

**CONSULTATION PAPER**  
ON REVIEW OF CONNECTED TRANSACTION  
RULES

**April 2013**



**Hong Kong Exchanges and Clearing Limited**  
**香港交易及結算所有限公司**

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## **How to respond to this paper**

We, The Stock Exchange of Hong Kong Limited (the **Exchange**), a wholly owned subsidiary of Hong Kong Exchanges and Clearing Limited (**HKEx**), invite written comments on the matters discussed in this paper on or before **26 June 2013**. You may respond by completing the questionnaire which is available at <http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201304q.doc>.

Written comments may be sent:

By mail or hand delivery to: Corporate and Investor Communications Department  
Hong Kong Exchanges and Clearing Limited  
12/F, One International Finance Centre  
1 Harbour View Street, Central  
Hong Kong  
**Re: Consultation Paper on Review of  
Connected Transaction Rules**

By fax to: (852) 2524 0149

By email to: [response@hkex.com.hk](mailto:response@hkex.com.hk)  
Please mark the subject line:  
**Re: Consultation Paper on Review of  
Connected Transaction Rules**

Our submission enquiry number is (852) 2840 3844.

Respondents are reminded that we will publish responses on a named basis in the intended consultation conclusions. If you do not wish your name to be disclosed to members of the public, please state so when responding to this paper. Our policy on handling personal data is set out in Appendix IV.

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## EXECUTIVE SUMMARY

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1. This paper presents a number of proposals to amend the connected transaction Rules with a view to refine the scope of connected transactions and to fine tune the framework for continuing connected transactions.
2. In 2010, we amended specific connected transaction requirements that were overly burdensome, restrictive or had unintended effects. We also took note of market comments, and continued to review our current model for regulating connected transactions.
3. We believe that our current regime for regulating connected transactions is appropriate and does not merit a fundamental redesign, having considered the corporate structures of Hong Kong listed issuers and recent developments in regulating related party transactions overseas.
4. We propose to amend specific aspects of the connected transaction Rules:

### *Plain language amendments*

- (1) simplify the language of the connected transaction Rules by replacing the current Chapter 14A with the “Guide on Connected Transaction Rules” issued in April 2012;

### *Scope of connected persons*

- (2) introduce further exemptions for connected persons at the subsidiary level:
  - exempt all transactions between the issuer group and persons connected at the subsidiary level, other than transactions between a subsidiary (or any subsidiary below it) and the person connected with that subsidiary; and/or
  - exempt transactions with persons connected only at the subsidiary level from the shareholder approval requirements;

- (3) clarify that the deeming provision will cover a shadow director or de facto controlling shareholder of the issuer and a person who is accustomed to acting according to a connected person's directions or instructions;
- (4) refine the definition of connected person to exclude certain persons who are unlikely to control or exert significant influence over the issuer;

*Scope of connected transactions*

- (5) exclude from the connected transaction Rules certain transactions involving the issuer group buying or selling interests in target companies from or to third parties where the risk of abuse by the controllers is limited;

*Connected transaction requirements*

- (6) make minor amendments to the regulatory framework for continuing connected transactions:
  - codify in the Rules that we would allow the issuer to seek a mandate from its shareholders for continuing connected transactions over a period of time in lieu of a framework agreement in circumstances where compliance with the requirement would be unduly onerous;
  - for continuing connected transactions of a revenue nature (other than financial assistance not provided in the issuer's ordinary and usual course of business), allow the annual cap to be expressed as a percentage of the issuer's annual revenue or other financial items in its published accounts (as an alternative to the current requirement for a monetary cap); and
  - modify the Rules relating to auditors' confirmation on continuing connected transactions to remove inconsistencies with Practice Note 740 (Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules) issued by the Hong Kong Institute of Certified Public Accountants;

- (7) revise the requirements for transfer, non-exercise or termination of options:
- introduce alternative classification Rules for the transfer or non-exercise of an option granted by a connected person (currently it is a connected transaction classified as if the option is exercised);
  - align the requirements for the termination of an option with those applicable to the transfer or non-exercise of the option;
- (8) minor change to clarify the requirements relating to the independent board committee's opinion on connected transactions;

*Exemptions for connected transactions*

- (9) remove the 1% cap on transaction value which is a condition for the exemption for provision or receipt of consumer goods or services; and
- (10) introduce exemptions for provision of indemnities to directors against liabilities incurred in the course of performing their duties.

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## I. INTRODUCTION

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### Background

5. The Exchange reviews the Listing Rules from time to time to ensure that they address developments in the market and international best practices, and also represent acceptable standards which help ensure investor confidence.
6. Requirements for connected transactions were introduced to the Listing Rules in the 1980s. A number of amendments and updates were made over the years to adapt to market needs. In particular, a substantial revision of the connected transaction requirements was made in 2004 after a market consultation to codify our practices in regulating connected transactions and to tighten the requirements to address corporate governance issues.
7. The connected transaction Rules were last amended in June 2010 following the market consultation in 2009. In that exercise, we amended a number of requirements that were overly burdensome. Major changes included:
  - increasing the de minimis thresholds for exemption from the shareholder approval requirement from 2.5% to 5% for all connected persons, and for fully exempt transactions with persons connected at the subsidiary level from 0.1% to 1%;
  - introducing an exemption for transactions with persons who are only connected with an issuer's insignificant subsidiaries; and
  - revising the definitions of connected person and associate to exclude persons who are not in position to exercise significant influence on the issuer.
8. The table below shows the connected transactions announced by issuers before and after the 2010 Rule changes:

	2011	2009	% change
<b>No. of connected transactions announced</b>			
<b>(1) By nature of requirements</b>			
- Subject to announcement and shareholder approval requirements	622	838	-26%
- Subject to announcement requirement only	1,255	1,195	+5%
<b>Total</b>	----- 1,877 =====	----- 2,033 =====	-8%
<b>(2) By nature of connected persons</b>			
- Connected person at the issuer level	1,574	1,423	+11%
- Connected person at the subsidiary level	248	507	-51%
- Others	55	103	-47%
<b>Total</b>	----- 1,877 =====	----- 2,033 =====	-8%
<b>No. of issuers at the beginning of the year</b>	----- 1,413 =====	----- 1,261 =====	+12%

9. The 2009 consultation also raised some issues that are reviewed in this consultation:

- to consider whether our definition of connected person at the issuer level is sufficiently broad to cover persons who can control or exert significant influence over an issuer;
- to further review the scope of exemptions for connected persons at the subsidiary level and provide additional relief where the risk of abuse is low; and
- to review the compliance framework for regulating revenue transactions with connected persons, including continuing connected transactions.

10. There are also market comments that the drafting and organisation of the connected transaction Rules are complex and difficult to understand. In April 2012, we issued a guide on the connected transaction Rules (the “**Guide**”) to assist issuers to understand and comply with them (hyperlink: [http://www.hkex.com.hk/eng/rulesreg/listrules/listguid/Documents/ctguide\\_e.pdf](http://www.hkex.com.hk/eng/rulesreg/listrules/listguid/Documents/ctguide_e.pdf)). It covers all the existing Rule requirements on connected transactions and the related interpretations published in listing decisions and FAQs. The Guide is written in plainer language and organised in a more straightforward manner.

### **Purpose of this paper**

11. This paper reviews the appropriate model to regulate connected transactions conducted by Hong Kong listed issuers and makes further proposals on the outstanding issues raised in the 2009 consultation. It also proposes a number of technical amendments to simplify the structure of the connected transaction Rules and address anomalies, with a view to improving the clarity of the Rules. These should improve the ease of compliance for issuers while maintaining the same level of investor protection.
12. In this review, we have taken into account the respondents’ views in the last consultation, the corporate structures of Hong Kong listed issuers, and developments in regulation of related party transactions in other jurisdictions.
13. We also take this opportunity to propose simplifying the language of the connected transaction Rules by replacing the current Chapter 14A with the plain language Guide.
14. We have conducted a soft consultation to solicit views from interested groups of issuers on the Rule requirements and some proposals. We thank them for sharing with us their views and suggestions in this exercise.

### **Other related consultation**

15. As part of the proposal to re-write Chapter 14A in plainer language as described in this paper, we propose to include self-contained definitions of connected person and associate in that chapter.

16. Chapter 1 currently contains the general definitions of connected person and associate which are different from those used in Chapter 14A. We have issued a separate consultation paper (hyperlink: <http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp2013042.pdf>) to review other parts of the Rules that use the general definitions in Chapter 1, and seek market views on the proposals to align the definitions of connected person and/or associate in some of these Rules with those used in Chapter 14A.

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## II. REGULATORY APPROACH TO CONNECTED TRANSACTIONS

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### Ownership and control of issuers in Hong Kong

17. Corporate governance has received increased attention in the last decade in light of some high-profile financial scandals and corporate collapses<sup>1</sup> involving abuse of power and illegal activities by corporate insiders.
18. For those markets where issuers are generally widely held by investors (e.g. the UK and the US), corporate governance focuses on addressing the conflict of interests between the management and investors. They are different from most other markets in Asia and Continental Europe where a high concentration of ownership is common.
19. Listed issuers in these jurisdictions are predominantly controlled by a dominant shareholder, for example, an individual/family or state-owned entity. In Hong Kong, about 75% of the issuers have a dominant shareholder who owns 30% or more of the issued shares<sup>2</sup>. In many cases, the dominant shareholders control the issuers through chains of corporate vehicles or complex ownership structures. They appoint and nominate persons to the issuers' boards, and in family-controlled issuers, the family members themselves often hold directorships.

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<sup>1</sup> For example the financial scandals at Enron (2002) and Parmalat (2003).

In the Enron case, the corporate managers engaged in earnings manipulation and accounting irregularities to inflate stock price and gain from the equity and options holding. For example, Enron entered into hedging transactions with related entities, which would not be available from independent parties, to avoid decline in the value of the investments. However, as the hedges lacked economic substance, the company eventually reported significant losses that surprised the market.

Parmalat was a food and dairy company based in Italy. The case revealed that the company's family controlling shareholder used various means to tunnel assets and profits of the company, and covered up the company's losses and financial difficulties through special purpose vehicles and offshore subsidiaries. In 2003, it was reported that Parmalat failed to repay debts despite apparently large amounts of cash and liquid assets on its balance sheet, and it created false documentation and bank accounts.

<sup>2</sup> Estimated based on HKEx and ETNet statistics as of March 2012.

20. It is common for the issuer's dominant shareholder to own a corporate group or business conglomerate. Transactions between the issuer and other companies within the same group frequently occur to facilitate the group's businesses, including intra-group transfers of goods and services for day-to-day operations. While the intra-group transactions may allow efficient use of resources of the group as a whole, they may or may not be in the interest of the issuer itself. The group affiliation provides opportunities for the dominant shareholder to take advantage of the issuer's resources to benefit its private business operations through intra-group transactions.
21. Given the ownership concentration and the lack of separation of owners from managers, the key corporate governance risk is the possible expropriation of minority shareholders by the dominant shareholders. However, the risk of abuse by management, which is more common for widely held issuers, is mitigated as the dominant shareholder is able to monitor the management and his interest is usually aligned with those of all shareholders in that respect.
22. Abusive connected transactions are a common way for connected persons to expropriate minorities. They can take many forms including:
- selling assets at below market prices to, or buying assets at inflated price from, connected persons;
  - providing financial assistance to connected persons on unfair terms;
  - providing goods or services to connected persons (or vice versa) at improper transfer pricing; or
  - issuing new shares to connected persons to unfairly dilute the minority shareholders' ownership in the issuer.
23. In Hong Kong, there is a high level of connected transactions. They are conducted mainly between the issuers and their major shareholder groups (representing about 75% of the connected transactions announced in 2011).

### **Our current approach to regulate connected transactions**

24. In Hong Kong, issuers' connected transactions are governed by the Listing Rules.

25. The purpose of the connected transaction Rules is to protect the interests of shareholders when the issuer group enters into transactions with connected persons. This is achieved through the general requirements that connected transactions are subject to:
- Immediate disclosure by announcements – An issuer must announce a connected transaction as soon as practicable after its terms have been agreed. The announcement must contain details of the transaction and the independent non-executive directors’ views on the transaction.
  - Prior shareholder approval – The connected transaction must be conditional on independent shareholder approval. The issuer must send a circular to its shareholders containing details of the transaction and the opinion of the independent board committee and the independent financial adviser on the terms of the transaction.
26. In addition, issuers are required to disclose their connected transactions in annual reports. Continuing connected transactions are also subject to annual review by independent non-executive directors and auditors.
27. The Rules provide de minimis exemptions for connected transactions (except transactions involving issues of new securities by an issuer) that fall below specific materiality thresholds:

<b>Percentage ratios</b>	<b>Exempt from disclosure and shareholder approval</b>	<b>Exempt from shareholder approval</b>
<ul style="list-style-type: none"> <li>- Total assets test</li> <li>- Revenue test</li> <li>- Consideration to market capitalisation test</li> <li>- Equity capital test</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 0.1%; or</li> <li>- Percentage ratios &lt; 1% (for transactions with persons connected with the issuer’s subsidiaries only); or</li> <li>- Percentage ratios &lt;5% and consideration &lt; HK\$1 million</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 5%; or</li> <li>- Percentage ratios &lt; 25% and consideration &lt; HK\$10 million</li> </ul>

28. There are other exemptions for specific types of connected transactions where the risk of abuse by connected persons is low.

29. In addition to our Rules, issuers making loans to or having similar transactions with their directors (or entities related to the directors) are also subject to the restrictions set out in the Hong Kong Companies Ordinance.
30. Further, the accounting standards (Hong Kong Accounting Standard 24 or International Accounting Standard 24) require issuers to disclose their transactions with related parties<sup>3</sup>, and the relationships between parents and subsidiaries irrespective of whether there have been transactions between those related parties, in their financial statements. The objective is to ensure that the reporting entity's financial statements contain disclosure necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transactions and outstanding balances with such parties.

