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Newsletter

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Legal Updates

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1. Guidelines on Data Export Security Assessments (Authors: David TANG, Min ZHU)

On May 27, 2017, the National Standardization Technical Committee for Information Security (“**Technical Committee**”) promulgated a draft for comment of the *Information Security Technology – Guidelines for Data Cross-Border Transfer Security Assessment (Draft)* (the “**Guidelines**”), in order to supplement the personal information and important data export assessment requirements stipulated under Cybersecurity Law, which came into force on June 1, 2017.

The Technical Committee, which is subordinate to the National Standardization Management Committee, is in charge of state information security standardization work under the guidance of the Office of the Central Leading Group for Cyberspace Affairs. Although the assessment standards referred in the Guidelines are not mandatory and are intended only for reference purposes, we believe these standards may reflect the attitude of regulators to some extent and therefore may provide practical guidance related to data export security assessments, particularly since the Cybersecurity Law and the forthcoming *Measures on Security Assessments for Personal Information and Important Data to be Transmitted Abroad (Draft)* (the “**Measures**”) leave open questions as to personal information and important data export security assessments.

Relationship between the Guidelines and the Measures

The Measures are currently closed to further public comment. If practical, we expect that the Measures will be promulgated as soon as possible after only one round of comments (similar to the *Measures on Network Product and Service Security Reviews (Trial)*), in order to support the implementation of the Cybersecurity Law. However, as mentioned in a previous article, the Measures only contain general principles and standards. Detailed rules must still be developed to assist with its implementation. Thus, the Guidelines have been formulated to be consistent with the logical framework of the Measures, and contain more detailed requirements relating to data export security assessments.

For example, the Measures provide that personal information and important data export security assessments will involve either self-assessment by network operators or to assessments organized by industry regulators or supervisory departments depending upon specific circumstances. The Guidelines further provide in Part 4, “Assessment Procedures,” the process and requirements for the security assessments to be conducted by network operators and clearly state that such processes and requirements may also apply to industry regulators or supervisory departments in performing their regulatory duties.

In addition, Part 5 of the Guidelines, “Assessment Points,” provides that two factors are to be

considered for data export security assessments, which are the “legitimate and reasonable” and “controllable risk” related to the assessed data exports. Part 5 further explains the key assessment content as provided under Article 8 of the Measures. The Measures also provide that the specific scope of “important data” is to be determined by referring to the relevant national standards and important data identification guidelines. The Guidelines, as the recommended national standards developed by the Technical Committee, will certainly be consulted to determine the scope of important data, particularly the attached Appendix A, *Guidelines on the Identification of Important Data*.

Points of Interest

With respect to the Guidelines in the current form, we believe the following details are worthy of special attention:

a. Scope of application

The Guidelines apply to network operators for conducting personal information and important data export security assessments. As with the Measures, the Guidelines do not limit the subjects responsible for data exports security assessments to critical information infrastructure (“CII”) operators. However, according to the remarks provided by a person in charge of Network Security Coordination Office of the Cyberspace Administration of China at a press conference immediately before the promulgation of the Cybersecurity Law, personal information and important data localization and export requirements are only to apply to CII operators rather than to all network operators. Thus, uncertainty continues to exist with respect to the application scope for the personal information and important data export security assessments. We look forward to clarification of the application scope in the formal issuance of the Measures.

b. Personal information

In addition to personal information that is defined under the Cybersecurity Law and the Measures, the Guidelines stipulate that an individual’s location and behavioral information is also to be regarded as “personal information.” This definition is consistent with the definition of personal information as stipulated under the *Provisions on the Protection of Personal Information of Telecommunications and Internet Users*, which was promulgated prior to the Cybersecurity Law. This issue will require special attention from operators of smartphone apps which collect real-time user location information, especially apps that will provide services to users based upon collected real-time location information. App operators should observe that all location and behavioral information that they collect may be regarded as personal information under the Guidelines. Besides this, as the definition of personal information under the Cybersecurity Law is not exhaustive and the government tends to issue industry regulations that are more stringent, we further believe that personal information should be interpreted broadly and should include individuals’ location and behavioral information.

c. Data exports and provision

The Guidelines clearly provide that “data exports” refers to the provision of personal information and important data that are in electronic form collected within the territory of People's Republic of China to foreign institutions or organizations. The provision of foreign data by Chinese institutions without any modification or processing is not regarded as data exports. In addition to network operators voluntarily providing or otherwise releasing domestic data to foreign institutions, users of products or services who provide data to overseas organizations, institutions or individuals through the products or services provided by the network operators are also to be regarded as data exports.

