successful launch on 23 October 2009. To gradually improve the regulatory regime for companies listed on ChiNext, the securities regulators and the Shenzhen Stock Exchange have, based on the existing laws and regulations, made amendments on a timely basis and introduced an array of documents and policies to address the following issues.

- **Regulating the Use of Over-raised Funds**

  Memorandum No. 1 on Information Disclosure Operations on ChiNext – Use of Over-raised Funds was revised in April 2010 to specifically govern the scope of applicability of over-raised funds of companies listed on ChiNext, the purposes of use of such funds, procedures for the use of such funds and deposit of such funds. This memorandum has elaborated on the requirements for the disclosure of information on the use of over-raised funds at different stages.

  The imposition of strict restrictions on the use of over-raised funds by companies listed on ChiNext will help effectively minimise the risks created during the use of such funds.

- **Management Shares**

  The Shenzhen Stock Exchange issued the *Notice for Further Regulating the Trading in the Shares of Companies Listed on ChiNext by the Directors, Supervisors and Senior Management Members of Such Companies* in November 2010 to extend the lock-up period of management shares, requiring directors, supervisors and other senior management members to hold their shares for a longer period if they leave office within a year upon completion of the listing of their companies, and to encourage making additional extension to the lock-up period and setting a minimum price for the sale of such management shares.

如果您需要本出版物的中文本，请与下列人员联系：

郭建良: (86 21) 3135 8756
Publication@llinkslaw.com

If you would like other Llinks publications, please contact:

Roy Guo: (86 21) 3135 8756
Publication@llinkslaw.com

Llinks Law Offices
www.llinkslaw.com

Sponsors are required to pay close attention to any change in position of management personnel, to supervise and guide their fulfillment of commitments and verify whether the trading and circulation of the shares with selling restrictions are in compliance with regulations.

These measures set out to strengthen the supervision of the trading of the companies' shares by their directors, supervisors and senior management members, maintain the stability of management teams and contribute to the development of companies in the long run.

- **Improved Sanction Mechanism**

The Shenzhen Stock Exchange published the *Criteria for Issuing Public Censures against Companies Listed on ChiNext* in April 2011, setting clear criteria for making public the reprimanding of companies listed on ChiNext, in particular the criteria for publicly reprimanding listed companies for their irregularities regarding the disclosure of information on material events, disclosure in periodic reports, occupation of funds, provision of guarantees and management of raised funds.

These requirements aim to enhance the regulatory deterrent capability in order to further improve the mechanisms for imposing penalties for breaches by listed companies and carrying out enforcement of self-regulation.

- **Information Disclosure**

The Shenzhen Stock Exchange implemented the *Guidelines on a Through-Train Pilot Scheme for Information Disclosure by Listed Companies* in October 2011, to strengthen a market-based constraint mechanism for information disclosure by listed companies. The *Shenzhen Stock Exchange Measures for Evaluating Information Disclosure by Listed Companies* revised in November 2011 requires the quantitative evaluation of information disclosure by listed companies.

Notice No. 41 published by the China Securities Regulatory Commission (CSRC) in December 2011, and *Memorandum No. 10 on Information Disclosure Operations on ChiNext – Disclosure of Annual Reports* published by the Shenzhen Stock Exchange in January 2012, have laid down more detailed requirements for various sections disclosed in the annual reports of companies listed on ChiNext, such as management discussion and analysis and distribution of profits. For instance, listed companies are required to specify various policies in their articles of association, such as the method of profit distribution and the specific conditions for declaring cash dividends and their proportion.
The *Rules Governing the Listing of Shares on the Shenzhen Stock Exchange's ChiNext* as amended recently have increased the information disclosure obligations of listed companies, requiring them to disclose all relevant matters during the processing of fund-raising projects. Also, listed companies with negative net assets are required to issue forecasts of their operation achievements.

- **Improved Delisting Mechanism**

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The amended *Rules Governing the Listing of Shares on the Shenzhen Stock Exchange's ChiNext* formally introduced a delisting regime for ChiNext under which:

- the particulars relating to the suspension and termination of a listing are revised;

- the criteria and the basis for determining resumption of a listing, as well as the application for resumption of a listing, are specified;

- the policy regarding "handling delisting risk warnings" is abolished, and specific requirements are set for disclosure of risks associated with the suspension and termination of a listing under different situations;

- the policy regarding "delisting consolidation period" is introduced and a delisting consolidation board is set up;

- the whereabouts of companies listed on ChiNext following their delisting are made clear.

The implementation of ChiNext's delisting regime further improved the regulatory mechanism for its listed companies, which in term are set to boost enhancements both in their portfolios as well as long-term development.

In addition to the above documents and policies, the Shenzhen Stock Exchange also issued various regulatory policies such as the *Notice for a Trial System for Maintaining Ongoing Supervisory Specialists in Certain Sponsors* and the *Shenzhen Stock Exchange Measures for Filing for the Record by Independent Directors*.

In summary, during the growth of ChiNext in the past two years or so, the Chinese securities regulators and the Shenzhen Stock Exchange have been establishing an increasingly sound regulatory regime governing companies listed on ChiNext in various aspects ranging from the use of raised funds, information disclosure and management's shareholding to the setup of a delisting mechanism, offering a solid foundation for the sustainable and stable development of ChiNext.

Contact Details

If you would like to know more information about the subjects covered in this publication, please feel free to contact the following people or your usual Llinks contact.

Shanghai	Beijing
Christophe Han Tel: (86 21) 3135 8778 Christophe.Han@llinkslaw.com	**James Weng** Tel: (86 21) (86 10) 6655 5050 - 1028 James.Weng@llinkslaw.com
Grant Chen Tel: (86 21) 3135 8669 Grant.Chen@llinkslaw.com	**Wen Li** Tel: (86 21) (86 10) 6655 5050 - 1027 Wen.Li@llinkslaw.com
Wayne Chen Tel: (86 21) 3135 8766 Way.Chen@llinkslaw.com	
Calista Huang Tel: (86 21) 3135 8788 Calista.Huang@llinkslaw.com	
Leo Wang Tel: (86 21) 3135 8716 Leo.Wang@llinkslaw.com	

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