### **Regulations of related party transactions (“RPTs”) in other jurisdictions**

31. The following provides an overview of the corporate ownership structures and regulatory approaches to connected transactions/RPTs in other major markets in Asia, Europe and America.

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<sup>3</sup> At present, the definition of related party under the Hong Kong Accountant Standard 24 is different from the definition of connected person in our Rules. Under the accounting standard, a related party is a person or entity that is related to the reporting entity:

- (a) A person or a close member of that person's family is related to a reporting entity if that person (i) has control or joint control over the reporting entity; (ii) has a significant influence over the reporting entity; or (iii) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.
- (b) An entity is related to the reporting entity if any of the following conditions applies: (i) The entity and the reporting entity are members of the same group; (ii) one entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group for which the other entity is a member); (iii) both entities are joint ventures of the same third party; (iv) one entity is a joint venture of a third party and the other entity is an associate of the third party; (v) the entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity; (vi) the entity is controlled or jointly controlled by a person identified in (a); (vii) a person identified in (a)(i) has significant influence over the entity or is a member of key management personnel of the entity (or a parent of the entity).

32. In Hong Kong, about 75% of the issuers have a dominant shareholder who owns 30% or more of interests in the issuer<sup>2</sup>. The following information is extracted from a manual for investors prepared by the CFA Institute<sup>4</sup> and gives an indication of the extent of ownership concentration of issuers in other jurisdictions:

	Percentage of publicly traded companies with a controlling share-owner (e.g. family, government, majority block holder) <sup>5</sup>	Other information provided in the CFA Institute's manual for investors
<b>Asia</b>		
<b>China</b>	69%	
<b>Japan<sup>6</sup></b>	7.9%	Some controlling share ownership is a result of the "keiretsu" system <sup>6</sup> .
<b>Malaysia</b>	26%	
<b>Singapore</b>	41%	This number might be higher if a broader cross section of the Singapore market was examined.
<b>South Korea<sup>6</sup></b>	10%	
<b>Continental Europe</b>		
<b>France</b>	32%	
<b>Germany</b>	30%	It is relatively common for companies to have a controlling share-owner.
<b>Italy</b>	47%	Concentration of power with the banks and family-run enterprises has been the traditional ownership structure in Italy.
<b>Other major markets</b>		
<b>Australia</b>	2%	Relatively rare in the Australian market.
<b>Canada</b>	24%	35% for companies incorporated in Ontario.
<b>UK</b>	7.1%	Family controlled companies are not common in the UK. Almost none of the publicly listed companies researched have controlling share-owners.
<b>US</b>	9%	9% for Delaware-incorporated companies researched.

<sup>4</sup> Source: "Shareowner Rights across the Markets: A Manual for Investors" issued by the CFA Institute in 2009, and an update of the manual issued in 2011

<sup>5</sup> The percentages cited reflect information gathered by GovernanceMetrics International (GMI), a firm that rates corporate governance, for a sample of companies found in major indexes in each market.

<sup>6</sup> In Japan and South Korea, corporate shareholding is relatively diverse compared to other Asian countries. In these jurisdictions, many companies belong to business groups (e.g. "keiretsu" in Japan, or "chaebols" in South Korea) where companies within a group own stakes in one another. RPT issues arise from inter-corporate dealings within the group.

### *The UK and the US*

33. Issuers in the UK and the US are more likely to have a diversified shareholding structure and no group affiliation, and the risk of potential abuse mainly arises from RPTs which are primarily conducted between the issuers and their management. This contrasts with many Asian and Continental European markets where many issuers are controlled by major shareholders and the potential for abuse by the management is limited.
34. Both the UK and the US require comprehensive disclosure of RPTs. However, their frameworks for regulating RPTs are different in that the UK requires prior shareholder approval of material RPTs while the US relies on enforcement actions with a legal environment that allows shareholders to seek legal redress quickly and cost effectively.
35. In the UK, RPTs are mainly governed by listing rule 11 which is one of the key “super-equivalent” rules<sup>7</sup> of the UK listing regime. For issuers with a Premium Listing in the UK, the rule requires material RPTs to be subject to immediate disclosure (for RPTs whose percentage ratio exceeds 0.25%) and independent shareholders’ approval (for RPTs whose percentage ratio exceeds 5%).
36. The issue of whether to retain the super-equivalent rules (including the shareholder approval requirements for issuers’ significant transactions and material RPTs) was raised by the UK Financial Services Authority (“**UK FSA**”) in its review of the UK listing regime in 2003<sup>8</sup> and 2008<sup>9</sup>. Market participants strongly supported the UK retaining a super-equivalent regime which provides added protection for investors.

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<sup>7</sup> The UK’s super-equivalent rules, which are higher than the EU minimum requirements, apply to issuers with a Premium Listing. There are two types of listing for the UK main market – a Premium (formerly Primary) Listing and a Standard (formerly Secondary) Listing. A Premium Listing means the company is expected to meet the UK’s highest standards of regulation and corporate governance – and as a consequence may enjoy a lower cost of capital through greater transparency and through building investor confidence. Issuers with a Standard Listing are required to comply with regulatory requirements imposed by the EU that apply to all securities that are admitted to trading on EU regulated markets.

<sup>8</sup> Source: “Discussion Paper 14 – Review of the listing regime” and “Feedback Statement 14 – Review of the listing regime” issued by the UK FSA in July 2002 and January 2003

<sup>9</sup> Source: “Discussion Paper 08/1 – A Review of the structure of the listing regime” and “Consultation Paper 08/21 – Consultation on amendments to the listing rules and feedback on DP08/1” issued by the UK FSA in January 2008 and December 2008

37. Our connected transaction Rules were originally based on the UK model. However, our Rules have been tailored to address the particular nature of the local market. They are more stringent in certain areas, for example, our Rules regulate RPTs of a revenue nature in an issuer's ordinary and usual course of business.
38. The US regime is essentially disclosure-based and backed by strong sanctions. The disclosure requirements for RPTs and executive and director compensation were significantly revised by the US Securities and Exchange Commission ("SEC") in 2006. The revised RPT rules require disclosure of a company's policies and procedures for approving RPTs, and increase the threshold for disclosure from US\$60,000 to US\$120,000. For executive and director compensation, the rules require disclosure of details of compensation in table form with narrative explanation, and a comprehensive, principle-based discussion and analysis of compensation. Further, the SEC adopted new rules in 2011 to require public companies to allow their shareholders to vote on executive compensation (generally known as "say-on-pay" votes) at least once every three years, and to hold a "frequency" vote at least once every six years in order to allow shareholders to decide how often they would like to be presented with the say-on-pay votes.
39. For issuers listed in the US, their RPTs are also governed by the listing rules. For example, the New York Stock Exchange's listed company manual contains a general provision that each RPT should be reviewed by an appropriate group within the listed company and the company should determine whether or not the transaction should be continued. It also requires shareholder approval of issues of securities to related parties (or their associates) in specific circumstances<sup>10</sup>.

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<sup>10</sup> NYSE Listed Company Manual Section 312.03 states that in any transaction, shareholder approval is required before issuance of securities to a related party that exceed 1% of the securities outstanding. However, if the related party involved in the transaction is classified as such solely because such person is a substantial security holder, and if the issuance relates to a sale of securities for cash at a price at least as great as each of the book and market value of the issuer's securities, then shareholder approval will not be required unless the securities to be issued exceeds 5% of the securities outstanding.

40. While the US regime does not require shareholder approval of RPTs in most circumstances, investors can sue issuers and their directors for false or misleading disclosure, and it is practical for them to do so given that class actions and contingency legal fees arrangements are common. Derivative lawsuits are also common in the US.
41. Unlike the US, Hong Kong law does not accommodate class action against issuers and their directors<sup>11</sup>. Derivative suits are possible but they are not common in Hong Kong.

### *Asia*

42. The regulatory approaches to RPTs vary throughout Asia.
43. It is common for issuers in Mainland China, Singapore and Malaysia to have concentrated shareholdings. Their listing rules govern RPTs and are similar to ours in that material RPTs are subject to immediate disclosure and prior approval by independent shareholders. While they adopt different percentage thresholds for immediate disclosure of RPTs<sup>12</sup>, they generally require prior shareholder approval of RPTs when the percentage ratio is or exceeds 5%.
44. On the other hand, prior shareholder approval for RPTs is generally not required in Japan and South Korea. Their rules require disclosure and/or board approvals for RPTs.
45. In Japan, ownership concentration is less common compared to other Asian markets. The issue of RPTs in Japan is transactions between companies within corporate networks (e.g. “keiretsu”) where a group of companies organises around a single company, usually a bank, for their mutual benefit, and these companies often own equity in each other. It is common for member companies to “help” each other out, and minority shareholders in the “supporting” companies may be disadvantaged by the “supported” companies. The law only requires disclosure of RPTs in financial statements<sup>13</sup>.

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<sup>11</sup> In May 2012, The Law Reform Commission of Hong Kong published a report proposing that a mechanism for class actions should be adopted in Hong Kong. The proposal was put forward after considering the responses to the consultation paper released by the Commission in November 2009.

<sup>12</sup> Shanghai: RPTs whose percentage ratio exceeds 0.5%;  
Singapore: RPTs whose percentage ratio exceeds 3%;  
Malaysia: one-off RPTs whose percentage ratio exceeds 0.25% or recurring RPTs whose percentage ratio exceeds 1%

<sup>13</sup> Source: “Inter-Corporate Network Dealings and Minority Shareholder Protection – Cases in Japan” by CFA Institute in March 2010

46. South Korea is dominated by “chaebols” which are powerful, family-controlled conglomerates. In the chaebol, companies own shares in one another and form a web of circular ownership. As a result of the ownership structure, a family which holds a small stake in a company can exert control over it via a network of controlled companies. The Korea Fair Trade Commission imposes a specific requirement for chaebols with assets in excess of KRW2 trillion (US\$1.7 billion) and conducting RPTs above KRW10 billion (US\$8.7 million) to seek approval of the board and disclose the RPTs to the public. In addition, the listing rules require companies to seek board approval for RPTs exceeding 1% of annual revenue or total assets and to report them to shareholders in general meeting<sup>14</sup>.
47. The Organisation for Economic Co-operation and Development (“OECD”)<sup>15</sup> and the CFA Institute<sup>14</sup> published reports on the regulation of RPTs in Asia in 2009. The reports indicated that abusive RPTs are one of the biggest corporate governance challenges in Asia in light of the controlled character of most issuers. Their reports include recommendations to better protect investors against abusive RPTs.
48. The OECD recommends that the legal and regulatory framework for RPTs should provide appropriate and effective threshold-based tiers, referring to materiality for disclosure and shareholder approval or board approval of RPTs according to the risk of potential abuse. Similarly, the CFA Institute considers regulators in Asia should define material RPTs and the threshold values for disclosure or prior approval. Material RPTs, specifically those involving transfers of assets and leading to dilution of minority interests, should be subject to independent shareholder approval.

### *Continental Europe*

49. Concentrated ownership is quite common in the Continental European countries including France, Italy and Germany.

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<sup>14</sup> Source: “Related-Party Transactions, Cautionary Tales for Investors in Asia” by the CFA Institute in January 2009

<sup>15</sup> Source: “Guide on Fighting Abusive Related Party Transactions in Asia” by the OECD in September 2009

50. The EU law requires disclosure of RPTs in issuers' annual and consolidated accounts, including the related party disclosures under IAS 24. In general, there is no requirement for prior shareholder approval of RPTs.
51. In France, the law requires transactions concerning a public company in which a director or a 10% shareholder has an interest to be approved by the board of directors and ratified in the annual shareholder meeting. However, routine RPTs (i.e. transactions at arm's length and in the ordinary course of business) are exempt from the approval requirement. The law also prohibits loans to managers or directors or guarantees for their benefit<sup>16</sup>.
52. In Germany, the law mandates a two-tier board structure for corporations<sup>17</sup>. Under the German corporate governance code, the following RPTs require approval of the supervisory board:
- extending loans to members of the management board or the supervisory board or their relatives;
  - important transactions with members of the management board or persons associated with them;
  - advisory and other service agreements and contracts for work with members of the supervisory board.
53. German law also governs transactions between a company and its dominant shareholder. Transactions that are conducted on unfair terms to the company are regarded as "concealed distributions" and are illegal<sup>18</sup>.
54. In Italy, Consob (the Italian Securities Authority) imposed new regulations on RPTs in March 2010. Under the new rules, material RPTs (i.e. over 5% of the company's market capitalisation, shareholders' equity or total assets or liabilities) must be disclosed, and the independent directors must actively participate in the negotiation of the transactions. The board of directors may only approve a material RPT after having received a favourable opinion from a committee of independent directors.

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<sup>16</sup> Source: "Related Party Transactions and Minority Shareholder Rights" issued by the OECD in April 2012

<sup>17</sup> Under the two-tier board structure, the management board is responsible for managing the corporation, and the supervisory board appoints, supervises and advises members of the management board.