The Guidelines thus provide assurance to some network operators that not all form (including non-electronic forms) of personal information and important data that are provided to foreign institutions or individuals will be regarded as data exports. However, as the network operators providing personal information and important data to foreign entities through their users using their products and services are also identified as data exports, network operators may be subject to regulatory requirements if they intend to employ technical means or special transaction architecture to allow users to export data via their products or services.

d. Assessment procedures

In accordance with the Guidelines, the assessment procedures include commencing self-assessments, preparing assessment plans, evaluating assessment plans (legitimate and reasonable, and risk control) and developing assessment reports. Assessment reports are to be preserved for at least for five years and will undoubtedly become a necessary document for network operators' personal information and important data export security assessments. In light of the key assessment points as described below, preparing the assessment reports will require network operators to conduct comprehensive due diligence investigations on their network security and data protection status that are related to their business operations, including investigations into relevant technologies, laws and policies.

e. Key assessment points

As mentioned above, the factors necessary to be considered for data export security assessments mainly include the “legitimate and reasonable” and “risk control” for data exports. We understand that the “legitimate and reasonable” standard is relatively easy to prove. Network operators may prove this standard by demonstrating the data export is necessary for their business operations.

However, the “risk control” standard is relatively difficult to prove. The Guidelines provide that this standard is to be proven from the perspective of data attributes (personal information and important data), commercial subjects' capacity (sender and receiver) and the stability of the macroeconomic environment (political and legal environment of the receiving party). Network operators may be subject to a heavy burden to prove this standard in this regard as a regulatory examination would be more comprehensive.

In addition, the Guidelines promote the “minimization principle” with respect to the assessment of

personal information and important data to be exported. The minimization principle requires that the exported information and data must be directly related to the provider's relevant business, which means that the provider's relevant business processes cannot be fulfilled without exporting the information. The transmission frequency (automatic transmission) and quantity of information transmitted should be kept at the lowest frequency and the quantity necessary to fulfill the provider's relevant business processes.

f. Appendix A: Important Data

Appendix A provides that the important data mentioned in the Guidelines refers to data (including original data and derived data) collected or developed by the Chinese government, enterprises and individuals within the territory of China, which do not involve state secrets but are closely related to national security, economic development and the public interest, and which if disclosed, lost, misused, tampered with or destroyed, or combined, integrated or analyzed without authorization, would cause severe adverse influences on national security, state economic and financial security, social and public interests or individual legal rights and interests.

In addition, Appendix A provides the scope of important data for 27 sectors (industries) for reference purposes, which essentially covers all major industry sectors and greatly exceeds the number of CII industries provided in the Cybersecurity Law. Appendix A concludes with a fallback provision that describes the standards for identifying important data in other industries which are not specifically provided for. Therefore, we tend to believe that the application scope of domestic data storage and export assessment should be interpreted broadly, provided that it does not prevent the orderly and free cross-border flow of data.

g. Appendix B: Assessment Measures

Appendix B of the Guidelines describes the assessment Measures in detail. First, the relevant network operators should assess the level of impact caused by personal information exports on individual rights and interests and the level of impact caused by important data on national security and social public interest, and should estimate the possibility of the occurrence of security event based upon sender and receiver's security capabilities and the local political environment of the location where the receiver is located. Secondly, network operators should make a comprehensive evaluation of the security risk related to the data export by considering the impact that the data exports may have on individual rights and interests, national security, and on the social public interest and the evaluation of the local political environment that the receiver is subject to and categorize the risk level as "extremely high," "high," "moderate" or "low." Data exports assessed as "extremely high" or "high" risk are to be prohibited.

