

HKEx LISTING DECISION

Cite as HKEx-LD55-1 (June 2006) (Withdrawn in October 2012; Superseded by GL43-12)

Summary	
Name of Parties	Company A - a Main Board listing applicant and its subsidiaries (the ‘Group’) Pre-IPO Investor - a proposed investor in the shares of Company A prior to the IPO
Subject	Whether a placing of Company A’s shares to the Pre-IPO Investor prior to listing that met the technical requirements regarding disclosure, lock-up and public-float as memorialised in Listing Decision HKEx-LD36-1 complied with Listing Rule 2.03, where: (a) the investment would be completed after approval in principle by the Listing Committee and shortly before listing; (b) the Pre-IPO Investor would receive a guaranteed discount to the IPO offer price of the shares upon listing; and (c) the Pre-IPO Investor would receive a put option allowing the purchased shares to be resold to Company A or its controlling shareholders after listing at approximately the same price as was paid for the shares plus agreed interest ?
Listing Rules	Listing Rules 2.03(2) and (4); and Listing Decision HKEx-LD36-1 (October 2003)
Decision	The Exchange determined that the terms of the pre-IPO placing were contrary to the principles of Listing Rule 2.03 and decided not to grant listing approval to Company A until further information about the intended purpose of the special arrangements and the role of the investor was submitted for consideration. The proposal was subsequently withdrawn and the listing was permitted to proceed.

SUMMARY OF FACTS

1. Shortly before listing, Company A and its controlling shareholder (the ‘Controlling Shareholder’) entered into a subscription agreement (the ‘Subscription Agreement’) with the Pre-IPO Investor for the subscription of new shares to be issued by Company A (the ‘Subscription Shares’). The Pre-IPO Investor was not in the same industry as Company A.
2. Details of the Subscription Agreement were set out in the draft prospectus. The subscription price for the Subscription Shares was fixed approximately equivalent to the lowest point of the intended offer price range. The placing of the Subscription Shares would raise proceeds for working capital and business development. Immediately after the issuance of the subscription shares and the IPO share offer, the Pre-IPO investor would hold slightly less than 10% interest in Company A.
3. The Subscription Agreement contained the following material terms:

Lock-up and Subscription Shares not counted as public shares

- a. the Subscription Shares would be subject to a lock-up period of six months from the listing date and would not be counted as part of the public float at the time of listing;

Adjustment provision

- b. the subscription price of the shares would be adjusted using a pricing formula to guarantee a minimum discount of approximately 10% to the IPO offer price of the shares through the issuance of bonus shares by the Controlling Shareholder (the ‘Adjustment Provision’). Such shares, if required, would be issued before the commencement of dealings of shares on the Exchange. However, if necessary to maintain the Controlling Shareholder’s shareholding at not less than 50% the Pre-IPO Investor would be compensated in cash by the Controlling Shareholder instead of through the issuance of bonus shares;

Put Option

- c. the Controlling Shareholder also granted a Put Option to the Pre-IPO Investor to put the Subscription Shares to the Controlling Shareholder in an option period falling on the eighteenth month after listing at an option price equals to the original subscription price per share plus an agreed rate of interest but less any dividends received by the Pre-IPO Investor;

Exit option if listing did not proceed

- d. if the listing of Company A's shares did not take place by an agreed date, the Pre-IPO Investor would be entitled to request the Controlling Shareholder or Company A to buy back the Subscription Shares at a price equals to the subscription price per share plus an agreed rate of interest but less any dividends received.

THE ISSUE RAISED FOR CONSIDERATION

- 4. Whether a placing of Company A's shares to the Pre-IPO Investor prior to listing that met the technical requirements regarding disclosure, lock-up and public-float as memorialised in Listing Decision HKEx-LD36-1 complied with Listing Rule 2.03), where:
 - a. the investment would be completed after approval in principle by the Listing Committee and shortly before listing;
 - b. the Pre-IPO Investor would receive a guaranteed discount to the IPO offer price of the shares upon listing; and
 - c. the Pre-IPO Investor would receive a put option allowing the purchased shares to be resold to Company A or its controlling shareholders after listing at approximately the same price as was paid for the shares plus agreed interest?