<sup>18</sup> Source: "Constraining Dominant Shareholders' Self Dealing: The Legal Framework in France, Germany, and Italy" by Pierre-Henri Conac, Lucas Enriques, Martin Gelter in 2008

55. Regulation of RPTs in the Continental European countries is generally less stringent than the UK Premium Listing regime. Noting the importance of RPTs to corporate governance, the European Forum for Corporate Governance<sup>19</sup> issued a statement in March 2011 to recommend the adoption of some common principles across Europe to address RPTs, which are broadly in line with the requirements of UK listing rule 11. In particular, the Forum recommended a threshold-based regime under which RPTs representing more than 1% of assets should be immediately announced, and RPTs of more than 5% of assets or which have a significant impact on profits or turnover should also be submitted to a shareholder vote with the related party precluded from voting.
56. Issues with RPTs were also raised in a green paper on the EU corporate governance framework issued in April 2011. The European Commission sought market views on whether minority shareholders need more protection against RPTs. A slight majority of respondents to the question considered that sufficient safeguards are already in place. Respondents in favour of more protection considered that more and better information on RPTs is necessary, and material RPTs should be subject to prior board or shareholder approval. The European Commission has not yet published its decision whether legislative proposals are necessary.

*Other developed markets – Australia and Canada*

57. High concentration of ownership is relatively rare for issuers in Australia. The Corporation Law requires a public company to obtain shareholder approval before it can give any financial benefit to a related party, unless the transaction is at arm's length or falls within other specific exceptions. The Australian Stock Exchange listing rules also require an issuer to seek shareholder approval for acquisitions or disposals of substantial assets (i.e. over 5% of the issuer's equity interest) from or to related parties, or issues of securities to related parties.

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<sup>19</sup> The Forum was established by the European Commission to examine best practices in Member States with a view to enhancing the convergence of national corporate governance codes and providing advice to the Commission.

58. In Canada, a relatively high percentage of public companies (about a quarter) have a controlling shareholder. The securities legislation in the province of Ontario (Multilateral Instrument 61-101) regulates RPTs by requiring disclosure and minority shareholder approval of material transactions.
59. In January 2012, it was reported that the Ontario Securities Commission (“OSC”) was considering a proposal to amend the RPT rules to introduce additional protection for minority shareholders, including lowering the threshold for shareholder approval of RPTs from 25% of the issuer’s market capitalisation to 10%.

## **Our views and conclusion**

60. Our approach to require immediate disclosure and shareholder approval of material connected transactions follows the UK and is also adopted in a number of Asian countries and other developed markets (including Shanghai, Singapore, Malaysia, Australia and Canada).
61. We note that some of the jurisdictions reviewed (e.g. Japan, South Korea, and the Continental European countries) adopt a different approach to regulate RPTs. However, shareholder activism has been on an increase with shareholders demanding a say on corporate governance matters. As an example the US mandated “say-on-pay” shareholder votes at public companies.
62. Given the nature and number of closely held listed issuers in Hong Kong, we believe that a robust framework for connected transactions is a critical component of our corporate governance framework. Having reviewed international best practices we believe that our regulatory approach to connected transactions is appropriate and does not merit a fundamental redesign. However, certain areas where the risk of abuse or financial fraud appears remote merit some relaxation (see Chapters IV to VI).

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### **III. PLAIN LANGUAGE AMENDMENTS TO CONNECTED TRANSACTION RULES**

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63. In April 2012, we issued the Guide to assist issuers to understand and comply with the connected transaction Rules. It illustrates the connected transaction requirements in plainer language with diagrams and examples. It does not amend or vary any Rule requirements.
64. We invited comments from issuers and market practitioners on the accuracy of the Guide and any areas where the Guide can be improved.
65. In this consultation, we propose to simplify the language of the connected transaction Rules by replacing the current Chapter 14A with the Guide. The draft new Chapter 14A and the consequential changes to other parts of the Rules are set out in Appendix I.

#### **Questions**

*Q1: Do you support the proposal to re-write Chapter 14A? If not, why not?*

*Q2: Do you consider that the draft new Chapter 14A in Appendix I accurately reflects the current Chapter 14A? If not, why not?*

*Q3: Do you have any other comments on the draft Rule amendments in Appendix I?*

## IV. SCOPE OF CONNECTED PERSONS AND CONNECTED TRANSACTIONS

66. To ensure a balanced and effective regime for connected transactions, our Rules should capture transactions with persons that pose a real risk of potential abuse. In this chapter, we discuss the issues relating to the scope of connected persons and connected transactions and seek market views on our proposals.
67. In our review, we have made references to the RPT rules in other jurisdictions that adopt a similar approach to require immediate disclosure and prior shareholder approval of material RPTs. Some key features are highlighted below:

	<b>Do connected transaction / RPT rules apply to:</b>				
	<b>Management and major shareholder of the issuer?</b>	<b>Management of the issuer's major shareholder?</b>	<b>Management and major shareholder of the issuer's subsidiary?</b>	<b>Capital transactions?</b>	<b>Revenue transactions?</b>
<b>Hong Kong</b>	Yes	No	Yes	Yes	Yes
<b>Shanghai</b>	Yes	Yes	No – note (a)	Yes	Yes
<b>Singapore</b>	Yes	No	No	Yes	Yes
<b>Malaysia</b>	Yes	Yes	Yes – note (b)	Yes	Yes
<b>UK</b>	Yes	Yes	Yes	Yes	No
<b>Australia</b>	Yes	Yes	No	Yes	No
<b>Canada</b>	Yes	Yes	Yes	Yes	Yes – note (c)

*Notes:*

- (a) *Shanghai Stock Exchange may deem a substantial shareholder of a subsidiary that is material to the issuer to be a related party.*
- (b) *The RPT rules apply only if the person is connected to the transacting subsidiary (or any holding companies of the transacting subsidiary).*
- (c) *Some RPTs in the ordinary and usual of business (including sale or purchase of inventory or lease of property) are exempt from the shareholder approval requirement.*

## PART 1 – SCOPE OF CONNECTED PERSONS

68. Chapter 14A lists out the specific categories of persons that are connected. They are:
- a director, chief executive or substantial ( $\geq 10\%$ ) shareholder of the issuer or any of its subsidiaries;
  - a person who was a director of the issuer or any of its subsidiaries in the last 12 months;
  - a supervisor of a PRC issuer or any of its subsidiaries;
  - an associate of any the above persons; and
  - a connected subsidiary<sup>20</sup>.
69. In addition, the Rules set out some specific circumstances where persons may be deemed to be connected when they conduct transactions with the issuer. There is also a general provision in the Rules that we may deem any other person as connected.

### Issues and proposals

#### A. Definition of connected person

70. Under the current Rules, there are two main categories of connected persons:
- a director, former director, chief executive, or substantial shareholder of the issuer, or an associate of any of them (“**connected person at the issuer level**”); and
  - a director, former director, chief executive, or substantial shareholder of any subsidiary of the issuer, or an associate of any of them (“**connected person at the subsidiary level**”).

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<sup>20</sup> A “connected subsidiary” is any non-wholly owned subsidiary of the issuer where a connected person at the issuer level directly holds a substantial (i.e.  $\geq 10\%$ ) interest in it, or a subsidiary of this non-wholly owned subsidiary.

71. For connected persons at the issuer level, our Rules extend the scope to connected subsidiaries (i.e. any non-wholly owned subsidiary of the issuer where the connected person directly holds a substantial (i.e.  $\geq 10\%$ ) interest in it). A connected person at the issuer level can control or exert significant influence over the issuer and its subsidiaries. If that person also has a material direct interest in that subsidiary, it is possible he may exercise influence over transactions between the subsidiary and the issuer (or its other subsidiaries) to obtain benefits through his direct interest in that subsidiary.
72. The following is a breakdown of the 1,877 connected transactions announced by issuers in 2011:

<b>By nature of connected persons</b>	<b>Number</b>	<b>%</b>
<b>Persons connected at the issuer level</b>	<b>1,574</b>	<b>84%</b>
<b>Persons connected only at the subsidiary level</b>	<b>248</b>	<b>13%</b>
<b>Others</b>		
- <i>Connected subsidiaries</i>	24	
- <i>Third parties whose transactions with the issuers fell under Rule 14A.13(1)(b)</i>	13	
- <i>Investment managers/advisers or custodians</i> <sup>21</sup>	13	
- <i>Deemed connected persons</i>	5	
	-----	
	<b>55</b>	<b>3%</b>
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<b>Total</b>	<b>1,877</b>	<b>100%</b>

### ***Related parties in other jurisdictions***

73. Similar to our Rules, related parties in the other jurisdictions reviewed include an issuer's key management personnel and major shareholder, and persons connected with them:

<sup>21</sup> For investment companies only

	<b>Are the following persons defined as connected persons/related parties?</b>		
	<b>The issuer's key management personnel</b>	<b>The issuer's major shareholder (Shareholding threshold)</b>	<b>Persons or entities connected with the key management personnel or major shareholder (e.g. a family relation or a control through ownership)</b>
<b>Hong Kong</b>	<b>Yes</b> <ul style="list-style-type: none"> <li>▪ Director, chief executive</li> <li>▪ Supervisor (for PRC issuer only)</li> </ul>	<b>Yes</b> ( $\geq 10\%$ )	<b>Yes</b>
<b>Shanghai</b>	<b>Yes</b> <ul style="list-style-type: none"> <li>▪ Director, supervisor, chief executive officer</li> <li>▪ Other senior officer<sup>22</sup></li> </ul>	<b>Yes</b> ( $> 5\%$ ; or controlling shareholder <sup>23</sup> )	<b>Yes</b>
<b>Singapore</b>	<b>Yes</b> Director, chief executive	<b>Yes</b> ( $\geq 15\%$ )	<b>Yes</b>
<b>Malaysia</b>	<b>Yes</b> Director, chief executive	<b>Yes</b> ( $\geq 10\%$ ; or $\geq 5\%$ and being the largest shareholder)	<b>Yes</b>
<b>UK</b>	<b>Yes</b> Director	<b>Yes</b> ( $\geq 10\%$ )	<b>Yes</b>
<b>Australia</b>	<b>Yes</b> Director	<b>Yes</b> ( $\geq 10\%$ )	<b>Yes</b>
<b>Canada</b>	<b>Yes</b> Director, president, vice-president, secretary, treasurer, general manager	<b>Yes</b> ( $>10\%$ )	<b>Yes</b>

74. At the holding company level, the scope of related parties in the other jurisdictions (except Singapore) is more extensive than ours in that related parties include key management personnel of the issuer's major shareholders:

<sup>22</sup> Include deputy chief executive officer, board secretary, financial officer, and any person defined as a senior officer in the issuer's articles of association

<sup>23</sup> Under the Shanghai rules, control means "to be in a position to decide an enterprise's financial and operational policies and thereby obtaining interest from the enterprise's business operations". This include, among others, holding the largest number of stocks of the company or able to decide more than half of the directorship on the company's board of directors by exercising voting rights.

	<b>Are members of key management personnel of the issuer’s major shareholder defined as connected persons/related parties?</b>
<b>Hong Kong</b>	No
<b>Shanghai</b>	<b>Yes</b> ( <i>Directors and chief executive officers and senior officers of the issuer’s controlling shareholder</i> )
<b>Singapore</b>	No
<b>Malaysia</b>	<b>Yes</b> ( <i>Directors and chief executive of the issuer’s holding company</i> )
<b>UK</b>	<b>Yes</b> ( <i>Directors of the issuer’s holding company and fellow subsidiaries</i> )
<b>Australia</b>	<b>Yes</b> ( <i>Directors of the issuer’s controlling shareholder and subsidiaries</i> )
<b>Canada</b>	<b>Yes</b> ( <i>Directors and senior officers of the issuer’s controlling shareholder</i> )

75. At the subsidiary level, the RPT rules in other jurisdictions are less stringent than ours:

- In Shanghai<sup>24</sup>, Singapore and Australia, persons connected at the subsidiary level are not related parties.
- In Malaysia, the RPT rules apply to persons connected at the subsidiary level only if the transaction is conducted between a subsidiary (or any subsidiary below it) and a person connected with that subsidiary.
- While the UK and Canada treat persons connected at the subsidiary level as related parties, they have a narrower definition of connected transaction subject to their rules (see also Part 2 below). The UK exempts all RPTs of a revenue nature conducted in the issuer’s ordinary and usual course of business. In Canada, the OSC exempts a wide scope of RPTs in the ordinary course of business (including sale or purchase of inventory and lease of property) from the shareholder approval requirement. Further, its threshold for shareholder approval (25% of issuer’s market capitalisation) is much higher than the 5% threshold adopted in our Rules.

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<sup>24</sup> Under the guidance note published by the Shanghai Stock Exchange in 2011, it may deem the substantial shareholder of a significant subsidiary of the issuer as a related party on a case-by-case basis.

## **A(1) Connected persons at the issuer level**

76. Our definition of connected person includes an issuer's directors and substantial shareholders (direct or indirect) and their associates as these persons can control or exert significant influence over the issuer. This is broadly comparable with those in other jurisdictions.
77. We note the RPT rules in other jurisdictions reviewed (except Singapore) define directors of an issuer's controlling shareholder/holding company, and persons connected with them, as related parties. This requirement safeguards against influence exerted by these directors over the issuer through their positions in the controlling shareholder/holding company.
78. We note the difference and consider our current Rules to exclude directors at the controlling shareholder/holding company level from the definition of connected person to be suitable for our circumstances. This is because:
- Given the high concentration of ownership of issuers in Hong Kong, the key corporate governance risk is the possible expropriation of minority shareholders by the dominant shareholder who controls the issuer. This is consistent with our review of 2011 announcements where a vast majority of connected transactions (75%)<sup>25</sup> were conducted with issuers' substantial shareholders or their associates.
  - Our definition of connected person includes an issuer's directors and substantial/controlling shareholder (direct or indirect), and their associates. It already covers directors at the holding company level who are also directors of the issuer, or associates (e.g. relatives) of the issuer's other directors or dominant shareholder. The effect of extending the Rules would be to catch those individuals whose only relationship is their directorship in the holding companies. However, it is less likely that an individual director of the holding company can, acting alone, unduly influence the issuer. The ultimate dominant shareholder has the incentive and power to monitor the directors (other than himself or his associates) in the interests of all shareholders.