Conclusion

The Guidelines provide detailed and practical requirements related to data export security assessments, which should be applied by different network operators on a case-by-case basis

according to individual circumstances. Although the Measures and the Guidelines have not yet been formally introduced, the data localization and export assessment provided by the Cybersecurity Law will undoubtedly become a necessity. Therefore, we recommend that enterprises who may be subject to these requirements, whether or not they are CII operators, should make a preliminary assessment of their own circumstances in light of the Guidelines and prepare themselves in advance to respond to data export assessment requirements that may apply going forward.

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2. Hong Kong New Board – To Embrace the New Economy (Authors: Han Kun Hong Kong Associate Law Firm Yurong YE, Felix MIAO, Fredric HUANG)

Recently, the Stock Exchange of Hong Kong Limited (“SEHK”) has published the New Board Concept Paper for the purpose of seeking market feedback on SEHK’s proposed establishment of a New Board. This newsletter is a brief introduction to the New Board Concept Paper.

Background: Ensuring Continued Success of Hong Kong’s IPO Market

Under the current listing framework, the Hong Kong security market has high industry concentrations and is underweight in high growth sectors, meaning that the competitiveness of HKEX as an IPO venue is facing challenge.

Companies from New Economy industries (such as Biotechnology, Health Care Technology, Internet & Direct Marketing Retail, Internet Software & Services, IT Services, Software, Technology Hardware, Storage & Peripherals) that have listed on Hong Kong market in the past ten years make up only 3% of Hong Kong’s total market capitalisation, as compared with 60%, 47% and 14% for NASDAQ, NYSE and LSE, respectively. Moreover, Hong Kong security market has minimal weightings in some of the fastest growing industries globally: Pharmaceuticals, Biotechnology & Life Sciences (1%), Healthcare Equipment & Services (1%) and Software & Services (9%, or 1% if Tencent is excluded).

Meantime, the Mainland listing venues and regulator have pursued a series of measures to improve the attractiveness of Mainland venues for emerging and innovative companies to raise equity capital in recent years. Among these were the launch of ChiNext and NEEQ in 2009 and 2012. The Mainland listing venues and regulator have also released an announcement regarding a path to step-up from NEEQ to a listing on ChiNext and plan for registration-based reform to improve the listing process.

One major attraction of the US market for many such companies is that Weighted Voting Rights (“WVR”) structures are permitted there, whereas the Hong Kong market does not allow them. Moreover, 18 out of 33 (55%) US-listed Mainland Chinese companies with WVR structures,

accounting for 84% of market capitalisation, are from precisely the information technology industry that the Hong Kong market is underweight in.

To complement and supplement the existing listing framework, open up to a more diverse range of issuers, broaden the capital market access in Hong Kong and ensure that only pre-profit companies with high growth potential or New Economy companies can apply to list in Hong Kong, SEHK proposes to establish a New Board, separate from the Main Board and the GEM.

New Board PRO or New Board PREMIUM?

		New Board PRO	New Board PREMIUM
Target Issuers		Earlier stage companies that do not meet the financial or track record criteria for GEM or the Main Board	Companies that meet the existing financial and track record requirements of the Main Board, but which are currently ineligible to list in Hong Kong because they have non-standard governance structures
Target Investors		Open to professional investors only	Open to both retail and professional investors
WVR structures (same share with different rights)		<p>WVR structures are allowed.</p> <p>The SEHK proposes the following two approaches to regulate the companies with a listing on the New Board with a WVR structure.</p> <p>(a) Approach one: disclosure-based approach. Companies are required to disclose, in a prominent way, the WVR structures that they adopted and the risks associated with such structure.</p> <p>(b) Approach two: in addition to disclosure requirements, mandatory safeguards are imposed on the companies with WVR structures, subject to whether such a company will be listed on New Board Pro or New Board Premium.</p>	
Listing Requirements	Business/Financial Criteria	No track record or minimum financial criteria requirement, subject to a minimum market capitalisation at the time of listing of HK\$200 million.	Quantitative entry requirements equivalent to those of the Main Board, namely, an applicant must have a trading record of not less than three financial years and meet one of the three financial criteria (Profit Test, Market Cap/Revenue Test and Market Cap/Revenue/Cashflow Test).
	The Place of Applicants	The place of incorporation and place of central management and control of the applicants to the New Board are required to be in jurisdictions with regulatory cooperation measures in place with the SFC (including Hong Kong, the People's Republic of China, the Cayman Islands and Bermuda).	