APPLICABLE LISTING RULES OR PRINCIPLE

- 5. Listing Rules 2.03(2) and (4) require that:
 - (2) the issue and marketing of securities is conducted in a fair and orderly manner and that potential investors are given sufficient information to enable them to make a properly informed assessment of an issuer...and
 - (4) all holders of listed securities are treated fairly and evenly...
- 6. Listing Decision, HKEx-LD36-1 published in October 2003 ('HKEx-LD36-1') states the following regarding pre-IPO placings:

The Exchange was of the view that, as a general principle on the Main Board, placings of shares shortly before a listing application should be permitted subject to full disclosure in the prospectus. However, the placee may be subject to a lock-up of his shares. The question of whether the placee should be subject to a lock-up is determined on a case-by-case basis having regard to all the circumstances of the case.

THE ANALYSIS

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7. The Exchange noted that the Subscription Shares were subject to a lock-up period of six months from the listing date and would not be counted as part of the public float at the time of listing. As such, the arrangements contemplated in the Subscription Agreement met the technical requirements described in HKEx-LD36-1.
8. However, the Exchange considered that the scenario contemplated in HKEx-LD36-1 was a ‘simple’ scenario where a pre-IPO placing was conclusively completed before listing with price and commitments affixed on the relevant parties.
9. The Exchange considered that the facts of the present case were highly unusual in that:
 - a. the Adjustment Provision in the Subscription Agreement effectively enabled the Pre-IPO Investor to complete its investment in Company A only after approval in principle by the Listing Committee and shortly before listing;
 - b. the Adjustment Provision effectively created two different pricing for the same securities at listing: one for the Pre-IPO Investor at a minimum guaranteed discount of approximately 10% up to a maximum discount of 25% to the offer price of the shares; and one for the public; and
 - c. the Put Option created rights held by the Pre-IPO Investor that were not generally available to the public investors.

Listing Rule 2.03

10. Mindful of the unusual circumstances of the present case, the Exchange reviewed the pre-IPO placing in light of the requirements of Listing Rule 2.03 and concluded that the pre-IPO placing was not in compliance with the principles in Listing Rule 2.03 for the following reasons:
 - a. the Pre-IPO Investor was in substance a financial investor and not a strategic investor. It was difficult to see how the Pre-IPO Investor being in an industry different from Company A could add value to Company A as a strategic investor;
 - b. the arrangements were being entered into shortly before listing but the

Pre-IPO Investor was obtaining shares at a discount to the offer price. These arrangements were inconsistent with the general experience with strategic investors that was contemplated in HKEx-LD36-1;

- c. although there are no specific provisions in the Listing Rules against two different prices for the same securities on the date of listing, the Exchange would not wish to see this becoming the ‘norm’ in listing applications. The presence of such arrangements were viewed as inconsistent with the requirements of Listing Rules 2.03(2) and 2.03(4) and raised possible questions regarding Company A’s suitability for listing given the use of unorthodox approach for fund raising;
- d. the few precedent cases quoted by the sponsor in support of an initial offer of shares at different IPO share prices were offerings by companies controlled by the PRC or Hong Kong government at the time of listing, where different prices were afforded to individual investors based on an objective criterion (eg possession of a HKID card). The precedents were not considered to be comparable to the present case; and
- e. the Adjustment Provision which effectively created two different prices for the same securities at listing would potentially create a disruptive effect at the time of listing that was inconsistent with Listing Rule 2.03(2). Disclosure of the arrangements in the prospectus was not considered to be sufficient to counteract the potential market disruption.

THE DECISION

- 11. The Exchange determined that the terms of the pre-IPO placing were contrary to the principles of Listing Rule 2.03 and decided not to grant listing approval to Company A until further information about the intended purpose of the special arrangements and the role of the investor was submitted for consideration. The proposal (regarding the Adjustment Option and Put Option) was subsequently withdrawn and the listing was permitted to proceed.