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<sup>25</sup> The remaining 25% include transactions with (i) issuers' directors or their associates (9%); (ii) persons connected only at the subsidiary level (13%); and (iii) other connected persons such as connected subsidiaries and deemed connected persons (3%).

- Transactions between issuers and persons who are only directors of their holding companies (or parties connected with these directors) are not common in Hong Kong. We did not find any such transactions based on the RPT disclosures<sup>26</sup> in 95 issuers' annual reports and interim reports<sup>27</sup>.
79. In the soft consultation, issuers consulted were of the view that the Rules should not be extended to directors of an issuer's controlling shareholder/holding company. They considered that these directors may only exercise influence over the issuer on a collective basis. An individual director of the controlling shareholder/holding company cannot influence the issuer on his own, and the issuer's directors would not transfer benefits to a person simply because he is a director of the controlling shareholder/holding company. The issuers also expressed that they would have practical difficulty in complying with such requirements as directors of the controlling shareholders/holding companies are not parties to the listing agreement and therefore not governed by the Rules. The issuers cannot compel these directors to provide information about their companies and persons closely related to them. It would also create significant administrative burden on the issuers in monitoring day-to-day transactions with these directors and all their controlled entities as our Rules govern a wide scope of transactions, for example, revenue transactions conducted in the ordinary and usual course of business.
80. We believe that our definition of connected person at the issuer level is sufficiently broad and covers persons that pose a higher risk of potential abuse. Extending the Rules to directors of the controlling shareholder/holding company may create substantial compliance burdens on issuers without much additional benefits.

## **Question**

***Q4: Do you agree that there is no need to extend the definition of connected person to the key management personnel of an issuer's controlling shareholder/holding company? If not, why not?***

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<sup>26</sup> HKAS 24 / IAS 24 (Related Party Disclosures) requires an entity to disclose, among others, transactions with key management personnel of its parent in its financial statements.

<sup>27</sup> These annual reports were released by issuers between October 2009 and April 2011, being the sample selected for the Exchange's Financial Statement Review Programme 2011.

## **A(2) Connected persons at the subsidiary level**

### *Background*

81. The issue whether the definition of connected person should include persons connected at the subsidiary level was considered in the 2009 market consultation.
82. There was strong market support for excluding persons connected only at the subsidiary level from the definition of connected person. The respondents agreed that these persons are unlikely to have undue influence over an issuer's action because of their relationships with the issuer's subsidiaries. As the issuer has a majority control over its subsidiaries, any undue influence on a subsidiary by persons connected at the subsidiary level would be subject to the check and balance of the issuer's board of directors who should act in the interest of the issuer and its shareholders as a whole. There is no conflict of interest in this situation given the alignment of interest between the issuer and its public shareholders.
83. However, some respondents were concerned about possible abuse if a general exemption were to be granted to all these connected persons. They considered that such a change would be material, and suggested that it be implemented gradually.
84. To address the concern, we decided to adopt a phased approach. As the first stage, we introduced exemptions for transactions with persons connected at the subsidiary level where the subsidiaries are insignificant in size relative to the issuer. We also proposed to further review the scope of the exemptions for connected persons at the subsidiary level and consult the market on further proposals.
85. The exemptions introduced in 2010 reduced issuers' compliance burdens. In 2011, transactions with persons connected only at the subsidiary level represented about 13% of all connected transactions announced by issuers, compared to 25% in 2009. However, our current Rules on connected persons at the subsidiary level continued to be more stringent than those in all other jurisdictions reviewed.

*Our further proposals*

86. As discussed in Chapter II, many issuers in Hong Kong are controlled by a dominant shareholder and the key corporate governance risk is the possible expropriation of minority by the dominant shareholders. Of the connected transactions announced in 2011, transactions involving persons connected at the subsidiary level accounted for 13% only (248 transactions). We have analysed these connected transactions and note the following:

	<b>Number</b>	<b>%</b>
<b>1. Nature of connected person</b>		
<b>Subsidiary's director/chief executive</b>	28	11%
<b>Subsidiary's substantial shareholders</b>	213	86%
<b>Subsidiary's substantial shareholder and director</b>	7	3%
	-----	-----
	248	100%
<b>2. Relationship between the connected person at the subsidiary level and the transacting subsidiary</b>		
<b>Connected person who is connected with the transacting subsidiary or its holding company</b>	90	36%
<b>Connected person who is not connected with the transacting subsidiary or its holding company</b>	158	64%
	-----	-----
	248	100%
<b>3. Nature of connected transactions</b>		
<b>Capital transactions</b>	118	48%
<b>Revenue transactions</b>	130	52%
	-----	-----
	248	100%
<b>4. Size of connected transactions</b>		
<b>Subject to announcement only</b>	131	53%
<b>Subject to announcement and shareholder approval</b>	117	47%
	-----	-----
	248	100%

- Of the 248 transactions, the majority (64%) were transactions between a connected person at the subsidiary level and the issuer or its other subsidiary (i.e. other than the subsidiary which is associated with the connected person). In these cases, the connected person was unlikely to have undue influence over the actions of the issuer or the transacting subsidiary. 36% represented transactions (90 transactions) between a subsidiary of the issuer and the person connected to it.
  - Of the 248 transactions, a majority (53%) were immaterial to the issuers and required disclosure by announcement only. The remaining 47% were more material and required disclosure and shareholders' approval.
  - Of the 248 transactions, a majority (52%) were revenue nature transactions. The remaining 48% were capital transactions. Of the 90 transactions between the issuer's subsidiary and a person connected to it, 76% were revenue nature transactions.
87. Only 13% of transactions were conducted with persons connected at the subsidiary's level. These transactions were subject to the oversight of the issuer's board of directors, who are independent of the connected persons and whose interest is aligned with the minority shareholders. The connected persons are unlikely to be able to influence the actions of the issuer or the transacting subsidiaries. This is particularly the case for transactions between a connected person at the subsidiary level and the issuer or its other subsidiary (i.e. other than the subsidiary which is associated with the connected person), which make up a majority (64%) of the transactions conducted with persons connected at the subsidiary level. However, issuers are required to establish additional systems and controls to identify and monitor these transactions. This is particularly burdensome for issuers that have a substantial number of subsidiaries or a large number of directors and substantial shareholders at the subsidiary level.
88. A small number of transactions were conducted between a subsidiary and persons connected with that subsidiary (i.e. 90 transactions, representing 36% of the 248 transactions). While some may argue that these connected persons have influence over the transacting subsidiaries and therefore may influence the terms of the transactions, we maintain that they are nevertheless subject to the oversight of the issuer's board whose interest is aligned with the minority shareholders. The potential for abuse is limited.

89. For these 90 transactions, most (87%) of these transactions between a subsidiary and its connected persons involved substantial shareholders of the subsidiary or their associates. It is likely that these transactions arise commercially, for example, the transfer of goods, service or technology between joint venture partners (76% of transactions were revenue in nature). In these circumstances, there is no conflict of interest as the joint venture partners operate independently and transactions with them are negotiated at arm's length. Proposals to exempt these connected persons would ease issuers' compliance burden, particularly those who have legitimate business arrangements with international joint venture partners and have difficulties in getting these joint venture partners to comply with the connected transaction requirements.
90. In view of the above, we propose to provide the following exemptions which may be adopted together or separately:

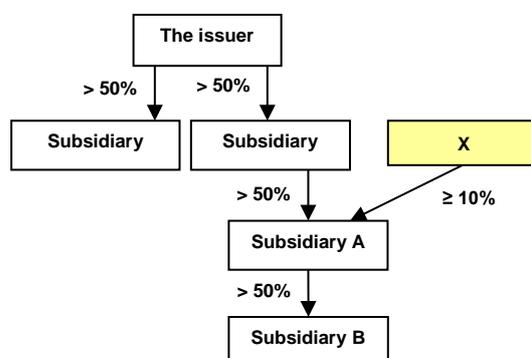
**(a) Exempt transactions with persons connected only at the subsidiary level from the independent shareholder approval requirement**

Given there is no conflict of interest between the issuer's board and its shareholders, approval of these transactions by the issuer's board (including independent non-executive directors) should provide sufficient safeguards against possible abuse by connected persons at the subsidiary level.

As noted in paragraph 86, of the 248 connected transactions that involved persons connected only at the subsidiary level in 2011, 117 transactions (47%) required disclosure and shareholder approval, and 131 transactions (53%) required disclosure only. Under this proposal, the 117 transactions would be approved by the issuer's board and disclosed by the issuers.

**(b) Exempt all transactions between the issuer group and persons connected at the subsidiary level, other than transactions between a subsidiary (or any subsidiary below it) and the person connected with that subsidiary**

For example, X is a substantial shareholder of Subsidiary A and a connected person at the subsidiary level. Under the proposal, X would be treated as a connected person of the issuer only when it enters into transactions with Subsidiary A or B, given X's potential influence over Subsidiaries A and B.



As noted in paragraph 86, of the 248 connected transactions that involved persons connected only at the subsidiary level, about 36% were transactions between a subsidiary (or the subsidiary below it) and the person connected with it.

We noted in paragraphs 88 and 89 above that these transactions should be conducted on normal commercial terms and would not require additional safeguards, particularly since in many cases, these subsidiaries are joint ventures whose business models involve transactions with joint venturers. However, some may take the view that connected person may be able to influence the transacting subsidiary and benefit from the transactions given his/its direct relationship with the transacting subsidiary. This would be similar to the approach adopted in Malaysia.

## Questions

**Q5: Do you support:**

***(a) the proposal described in paragraph 90(a) to require transactions with persons connected only at the subsidiary level be subject to the approval of the issuer's board members (including independent non-executive directors) who do not have a material interest in the transaction, instead of the approval of shareholders, and disclosed to the shareholders? If not, why not?***

*(b) the proposal described in paragraph 90(b) to exempt all transactions between the issuer group and connected persons at the subsidiary level, other than transactions between a subsidiary (or any subsidiary below it) and the person connected with that subsidiary? If not, why not?*

## **B. The deeming provision**

91. Our definition of connected person is quite specific and adopts bright line tests to determine connectedness (for example, the shareholding thresholds for defining a control or substantial interest in a company). The Rules state that the Exchange may deem the following persons as connected:
- relatives (including in-laws, grandparent, grandchild, uncle, aunt, cousin, nephew or niece) of a director, chief executive or substantial shareholder, or companies controlled by them; or
  - an entity which has entered into an arrangement with a connected person in respect of the transaction between the issuer and that entity.
92. In addition, the Exchange has the power to deem any person as an issuer's connected person.
93. Most other jurisdictions that adopt similar approach to regulate RPTs (including Shanghai, Singapore, Malaysia, the UK, Australia and Canada) also define specific categories of persons as related parties. Some of these jurisdictions also include principle-based tests in their rules to define related parties. In the UK, related parties are defined to include shadow directors and persons exercising significant influence over the issuer. In the UK and Malaysia, a related party's associate includes any person who is accustomed to acting according to the related party. In Australia, related parties include any entity acting in concert with a related party on the understanding that the related party will receive a financial benefit if the issuer gives a financial benefit to the entity.

94. Our definition of connected person does not cover some circumstances. We have encountered situations where parties to the transactions have significant influence over the issuer and stand to benefit from these transactions. For example, the party may be a de facto controlling shareholder or the holder of a substantial amount of convertible bonds of the issuer. Under the current regime, we would need to apply the general deeming provision to egregious cases.
95. We propose to specify that the deeming provision will cover the following persons:
- a shadow director or de facto controlling shareholder of the issuer; and
  - a person who is accustomed to acting according to a connected person's directions or instructions (similar to the test for assessing public shareholders under Rule 8.24).
96. We believe that the proposal would ensure the deeming provision to target at those who are able to exercise significant influence over an issuer.

## **Question**

***Q6: Do you agree with the proposal to introduce principle-based tests described in paragraph 95 for deeming a person as connected? If not, why not?***

## **C. Exceptions to the definition of connected person**

97. Under the Rules, certain categories of persons are excluded from the definition of connected person where the risk of abuse is low. In this section, we identify some areas where the definition may need to be modified or clarified to reflect existing market practice or streamlined to reduce the administrative burdens of issuers.

**C(1) Insignificant subsidiary exemption (if persons connected at the subsidiary level are not excluded from the definition of connected person)**

98. At present the insignificant subsidiary exemption applies to transactions between the issuer group and persons connected with the issuer's insignificant subsidiaries, subject to a 10% restriction on the consideration test for any capital transaction between an insignificant subsidiary and the person connected with that subsidiary.
99. An "insignificant subsidiary" is a subsidiary of the issuer whose total assets, profits and revenue are less than (i) 10% under the percentage ratios for each of the latest three financial years; or (ii) 5% under the percentage ratios for the latest financial year.
100. As the persons are connected only by virtue of their relationship with the insignificant subsidiaries, they have little influence over the issuer group. We propose to exclude all these persons from the definition of connected person, rather than exempting transactions conducted with these persons.
101. The proposal would simplify the current exemption and reduce issuers' administrative burdens as they no longer need to maintain a list of persons connected with the insignificant subsidiaries. Further, capital transactions with these persons that exceed 10% under the consideration test would no longer be connected transactions. We consider the risk of abuse would be low as these transactions would still be subject to the notifiable transaction Rules, in particular disclosure by way of announcement.