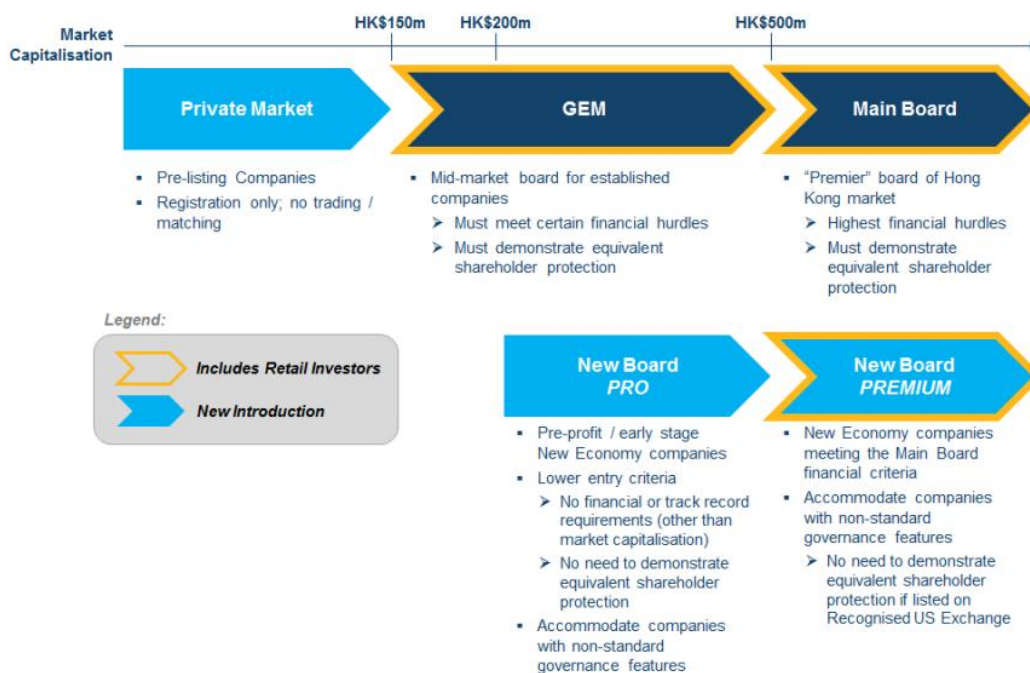
Open Market Requirements	A listing applicant shall have a minimum of 100 investors at the time of listing and a minimum public float at listing of 25%. Such requirements are the same as those that currently apply for GEM issuers at the point of listing.	To follow the Main Board open market requirements in force from time to time. Such requirements include (i) the equity securities must be held by at least 300 holders with a public float requirement of 25% of the total number of issued shares; and (ii) the securities for which listing is sought held by the public must also have an expected market capitalisation at the time of listing of not less than HK\$500 million.
Secondary Listing of Chinese Companies	Companies with a “center of gravity” in Greater China are allowed to pursue a secondary listing in Hong Kong.	
Shareholder Protection Standards	Applicants for New Board PRO will not be required to provide shareholder protection standards equivalent to those in Hong Kong.	Applicants for New Board PREMIUM will be required to provide shareholder protection standards equivalent to those in Hong Kong. In addition to the exemptions that may be granted by the Stock Exchange, with companies with unconventional governance features, including companies with WVR structures could list on either New Board PREMIUM or New Board PRO which are already listed on a recognised US Exchange (NYSE and NASDAQ) and demonstrated, to SEHK’s satisfaction, a good compliance record during that time.
Suitability Assessment	A “lighter touch” suitability assessment for new applicants to New Board PRO - not applying the existing suitability criteria set out in the relevant guidance letters. Factors set out under guidance letters for considering an applicant’s suitability include reliance upon a parent group/connected	A more stringent approach.