**Question**

*Q7: Do you agree with the proposal described in paragraph 100 to exempt all persons connected only because of its relationship with the issuer's insignificant subsidiaries? If not, why not?*

## **C(2) Exemption for trustee interests**

102. In Hong Kong, it is common for a person to hold interests in companies through trust arrangements. Our definition of associate therefore includes the trustees of any trust of which a director, chief executive or substantial shareholder (or if such person is a natural person, any of his immediate family members) is a beneficiary.
103. There are pension schemes or employee share schemes whose participants include connected persons. In the UK and Malaysia, trustees of pension schemes and employee shares schemes are exempt from the RPT rules.
104. For issuers listed in Hong Kong, our practice is to adopt a purposive approach in applying the Rules and we would not treat the trustees of an employee share scheme or occupational pension scheme as the connected persons' associates if the scheme is established for a wide scope of participants and most of the participants are not connected persons.
105. We propose to codify this practice by introducing an exemption for any trustee of an employee share scheme or occupational pension scheme provided that the connected persons' interests in the scheme are less than 10%.

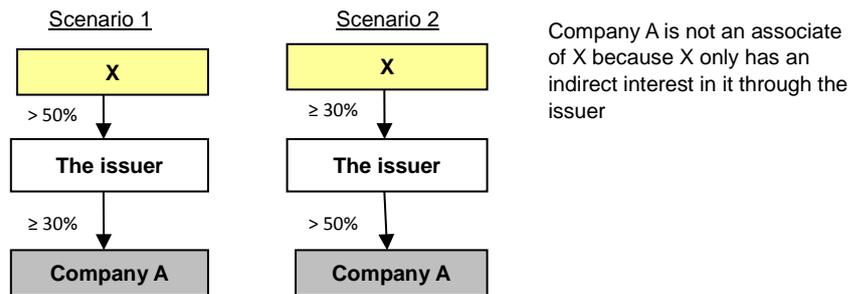
## **Question**

*Q8: Do you agree with the proposal described in paragraph 105 to exclude from the definition of associate any trustee of an employee share scheme or occupational pension scheme if the connected persons' interests in the scheme are less than 10%? If not, why not?*

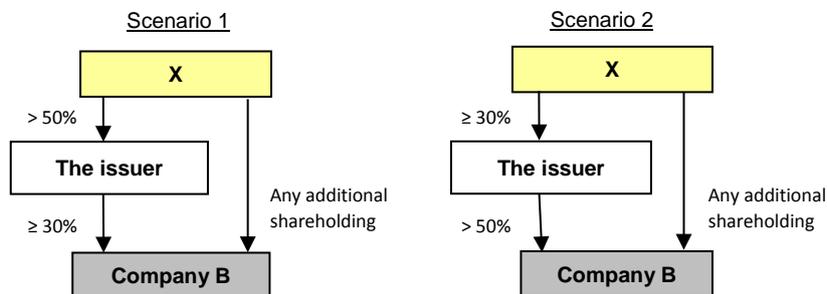
## **C(3) Exemption for connected person holding an interest in an associate through the issuer**

106. Under the Rules, associates include an entity in which a connected person has 30% or more direct or indirect interest.

107. Note 1 to Rule 14A.11(4) (paragraph 9 of the Guide) provides an exemption to the above definition. An entity would not be treated as an associate if the connected person holds an interest in the entity only through his/its shareholding in the issuer (e.g. Company A in the following diagrams). This is because the connected person's interest in the entity is the same as other shareholders of the issuer. There is no concern about the connected person taking advantage of his position to obtain a benefit through this entity to the detriment of other shareholders of the issuer.



108. However, the Rule does not specify whether the exemption would still apply if the connected person has a direct interest in the entity in addition to the indirect interest held through the issuer (e.g. Company B in the following diagrams).



109. In practice, we will consider the materiality of his/its direct interest in the entity compared to the indirect interest held through the issuer (see Listing Decision Series No. LD100-1).
110. We propose to modify Note 1 to Rule 14A.11(4) (paragraph 9 of the Guide) to clarify that the exemption would apply if the connected person and his associate's interests in the entity (other than those held through the issuer) are together less than 10%. This is in line with the threshold currently adopted for defining a "connected subsidiary" where we consider a subsidiary to be connected with the issuer if the connected person's direct interest in the subsidiary is 10% or more.

111. Under the proposal, Company B would not be treated as an associate of X if X's direct interest in it is less than 10%.

## Question

*Q9: Do you agree with the proposal described in paragraph 110 to clarify that the exemption in Note 1 to Rule 14A.11(4) (paragraph 9 of the Guide) would apply if the connected person and his associate's interests in the entity (other than those held through the issuer) are less than 10%? If not, why not?*

## PART 2 – SCOPE OF CONNECTED TRANSACTIONS

### Nature of connected transactions

112. Our connected transaction Rules govern a wide scope of transactions, including both capital and revenue transactions. They may be one-off transactions or continuing transactions.
113. The following is a breakdown of the 1,877 connected transactions announced by issuers in 2011:

<b>By nature of connected transactions</b>	<b>Number</b>	<b>%</b>
<b>Revenue transactions</b>	1,218	65%
<b>Capital transactions</b>		
- Issue of new securities by the issuer	41	2%
- Financial assistance	131	7%
- Acquisitions, disposals and others	487	26%
	1,877	100%

### *RPTs in other jurisdictions*

114. The RPT rules in all other jurisdictions reviewed govern connected transactions of a capital nature.
115. For revenue transactions with related parties:
- They are subject to the RPT rules in other Asian markets reviewed (i.e. Shanghai, Singapore and Malaysia).

However, it should be noted that Shanghai and Singapore have a smaller set of connected persons as they generally do not treat persons connected at the subsidiary level as related parties, and the RPT rules in Malaysia are less stringent than ours in terms of regulating connected persons at the subsidiary level (see paragraph 75). Issuers in these markets may find it less burdensome to comply with the rules governing revenue transactions with related parties.

- In Canada, the OSC rules provide a broad exemption for RPTs in the ordinary and usual course of business from the shareholder approval requirement. They include buying or selling inventory that has been approved by the board, or leasing property on reasonable commercial terms.
- The UK and Australian RPT rules exempt all revenue transactions.

***Revenue transactions with connected persons***

116. As noted above, about 65% of the connected transactions announced in 2011 were revenue in nature. The following is a breakdown of these revenue transactions:

<b>By nature of connected persons</b>	<b>Number</b>	<b>%</b>
<b>Persons connected at the issuer level</b>	1,053	86%
<b>Persons connected only at the subsidiary level</b>	130	11%
<b>Others</b>	35	3%
	-----	-----
	1,218	100%

117. Of the 1,053 revenue transactions with connected persons at the issuer level, about 91% involved the issuer's substantial shareholder or his/its associates (some of them were also directors), and the remaining 9% involved persons who are directors of the issuer or associates of these directors.

118. As discussed in Chapter II, issuers in Hong Kong are predominantly controlled by a dominant shareholder. The dominant shareholder usually has other business interests, and in many cases the issuer is part of a larger business group. It is common for the issuer to conduct transactions with the unlisted group companies of the dominant shareholder. Expropriation of minorities may take the form of not only asset sales or financing arrangements, but also through provision of goods or services in the issuer's ordinary and usual course of business. Transactions between the issuer and other companies within the same group frequently occur to facilitate the group's businesses, including transactions in day-to-day operations. The group affiliation provides opportunities for the dominant shareholder to abuse the issuer's resources to benefit its private business operations through intra-group transactions.
119. In the 2009 consultation, we decided that the connected transaction Rules will continue to govern revenue transactions with connected persons. Nevertheless, we acknowledged there may be areas suitable for refinement, and that we would review these areas in the next phase of review.
120. In Chapter V, we review the compliance framework for continuing connected transactions.

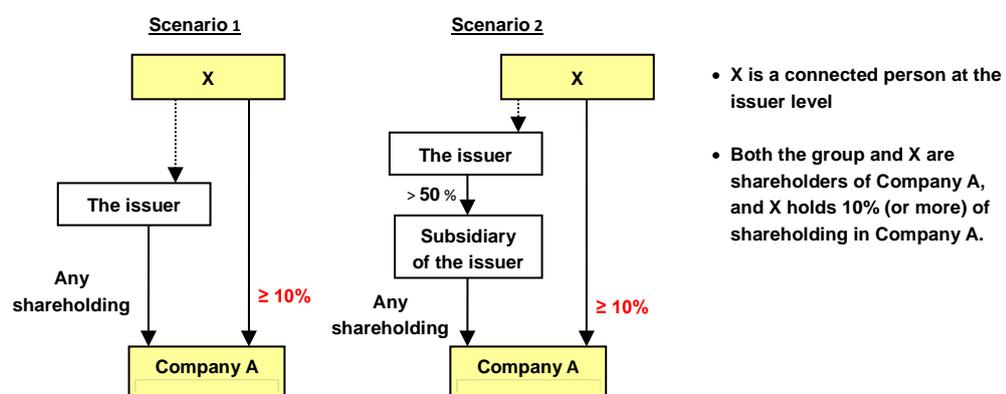
### **Connected transactions with third parties**

121. Under the Rules, transactions between an issuer group and connected persons are connected transactions.
122. Connected transactions also include transactions between the issuer group and third parties that may confer benefits on connected persons. They relate to investments in, or financing arrangements with, companies in which the issuer group and its connected person(s) are, or will as a result of the transactions become, shareholders. The inclusion of transactions with third parties as "connected transactions" is arguably counter-intuitive and may pose compliance challenges for issuers. The following section reviews whether these requirements meet the purpose intended.

## Issues and proposals

### D. Financing arrangements with a commonly held entity

123. Connected transactions include an issuer providing financial assistance to, or receiving financial assistance from, a “commonly held entity”. A commonly held entity is a company whose shareholders include (i) the issuer group; and (ii) any connected person(s) at the issuer level who can control the exercise of 10% or more of the voting power at the company’s general meeting (e.g. Company A in the following diagrams).



124. In 2011 there were no reported connected transactions involving financing arrangements with commonly held entities.
125. In Shanghai, a transaction may be deemed to be connected if the counterparty is an entity of which both the issuer and a related party are shareholders (e.g. provision of financial assistance exceeding the issuer’s investment proportion, giving up the right to make pro-rata capital contribution or the first right of refusal to acquire interest in the entity). In Malaysia, the RPT rules apply to transactions with an entity where the related party has 5% or more interest in the entity (other than through the issuer). The UK RPT rules apply to an arrangement under which the issuer and a related party each provide financing to another party.

126. Financial assistance is generally a higher risk area. Our Rules prevent a connected person at the issuer level from influencing the issuer in financing arrangements with the commonly held entity and benefiting from preferential terms through his/its interest in the entity. There are exemptions if the issuer provides financial assistance to a commonly held entity on a pro rata basis, or receives financial assistance from the entity on normal commercial terms and on an unsecured basis. We propose to retain these Rules.

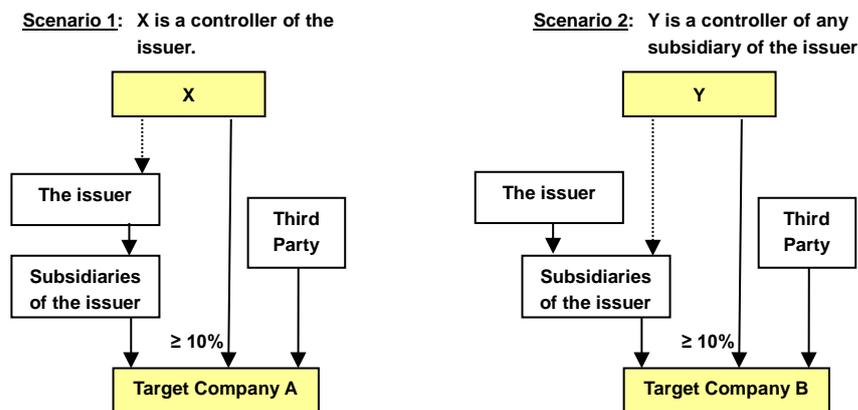
## Question

*Q10: Do you agree that we should retain the connected transaction requirements for financing arrangements with commonly held entities? If not, why not?*

### E. Buying or selling interests in a target company

127. At present, the connected transaction Rules also apply to any acquisition or disposal of interests in a target company in the circumstances described in Rule 14A.13(1)(b) (paragraphs 27 to 32 of the Guide) where each of the issuer and its controller is, or will be, a shareholder of the target company. A “controller” is a director, chief executive or controlling ( $\geq 30\%$ ) shareholder of the issuer or any of its subsidiaries.

- Under Paragraph (i) of Rule 14A.13(1)(b) (paragraphs 27 to 29 of the Guide), the purchase or sale of an interest in a target company from or to a third party is a connected transaction if a controller or proposed controller (or any of his/its associates) is the target company’s substantial ( $\geq 10\%$ ) shareholder. For example, an acquisition or disposal of an interest in Target Company A or B from or to Third Party in the following scenarios:

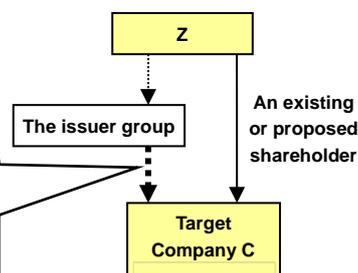


- An issuer may enter into a transaction with a third party which involves the issuer (or the controller) acquiring an interest in a target company of which the controller (or the issuer) is a shareholder. These are also connected transactions under Paragraphs (ii) to (iv) of Rule 14A.13(1)(b) (paragraphs 31 and 32 of the Guide) if the issuer’s investment in the company is of a fixed income nature or on terms different from those available to the controller. For example, a transaction between the issuer and a third party which involves the issuer acquiring an interest in Target Company C or the controller subscribing shares in Target Company D in the following scenarios:

**Scenario 3:**

- Z is a controller of the issuer or its subsidiary.
- Z is, or will become, a shareholder of Target Company C.

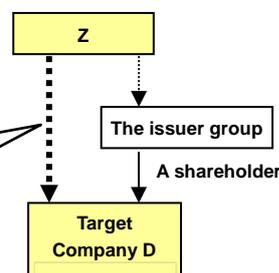
The issuer group proposes to acquire an interest in Target Company C which is (i) of a fixed income nature, (ii) on terms less favourable than those available to Z; or (iii) shares of a different class from those held or to be acquired by Z.



**Scenario 4:**

- Z is a controller of the issuer or its subsidiary.
- The issuer group is a shareholder of Target Company D.

The issuer group enters into a transaction with a third party which involves Z subscribing for shares in Target Company D which are (i) of a different class from those held by the group; or (ii) to be subscribed on specially favourable terms to Z



128. Of the connected transactions announced in 2011, there were only 13 transactions (0.7%) under Paragraph (i) of the Rule (paragraphs 27 to 29 of the Guide) and no transactions under Paragraphs (ii) to (iv) of the Rule (paragraphs 31 and 32 of the Guide).
129. The other jurisdictions reviewed do not have RPT rules to capture these specific types of transactions. In the UK, RPTs include any arrangement (other than revenue transactions in the ordinary and usual course of business) between an issuer and any other person the purpose and effect of which is to benefit a related party. In Malaysia, RPT is broadly defined as a transaction entered into by the issuer group which involves the interest of a related party.

130. Rule 14A.13(1)(b) (paragraphs 27 to 32 of the Guide) governs an issuer's acquisitions from or disposals to third parties of interests in target companies which are also partly owned (or to be owned) by controllers. Its purpose is to prevent the controllers from using the issuer's resources to enhance their control over the target companies.
131. The Rule is a bright line test. Its current scope is too wide and causes significant compliance burdens on issuers as they need to establish systems and controls to capture connected transactions that are not transactions with "connected persons". Having regard to the purpose of the connected transaction Rules, we propose changes in the following areas where the risk of abuse is low:

**(a) Exclude controllers at the subsidiary level**

The Rule currently applies to controllers connected at the issuer level and controllers connected at the subsidiary level. As discussed in section A(2) above, connected persons at the subsidiary level are less likely to have undue influence over an issuer's action simply because of their relationship with the issuer's subsidiaries. The potential for abuse by these persons in a transaction between the issuer and a third party is limited. We propose to exclude transactions with third parties involving target companies partly owned by controllers at the subsidiary level.

**(b) Exclude disposals of interests in target companies**

Paragraph (i) of the Rule (paragraphs 27 to 29 of the Guide) governs both an acquisition and disposal of an interest in a target company in which a controller is a substantial shareholder. We propose to exclude disposals of interests in target companies from the Rule.

While in an acquisition the controller can benefit by using the issuer's resources to acquire an interest in the target company and enhance his control over the target company, it is less likely that a disposal of the target company by the issuer to a third party would confer a benefit on the controller.

In a scenario where both the issuer and the controller dispose of their interests in the target company at the same time, it is possible for the controller to benefit from leveraging on the issuer's disposal. However, we believe that it would be more effective to address this concern by using the current deeming provision which deems a third party transacting with the issuer to be connected if he/it has entered, or proposes to enter, into any agreement or arrangement with a connected person with respect to his/its transaction with the issuer.

**(c) Remove Paragraphs (ii) to (iv) of the Rule (paragraphs 31 and 32 of the Guide)**

These paragraphs apply to an issuer's transaction with any third party if the transaction involves the issuer (or its controller) acquiring interests in a target company in very specific circumstances where the controller has an insignificant (<10%) interest in the target company. Based on our experience, the occurrence of these types of transactions is remote, however the requirements add complexity to the Rules and burden to issuers who need to establish controls to identify possible transactions. To reduce the complexity of the connected transaction Rules and taking into account the operation of the deeming provision in situations involving potential abuse (see (b) above), we propose to remove Paragraphs (ii) to (iv) (paragraphs 31 and 32 of the Guide).

## **Questions**

***Q11: Do you agree with the proposal described in paragraph 131(a) to restrict Paragraph (i) of Rule 14A.13(1)(b) (paragraphs 27 to 29 of the Guide) to transactions involving controllers at the issuer level? If not, why not?***

***Q12: Do you agree with the proposal described in paragraph 131(b) to exclude disposals of interests in target companies from Paragraph (i) of Rule 14A.13(1)(b) (paragraphs 27 to 29 of the Guide)? If not, why not?***

***Q13: Do you agree with the proposal described in paragraph 131(c) to remove Paragraphs (ii) to (iv) of Rule 14A.13(1)(b) (paragraphs 31 and 32 of the Guide)? If not, why not?***

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## V. CONNECTED TRANSACTION REQUIREMENTS

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### Issues and proposals

#### F. Compliance framework for continuing connected transactions (“CCTs”)

##### *Nature of CCTs*

132. Connected transactions may be one-off transactions or continuing transactions. Under the Rules, CCTs are transactions involving provision of goods or services or financial assistance which are carried out on a continuing or recurring basis and are expected to extend over a period of time. They are usually transactions in the issuer’s ordinary and usual course of business.
133. There were about 1,202 CCTs representing 64% of the connected transactions announced in 2011. 95% of the CCTs were revenue transactions and 5% were transactions involving provision of financial assistance.

##### *Our requirements for CCTs*

134. Non-exempt CCTs are subject to the following requirements<sup>28</sup>:
- a written agreement for a fixed period (generally not exceeding 3 years<sup>29</sup>);
  - the agreement must:
    - set out the basis of the calculation of the payments to be made; and
    - reflect normal commercial terms;
  - a monetary annual cap;
  - announcement;
  - circular disclosing details of the transaction, recommendation of the independent board committee and opinion from an independent financial adviser;
  - independent shareholder approval;

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<sup>28</sup> They were introduced in March 2004 based on the results of the 2002 market consultation and our waiver practices for CCTs before the Rule changes.

<sup>29</sup> The duration of the agreement may be longer than 3 years in special circumstances where the nature of the transactions requires the agreement to be of that duration. In this case, an independent financial adviser will need to explain why a longer period for the agreement is required and to confirm that it is normal business practice for the contacts of this type to be of that duration.

- annual review by independent directors to confirm that the transactions have been entered into in the ordinary and usual course of business of the issuer, on normal commercial terms and in accordance with the agreement on terms that are fair and reasonable and in the interest of the shareholders as a whole; and
- annual review by auditors to confirm that the transactions were approved by the board of directors, conducted in accordance with the pricing policy of the issuer, were entered into in accordance with the agreement and have not exceeded the annual cap.

135. In practice, there are two types of agreements for CCTs:

- An “**agreement with fixed terms**” – This agreement sets out the specific terms for a CCT, including the actual consideration in monetary terms, or a fixed formula for determining the consideration. The total consideration for the agreement may be fixed (in monetary terms or by reference to a predetermined formula), or the per unit consideration may be fixed but the total consideration would depend on the volume transacted (e.g. number of units). Examples of agreements with fixed consideration include leasing of properties and the provision of management or consultancy services where the consideration is expressed as a fixed monetary amount or as a percentage of sales or assets. Examples of agreements with no fixed consideration include the sales or purchases of goods or raw materials for a fixed unit price or based on some reference prices published from time to time (e.g. prices prescribed by government, or commodity prices quoted on an exchange). While the total consideration for this type of agreement is not fixed, issuers are required to set an annual cap which provides safeguards by limiting the total size of the transactions.

- A “**framework agreement**” – This agreement sets out the framework within which a series of CCTs are to be conducted over a period. The actual terms of each transaction would be negotiated on a per transaction basis. The consideration for individual transactions may be subject to pricing guidelines or based on a range of parameters, a majority of these agreements require the transactions to be conducted at market prices. Examples of CCTs subject to framework agreements include sales and purchases of goods or services and continuing financial assistance. The agreement would provide for the terms of individual transactions to be negotiated on an arm’s length basis.

136. Based on a sample of CCTs announced in 2011 and 2012, approximately 37% of CCTs were governed by agreements with fixed terms, and approximately 63% were governed by framework agreements<sup>30</sup>.

***Requirements for continuing or recurring RPTs in other jurisdictions***

137. The RPT rules in other Asian markets with concentrated ownership (including Shanghai, Singapore and Malaysia) also govern continuing or recurring transactions with related parties. These requirements are generally less stringent than ours:

- Shanghai requires written agreements for continuing RPTs. The agreements must specify the transaction amount; if not, the issuer must comply with the shareholder approval requirement. For continuing RPTs without framework agreements, the issuer may obtain an annual mandate from shareholders for the transactions and the estimated transaction amount. If an RPT requires shareholder approval, the issuer must provide an audit or appraisal report on the subject matter of the transaction issued by a qualified securities service agency. However, RPTs relating to day-to-day operations may be exempt from the audit or appraisal report requirement.

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<sup>30</sup> Approximately 60% of announcements were randomly sampled.

- In Singapore, the RPT rules do not require an issuer to enter into written agreements or set caps for recurring day-to-day transactions of revenue or trading nature. The issuer may seek an annual mandate from its shareholders for these transactions, and disclose in the shareholder circular details about these transactions including its nature, the identity of the interested persons, the methods or procedures for determining transaction prices, and the historical value of transactions conducted. The audit committee must opine on these transactions. The issuer must seek an independent financial advisor's (IFA) opinion on whether the methods or procedures are sufficient to ensure that the transaction will be carried out on normal commercial terms and will not be prejudicial to the interests of the issuer and its minority shareholders. The IFA opinion is not required for successive renewals if the methods or procedures have not changed and the audit committee can make this confirmation.
- Malaysia adopts a similar approach to Singapore, except that an issuer must set a cap on the transaction value. While Malaysia does not require an IFA opinion, the audit committee must give a view on whether the methods or procedures are sufficient to ensure the recurring RPTs are conducted on prices and terms no more favourable to the related party than those generally available to the public and are not to the detriment of the minority shareholders.

### *Market Views*

138. Before the 2004 Rule amendments, the Main Board Rules did not specifically address CCTs. Our practice was to grant waivers for CCTs subject to a number of conditions, including imposing an annual cap on the transactions, requiring the transactions to be conducted on normal commercial terms and requiring the independent directors and auditors to review the transactions annually. The purpose of the waivers was to ease issuers' burden to comply with the Rules each time a transaction which is part of a continuing series takes place. The conditions established a framework for the conduct of the CCTs and to safeguard against potential abuse.

139. In March 2004, we codified our waiver practice into new Rules for CCTs. As part of the Rule changes, we required issuers to enter into written agreements for a period up to 3 years, and the independent directors and financial advisers to opine on the transactions. Details of our requirements are set out in paragraph 134.
140. The market practice regarding disclosure about CCTs, and in particular, framework agreements vary significantly. Some issuers provide details about the terms and conditions of the proposed framework agreements while others provide general information. Disclosure in the announcements and circulars generally focuses on the identity of the parties, nature of the transactions, reasons for entering into the transactions with the connected persons and the proposed annual caps for the transactions.
141. Rule 14A.35(1) requires the written agreement between the parties to set out the basis of the calculation of the payments to be made. In many instances, pricing policy is disclosed in general terms with no indication of the expected quantum or percentage as to what is meant by “cost plus” or “by reference to”.
142. Examples of disclosure include:

*Case A*

- Under a mutual supply agreement, the issuer has agreed to sell its products and provide storage and transportation services to a connected person for 3 years. The transactions shall be priced in accordance with the following terms:
  - (a) government-prescribed price;
  - (b) where there is no government-prescribed price but where there is government-guidance price, the government-guidance price will apply;
  - (c) where there is neither a government-prescribed price nor a government-guidance price, the market price will apply (*details are not given as to how this will be determined*);
  - (d) where none of the above is applicable, the price is to be agreed between the relevant parties for the provision of the products or services, which shall be the reasonable cost incurred in providing the same plus 10% or less of such cost. The issuer’s directors believe that the 10% margin set out therein is in line with the respective business practices in the PRC market.

*Case B*

- Under a subcontracting agreement, the issuer has agreed to provide subcontracting services to a connected person for producing certain equipment ordered by the customers of the connected person for 3 years. The transactions shall be priced in accordance with the following terms:
  - (a) at the price agreed between the issuer and such customers; if not, at a price to be determined by reference to the average market price (*details are not given as to how this will be determined*); or
  - (b) where (a) above is not appropriate or applicable, at a price to be agreed between the issuer and the connected person on a “cost plus” basis (*details are not given as to how this will be determined*); or
  - (c) where none of the above pricing bases is appropriate or applicable, at a price to be agreed between the issuer and the connected person based on reasonable commercial principles (*not defined*).

*Case C*

- Under a master agreement between the issuer and a connected person in relation to a joint venture project, the parties may in the next 3 years enter into agreements relating to provision of management, marketing and other support services for the project. Such agreements may be entered into from time to time on normal commercial terms (*not defined*).

*Case D*

- Under a master agreement, the issuer has agreed to sell its products to a connected person at a price which is 20% to 25% lower than average wholesale prices (*not defined*) as the connected person has agreed to promote and raise the brand image and market position of the products at its own cost and expense. In addition, the connected person shall be solely responsible for all the costs to be incurred in relation to the sales and distribution of the products.