		person/major customer and the sustainability of the applicant's business model.	
Listing Documents		The prospectus requirements would not apply to New Board PRO. Given the professionals-only nature of New Board PRO, it is proposed that an applicant would only be expected to ensure that it produces a listing document that provided accurate information sufficient to enable professional investors to make an informed investment decision.	Since New Board PREMIUM includes retail investors and issuers would be expected to conduct a public offering, a listing applicant would have to adhere to the Prospectus requirements of Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32. of the Laws of Hong Kong) and also existing Main Board requirements for a Prospectus.
Sponsor		The existing sponsor regime would not apply. An applicant only needs to appoint a financial adviser (a licensed corporation licensed for Type 6 regulated activity (advising on corporate finance)).	The existing sponsor regime would apply.
Role of the Listing Committee		Listing applications would be vetted and approved by the Listing Department under delegated authority from the Listing Committee, which is in line with the current GEM listing applications approval arrangement.	Listing applications would be presented to the Listing Committee for approval following vetting by the Listing Department, which is in line with the current Main Board listing application approval arrangement.
		The Listing Committee would make decisions on the cancellation of listings, disciplinary matters and be responsible for hearing appeals for both New Board segments.	
Continuous Listing and Corporate Governance Obligations		Companies listed on the New Board would be expected to comply with the standards applicable to Main Board-listed companies in respect of: <ul style="list-style-type: none"> - timely disclosure of material information; - publication of financial statements under prescribed accounting standards; - notifiable and connected party transaction rules; 	

	<ul style="list-style-type: none"> - directors' suitability and independent non-executive directors' representation; - requirement to appoint a company secretary; - general meetings; - super-majority voting on certain fundamental matters; and - pre-emption rights for existing shareholders. 	
Fast-track Migration Mechanism	<p>There would be no fast-track migration mechanism between the New Board and the Main Board or GEM, or from New Board PRO to New Board PREMIUM. For a listed company on New Board PRO wishing to list on these platforms to attract retail investors, it would have to meet all the admission criteria and other listing requirements of the relevant board (e.g. issuing a prospectus). A requirement to raise additional capital via a public offer may also be imposed.</p>	
Suspension	<p>SEHK would suspend a New Board-listed company's securities for a material breach of the New Board Listing Rules.</p>	
Delisting	<p>The listing of a company listed on the New Board PRO would be immediately cancelled if it had been suspended for a continuous period of 90 calendar days.</p>	<p>SEHK can cancel the listing of a company listed on the New Board PREMIUM if it had been suspended for a continuous period of 6 months.</p>
	<p>SEHK would retain the right to cancel the listing of a New Board-listed company before the expiration of the above prescribed periods and the right to cancel a listing without an intervening suspension period if SEHK considers the listed company or its business is no longer suitable for listing.</p>	

Vision for Hong Kong's Future Listing Framework

- The Main Board would be positioned as a “premier board” with an increased minimum market capitalisation requirement of HK\$500 million (raised from HK\$200 million), along with existing financial and track record criteria.
- GEM would serve the needs of small and mid-sized issuers that meet its financial and track record criteria and desire to attract retail as well as professional investors.
- The New Board would fill the gaps in Hong Kong's current listing framework, so that the needs of New Economy and early-stage companies could be accommodated while maintaining appropriate regulatory and shareholder protection standards.



Proposed Corresponding Reform of and Changes to the GEM and Main Board

- The SEHK proposes removing the “stepping stone” concept (GEM as a stepping stone to the Main Board) and the streamlined process for transfers from GEM to the Main Board. This means that GEM Transfer applicants will be required to appoint a sponsor and issue a “prospectus-standard” listing document.
- All GEM Transfer applicants shall have published and distributed at least two full financial years of financial statements after their GEM listings before they can be considered for a GEM Transfer.
- The initial listing requirements in GEM Board will be raised (including increasing minimum market capitalisation requirement from HK\$100 million to HK\$150 million, increasing minimum cash flow requirement from HK\$20 million to HK\$30 million and extending the lock-up on

controlling shareholders upon listing from one year to two years).

- d. The initial listing requirements in Main Board will be raised (including increasing minimum market capitalisation requirement from HK\$200 million to HK\$500 million, increasing the minimum public float value from HK\$50 million to HK\$125 million and extending the lock-up on controlling shareholders upon listing from one year to two years).

For further details, please see the Consultation Paper on Review of the Growth Enterprise Market (GEM) and Changes to the GEM and Main Board Listing Rules which is available at the following link:

<http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2017062.pdf>.

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Important Announcement

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