- It is the issuer's business practice to offer not more than 15% discount to customers purchasing in bulk quantity. However, taking into account the usual discount available to its customers and the commitment of the connected person to promote the issuer's products, the directors considered that the discount of 20% to 25% to be given to the connected person under the master agreement is fair and reasonable and in the interests of the issuer and its shareholders as a whole. The directors confirmed that the terms of sales will be no less favourable than terms offered to other independent third parties who are willing to order similar quantity under similar conditions.
143. One of the key principles behind the Rules is for investors to be given sufficient information to enable them to make properly informed decision. It is questionable whether disclosure about framework agreements governing CCTs provides shareholders with sufficient information about the terms and conditions of the transactions, and particularly the pricing policy, to enable them to assess whether the CCTs will be on normal commercial terms and will not be prejudicial to the interests of the issuer and its minority shareholders.
144. To safeguard shareholders' interest, the Rules on CCTs require an issuer to seek and obtain its shareholders' approval for transactions that are of a significant size relative to the issuer. Once the CCTs are approved:
- the independent directors must review and confirm, at the end of every financial year, that the transactions have been entered into in the ordinary and usual course of the issuer's business, on normal commercial terms (or if there are not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms no less favourable than terms available to or from independent third parties), and in accordance with the relevant agreement governing the transactions on terms that are fair and reasonable and in the interests of the shareholders as a whole; and
  - the auditors must confirm to the issuer's board of directors that the transactions have been properly approved and transacted in accordance with the agreed terms and conditions and have not exceeded the annual cap.

145. We understand from issuers that in order to make this confirmation, the issuer would need appropriate internal control procedures in place; its internal audit would generally review these transactions; the external auditor would perform work on these transactions; and independent directors would scrutinise these transactions.
146. Some market participants consider that our CCTs Rules impose significant burdens on issuers. They generally consider that an issuer transacts with connected persons only where it is commercially desirable to do so. In those circumstances management of the issuer would negotiate for the best terms, in the same manner as transactions with independent third parties. The management of an issuer should have a free hand in operating its business.
147. On the other hand, there are views that the current Rules do not provide sufficient information for shareholders. In particular, the framework agreements governing CCTs normally do not contain detailed terms about the transactions and the safeguards described in paragraph 144 do not provide sufficient assurance that the transactions will be carried on normal commercial terms and will not be prejudicial to the interests of the issuer and its minority shareholders.
148. Under the current regime, the shareholders have in effect given the management a mandate to conduct these transactions, subject to other safeguards provided in the Rules, including a cap on the total amount of the transactions and annual review of CCTs by the independent directors and auditors.
149. We seek market views on the current Rules governing CCTs and the market practice in relation to CCTs conducted under framework agreements.

## **Questions**

***Q14: Do you consider that information provided to shareholders regarding CCTs conducted under framework agreements contains sufficient specificity, in particular as to the methods or procedures to determine pricing for investors to make informed decisions? If not, what information should be disclosed in announcements and circulars? Please give reasons for your view.***

***Q15: Do you consider that the current Rules governing CCTs and market practice in relation to CCTs that are conducted under framework agreements are appropriate? Do they provide sufficient safeguards to ensure that the transactions will be on normal commercial terms and will not be prejudicial to the interests of the issuer and its minority shareholders? Please give reasons for your view.***

## **F(1) Written agreements**

150. In the past, some issuers encountered difficulties in signing framework agreements for CCTs. In some situations the parties to individual transactions were subsidiaries of the connected person and operated independently, and it was impracticable to arrange a framework agreement with the connected person. Waivers from the written agreement requirement were granted on the condition that the issuers would be able to disclose sufficient information for shareholders to assess the transactions.

151. We propose to amend our Rules to reflect the current waiver practice. Under our proposal we may waive the requirement for a written agreement subject to the following conditions:

- (1) The issuer must demonstrate that it has practical difficulty in entering into a written agreement with the connected person for the CCTs, and it is unduly burdensome for it to comply with the Rules each time an individual transaction takes place. Factors that the Exchange will consider include the issuer's relationship with the connected person, and the nature of the CCTs including whether they are of a revenue nature in the issuer's ordinary and usual course of business and the frequency or regularity of the transactions.
- (2) The mandate period must not exceed 3 years.
- (3) The information provided in the issuer's announcement and circular would be comparable to the case where a framework agreement was signed and the terms disclosed in the circular. The issuer's announcement and, if applicable, circular must disclose the terms of the mandate which must include a framework for determining the terms of the transactions as are normally contained in the written framework agreements for CCTs.

- (4) The issuer must re-comply with the announcement and shareholder approval requirements if it proposes to renew the mandate or make a material change to the framework previously disclosed.

## Questions

*Q16: Do you agree with the proposal to codify the waiver practice to allow an issuer to obtain a shareholders' mandate (or a mandate from the board if the transactions is exempt from the shareholder approval requirement) in lieu of a framework agreement with the connected person? If not, why not?*

*Q17: If your answer to Q16 is yes:*

*(a) Do you agree to limit the mandate period to not more than 3 years? If not, why not?*

*(b) Do you agree with the waiver conditions described in paragraph 151? If not, why not?*

## **F(2) Annual cap**

152. The purpose of an annual cap is to provide information for shareholders to gauge the size of the transactions and the extent of the issuer's reliance on them.
153. There are views that the cap requirement should be removed for CCTs of a revenue nature as issuers should not be restricted by caps when they conduct ordinary business on normal commercial terms. Transparency could be achieved by the issuer disclosing the estimated transaction value and updating the market if the estimated value is exceeded. It is unduly burdensome for an issuer to revert to shareholders for approval of a revised cap before it can continue with its normal business operations.
154. On the other hand, the annual cap requirement serves as a safeguard against the issuer's over-reliance on connected transactions. Without a cap, the potential for abuse increases as the connected person may increase the volume of transactions with the issuer to satisfy his/its own business needs during the term of the agreement.

155. We consider it necessary to retain the cap requirement for CCTs. However, as discussed below, we believe that the requirement for issuers to set caps only in monetary terms may be relaxed.
156. The current requirement for a monetary cap was introduced in the 2004 Rule amendments to provide certainty on the absolute size of the transactions. We note the comments from some issuers that it is hard to predict the monetary value of their connected transactions, but it would be easier for them to assess the relative size of the transactions. As a result, some issuers include large buffers in the monetary caps to allow for volatility in market prices and changes in market conditions. In these cases, the monetary caps do not reflect the size or value of the connected transactions, and the monetary cap may not be meaningful to shareholders.
157. We propose to allow the cap for CCTs of a revenue nature to be expressed in monetary terms or as a percentage of the issuer's annual revenue or other financial items in its published audited accounts. However, we consider it necessary to retain the requirement to set cap in monetary terms for those involving financial assistance that is not provided in the issuer's ordinary and usual course of business.

## **Question**

*Q18: Do you support the proposal to allow the cap for a CCT of a revenue nature be expressed a percentage of the issuer's annual revenue or other financial items in its published audited accounts? If not, why not?*

## **F(3) Auditors' confirmation letter**

158. Under the Rules, an issuer must engage its auditors to review its CCTs every year and report whether the transactions:
- have been approved by the issuer's board of directors;
  - are in compliance with the group's pricing policies if the transactions involve provision of goods or services by the group;
  - are in accordance with the agreement governing the transactions; and
  - have not exceeded the cap.

159. In June 2010, the Hong Kong Institute of Certified Public Accountants (“**HKICPA**”) issued the Practice Note 740 - Auditor’s Letter on Continuing Connected Transactions under the Hong Kong Listing Rules (“**PN 740**”). The practice note was prepared in consultation with the Exchange and staff at the SFC. Its purpose is to provide guidance to auditors when they are engaged by issuers to report on CCTs under the Rules. It also helps ensure consistency in the scope of work performed by auditors when reporting on CCTs.
160. As set out in PN 740, auditors may conduct a limited assurance engagement<sup>31</sup> on the CCTs to satisfy the Rule requirements. The auditors’ opinion is expressed in the form of negative assurance. While there are some differences between the wordings of the auditors’ confirmation suggested in PN 740 and those required under our Rules, in practice we accept auditors’ confirmations prepared according to PN 740 as they meet the purpose and intent of our Rules.
161. We propose to codify this practice and modify the wording in the Rules to remove inconsistencies with PN 740. The proposed Rules would require the auditors to confirm whether anything has come to their attention that causes them to believe that the CCTs:
- have not been approved by the issuer’s board of directors;
  - were not, in all material respects, in accordance with the group’s pricing policies if the transactions involve provision of goods or services by the group;
  - were not entered into, in all material respects, in accordance with the relevant agreement governing the transactions; and
  - have exceeded the cap (if applicable).

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<sup>31</sup> A limited assurance engagement, in contrast to an audit, is not designed to obtain reasonable assurance that the CCTs disclosed in the issuer’s annual report are free from material misstatement. It consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. In addition, the auditors will typically test a sample of transactions when carrying out an engagement under PN 740. A limited assurance engagement may bring significant matters affecting the disclosed CCTs to the auditors’ attention, but it does not provide all of the evidence that would be required in an audit.

## Question

*Q19: Do you support the proposal described in paragraph 161 to modify the Rules relating to auditors' confirmation on CCTs in line with PN 740? If not, why not?*

### **G. Requirements for connected transactions involving option arrangements**

162. Under the current Rules, connected transactions include an issuer:
- granting an option to a connected person to buy or sell assets or subscribe for securities;
  - acquiring or accepting an option from a connected person, or exercising or transferring the option;
  - terminating an option (except where the termination is made according to the terms of the original agreement and does not involve any payment of penalty, damages or other compensation); or
  - deciding not to exercise an option granted to it by a connected person.

#### **G(1) Transfer or non-exercise of option**

163. Currently a transfer or non-exercise of an option is a connected transaction classified as if the option is exercised.
164. We consider the requirements are necessary to prevent potential abuse by connected persons in option arrangements. If an option is granted by a connected person to an issuer, the connected person can influence the issuer not to exercise the option, or to transfer it to another party, if the exercise of the option is not in his interest.
165. There are market views that the current Rules are onerous as they require the issuer to calculate the size of any transfer or non-exercise of the option as if the option is exercised. This may overstate the value of the transaction as the exercise price would not be paid.

166. One alternative is to allow the issuer to classify the transaction based on the asset and consideration ratios using the higher of (i) the difference between the exercise price and the value of the assets subject to the option; and (ii) any amount payable or receivable by the group. However, the value of the option assets must be readily ascertainable. If this alternative is adopted, the issuer would be required to provide:

- a valuation of the option assets prepared by an independent expert using generally acceptable methodologies; and
- a confirmation from the independent non-executive directors and independent financial adviser that the transfer or non-exercise of option is fair and reasonable and in the interests of the issuer and its shareholders as a whole.

In any event, the issuer must announce the transfer or non-exercise of the option with the views of the independent non-executive directors and the independent financial adviser.

167. On the other hand, we also note the views that the current classification Rules are appropriate. The connected transaction Rules are to ensure that connected transactions are (i) conducted on terms that are fair and reasonable and (ii) in the interests of the issuer. To assess whether it is in the interest of the issuer to give up its right to buy or sell the underlying assets, it should take into account the total value of the assets as required under the current Rules.

168. We consider that the current Rules to classify a transfer or non-exercise of an option as if the option is exercised should be retained. The proposal described in paragraph 166, if adopted, would provide an alternative means to classify the transaction only if the value of the option assets is readily ascertainable.

## **Question**

***Q20: Do you agree with the proposed alternative classification Rules for any transfer or non-exercise of an option? If not, why not?***

## **G(2) Termination of option**

169. Currently, the termination of an option involving a connected person is defined as a connected transaction. However, the Rules do not require it to be classified as if the option is exercised and do not specify how the size tests should be calculated. If the termination is made according to the terms of the original agreement and does not involve any payment of penalty, damages or other compensation, it is exempt from the connected transaction requirements.
170. We consider that the termination of an option is indistinguishable from non-exercise of the option which is classified as if the option is exercised. To clarify the appropriate treatment under the Rules, we propose that the termination of an option should also be classified as if the option is exercised unless the issuer has no discretion over the termination, for example, it is triggered by an event specified in the original agreement and is outside the control of the issuer.
171. We also propose that if the proposed alternative classification Rules for any non-exercise of an option described in paragraph 166 is adopted, it would also apply to the termination of an option.

### **Question**

***Q21: For any termination of an option involving a connected person:***

- (a) ***Do you agree with the proposal described in paragraph 170 to classify the termination as if the option is exercised unless the issuer has no discretion over the termination? If not, why not?***
- (b) ***Do you agree that the proposed alternative classification Rules described in paragraph 166 should also apply to the termination? If not, why not?***

## **H. Minor changes to clarify the requirements relating to independent advice on connected transactions**

172. Under Rules 14A.21 and 14A.22 (paragraphs 42 and 47 of the Guide), an issuer's independent board committee and independent financial adviser are required to give opinion on the issuer's proposed connected transaction and advise the independent shareholders how to vote. The matters that the independent board committee and the independent financial adviser need to opine on are the same, except that Rule 14A.22 requires the independent financial adviser to state whether the connected transaction is on normal commercial terms and in the issuer's ordinary and usual course of business, but Rule 14A.21 does not specifically require the independent board committee to opine on these matters.
173. To remove the inconsistency, we propose to revise Rule 14A.21 to clarify that the independent board committee also needs to advise whether the connected transaction is on normal commercial terms and in the issuer's ordinary and usual course of business. This is in line with our current practice.

### **Question**

***Q22: Do you agree with the proposed Rule change to clarify that the independent board committee also needs to advise whether the connected transaction is on normal commercial terms and in the issuer's ordinary and usual course of business? If not, why not?***

## VI. EXEMPTIONS FOR CONNECTED TRANSACTIONS

174. To reduce issuers' compliance burden, exemptions and waivers from all or some of the connected transaction requirements are available for specific categories of connected transactions. These apply to connected transactions that are immaterial to the issuer, or specific circumstances where the risk of abuse by connected persons is low.

### Issues and proposals

#### I. De minimis exemptions

175. The de minimis exemptions currently provide both percentage and monetary limits to exempt small transactions. The following table summarises the de minimis thresholds under our Rules and those in other jurisdictions.

	Percentage ratios	Fully exempt	Exempt from shareholder approval
<b>Hong Kong</b>	<ul style="list-style-type: none"> <li>- Total asset test</li> <li>- Revenue test</li> <li>- Consideration to market capitalisation test</li> <li>- Equity capital test</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 0.1%; or</li> <li>- Percentage ratios &lt; 1% (for transactions with persons connected with the issuer's subsidiaries only); or</li> <li>- Percentage ratios &lt; 5% and consideration &lt; HK\$1 million</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 5%; or</li> <li>- Percentage ratios &lt; 25% and consideration &lt; HK\$10 million</li> </ul>
<b>Shanghai</b>	<ul style="list-style-type: none"> <li>- Net asset test</li> </ul>	<p><u>If the connected person is a corporation:</u></p> <ul style="list-style-type: none"> <li>- Transaction value ≤ Rmb 3 million;</li> <li>or</li> <li>- Percentage ratios ≤ 0.5%</li> </ul> <p><u>If the connected person is an individual:</u></p> <ul style="list-style-type: none"> <li>- Transaction value ≤ Rmb 300,000</li> </ul>	<ul style="list-style-type: none"> <li>- Transaction value ≤ Rmb 30 million; or</li> <li>- Percentage ratios ≤ 5%</li> </ul>
<b>Singapore</b>	<ul style="list-style-type: none"> <li>- Net tangible asset test</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 3%; or</li> <li>Transaction value &lt; S\$100,000</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 5%</li> </ul>

	<b>Percentage ratios</b>	<b>Fully exempt</b>	<b>Exempt from shareholder approval</b>
<b>Malaysia</b>	<ul style="list-style-type: none"> <li>- Net asset test</li> <li>- Total asset test</li> <li>- Profit test</li> <li>- Consideration to net asset test</li> <li>- Consideration to market capitalisation test</li> <li>- Equity capital test</li> <li>- For joint venture, business transactions or arrangements, the total project cost to the issuer's total assets; or total equity participation into the joint venture to the issuer's net assets</li> <li>- For disposal or acquisition which took place within last 5 years, original cost of investment to the issuer's net asset</li> </ul>	<p><u>One-off transactions:</u></p> <ul style="list-style-type: none"> <li>- Percentage ratios &lt; 0.25%; or</li> <li>- Transaction value &lt; RM250,000</li> </ul> <p><u>Recurring transactions:</u></p> <ul style="list-style-type: none"> <li>(a) Percentage ratios &lt; 1%;</li> <li>(b) Transaction value &lt; RM1 million</li> </ul> <p><i>Note: The lower of (a) or (b) applies if the issuer's issued capital is less than RM60 million, or the higher of (a) or (b) if the issuer's issued capital is RM60 million or more.</i></p>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 5%</li> </ul>
<b>UK</b>	<ul style="list-style-type: none"> <li>- Gross asset test</li> <li>- Consideration test</li> <li>- Profit test</li> <li>- Gross capital test</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios ≤ 0.25%</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 5%</li> </ul>
<b>Australia</b>	<ul style="list-style-type: none"> <li>- Value of the subject asset or consideration to equity interest of the issuer set out in the latest accounts</li> </ul>	<ul style="list-style-type: none"> <li>- Not specified</li> </ul>	<ul style="list-style-type: none"> <li>- Percentage ratios &lt; 5%</li> </ul>
<b>Canada</b>	<ul style="list-style-type: none"> <li>- Consideration to market capitalisation test</li> </ul>	<ul style="list-style-type: none"> <li>- Not specified</li> </ul>	<ul style="list-style-type: none"> <li>- Consideration ≤ 25% of the issuer's market capitalisation</li> </ul>

176. The monetary limits provide a more relaxed regulatory regime for smaller issuers. For example, for a company with a market capitalisation of less than HK\$1 billion, connected transactions of up to HK\$1 million might not be discloseable even if they exceed the 0.1% percentage threshold, and for a company with a market capitalisation of less than HK\$0.2 billion, connected transactions of up to HK\$10 million might not require shareholder approval even if they exceed the 5% threshold.

177. As set out in the table under paragraph 175, other Asian markets like Shanghai, Singapore and Malaysia also adopt monetary limits to exempt insignificant RPTs, whereas the UK, Australia and Canada do not have any monetary limits. We note that our current limits of HK\$1 million and HK\$10 million are not particularly restrictive compared to those in other Asian markets:

- About 50% of issuers may benefit from the current limit of HK\$1 million for full exemption from the connected transaction requirements<sup>32</sup>. If the limit is set at HK\$5 million, about 76% of issuers may benefit from it<sup>33</sup>. For fully exempt RPTs, Shanghai adopts a monetary limit of Rmb 3 million if the connected person is a corporation or Rmb 300,000 if the connected person is an individual. In Malaysia, the monetary thresholds for one-off RPTs and recurring RPTs are RM250,000 and RM1 million, respectively. Singapore imposes a monetary threshold of S\$100,000 for all types of RPTs.

There are comments in the market that a limit of HK\$1 million is too low for issuers generally. On the other hand, there are also views that shareholders should be provided with adequate disclosure about issuers' connected transactions that do not require shareholders' approval. We seek market views whether the limit should be retained or increased.

- About 14% of issuers may benefit from the current limit of HK\$10 million for exemption from the shareholder approval requirement<sup>34</sup>. If the limit is set at HK\$50 million, about 50% of issuers may benefit from it<sup>32</sup>. We note that among the overseas markets reviewed, only Shanghai imposes a monetary limit (Rmb 30 million). Other Asian markets adopt a more conservative approach and do not specify a monetary limit. We do not propose to increase our limit.

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<sup>32</sup> As at the end of July 2012, about 761 issuers (excluding collective investment schemes listed under Chapter 20 of the Main Board Rules) (50%) have a market capitalisation of less than HK\$1 billion.

<sup>33</sup> As at the end of July 2012, about 1,165 issuers (excluding collective investment schemes listed under Chapter 20 of the Main Board Rules) (76%) have a market capitalisation of less than HK\$5 billion.

<sup>34</sup> As at the end of July 2012, about 220 issuers (excluding collective investment schemes listed under Chapter 20 of the Main Board Rules) (14%) have a market capitalisation of less than HK\$0.2 billion.

## Questions

*Q23: Do you agree that we should retain the monetary limit of HK\$1 million for fully exempt connected transactions? If not, do you think that the limit should be increased to HK\$2 million, HK\$3 million, HK\$4 million, HK\$5 million, or some other amount (please specify with reasons)?*

*Q24: Do you agree that we should retain the monetary limit of HK\$10 million for connected transactions exempt from the shareholder approval requirements? If not, what is the appropriate limit?*

## **J. Exemption for provision of consumer goods or services**

178. Currently an issuer providing or receiving consumer goods or services to or from a connected person is fully exempt from the connected transaction Rules, provided that the transaction meets all the exemption conditions:

- the goods or services must be of a type ordinarily supplied for private use or consumption;
- they must be for the buyer's own consumption or use, and not be (a) processed into the buyer's products, or for resale; or (b) used by the buyer for any of its businesses or contemplated businesses. This condition does not apply if the group is the buyer and there is an open market and transparency in the pricing of the goods or services;
- they must be consumed or used by the buyer in the same state as when they were bought;
- the total consideration or value of the goods or services must be less than 1% of the group's total revenue or total purchases, as published in its latest audited accounts; and
- the transaction must be made on no more favourable terms to the connected person, or no less favourable terms to the group than those available from independent third parties.

179. There are views that the 1% cap is not necessary as the other conditions are sufficiently restrictive to avoid abuse of the exemption. As issuers need to set up systems and controls to monitor the cap, the cost of compliance may be disproportionate to the benefits.
180. The RPT rules in Shanghai, Singapore and Malaysia provide similar exemptions for provision or receipt of goods or services based on a fixed price or publicly quoted price. They do not have a restriction on the transaction value.
181. As there are already de minimis exemptions for immaterial connected transactions, we consider that the exemption for provision of consumer goods and services should primarily be principle-based having regard to the nature of these transactions rather than their size. We note that the other conditions under the current exemption are stringent enough to provide sufficient safeguard for minority shareholders. We propose to remove the 1% cap on transaction value. Other exemption conditions would continue to apply.

## **Question**

*Q25: Do you support the proposal described in paragraph 181 to remove the 1% cap on transaction value for the exemption for provision or receipt of consumer goods or services? If not, why not?*

## **K. Exemption for provision of director's indemnity**

### *Directors' indemnities*

182. Under the Rules, granting an indemnity by an issuer for the benefit of a director is a connected transaction. This covers an issuer granting indemnities in favour of its directors against any claims that may arise from the proper discharge of their duties. In the past, we exempted these indemnities from the connected transaction requirements on a case-by-case basis (see Listing Decision Series No. LD76-4).

183. We propose to codify this practice by introducing a specific exemption for an issuer granting indemnity to a director against liabilities that may be incurred in the course of the director performing his duties, which does not contravene any law of the issuer's place of incorporation<sup>35</sup>. There is a similar exemption in the UK listing rules<sup>35</sup>.

*Insurance for directors against liabilities*

184. An issuer may purchase insurance for directors against liabilities to third parties that may be incurred in the course of performing their duties, including liabilities in connection with any negligence, default, breach of duty or breach of trust relating to the issuer.
185. Under Hong Kong law, a company is prohibited from indemnifying a director against any liability in connection with any negligence, default, breach of duty or breach of trust relating to the company. However, the prohibition does not prevent the company from purchasing or maintaining insurance for the director against any such liability. In the UK, there are similar provisions under the UK Companies Act 2006. The UK listing rules exempt RPTs involving an issuer maintaining a contract of insurance for a director provided that it is in accordance with those specifically permitted under the UK Companies Act 2006.

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<sup>35</sup> In Hong Kong, as part of the exercise to rewrite the Companies Ordinance, the Government has reformed the law on directors' liabilities, including the ability of companies to indemnify directors against liabilities incurred in the course of performing their duties. There are new provisions to allow a company to indemnify a director against liability to a third party if the indemnity does not cover certain liabilities and costs (such as criminal fines, penalties imposed by regulatory bodies, the costs for defending criminal proceedings where the director is found guilty, and the costs for defending civil proceedings brought against the director in which judgment is given against the director). In addition, a loan to, or similar transaction with, a director is exempt from the members' approval requirements if it involves provision of funds to the director to meet expenditure on putting up a defense in any proceedings, investigation or regulatory action in connection with any alleged negligence, default, breach of duty, or breach of trust by the director relating the company, and it is made on the terms that the funds are to be repaid if the director is convicted in the proceedings, or judgment is given against the director in the proceedings, or the court refuses to grant the director relief on the application.

In the UK, there are similar provisions under the UK Companies Act 2006. The listing rules exempt RPTs involving an issuer providing of loans or assistance to a director provided that it is in accordance with those specifically permitted under the UK Companies Act 2006.

186. We propose to introduce a specific exemption for an issuer purchasing and maintaining insurance for a director against liabilities to third parties that may be incurred in the course of performing his duties if it does not contravene any law of the issuer's place of incorporation.

## **Questions**

*Q26: Do you agree with the proposal described in paragraph 183 to exempt an issuer granting indemnity to a director against liabilities that may be incurred in the course of the director performing his duties, if it does not contravene any law of the issuer's place of incorporation? If not, why not?*

*Q27: Do you agree with the proposal described in paragraph 186 to exempt an issuer purchasing and maintaining insurance for a director against liabilities to third parties that may be incurred in the course of performing his duties, if it does not contravene any law of the issuer's place of incorporation? If not, why not?*

*Q28: Do you have any other comments or suggestions relating to the connected transaction Rules?*

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**APPENDIX I : PROPOSED PLAIN LANGUAGE RULE  
AMENDMENTS DESCRIBED IN CHAPTER  
III**

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**(I) Draft new Chapter 14A**

**Chapter 14A**

**EQUITY SECURITIES**

**CONNECTED TRANSACTIONS**

**INTRODUCTION**

Cross-  
references to  
existing  
Rules or  
guidance  
materials

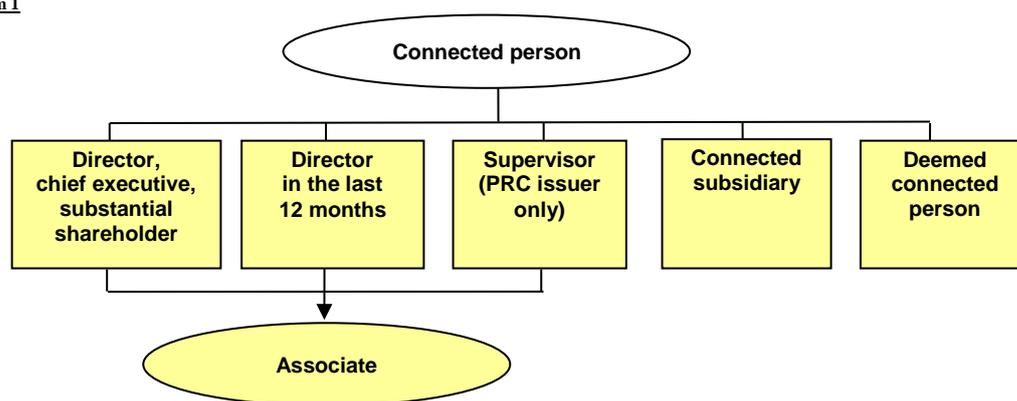
14A.01,  
14A.02,  
14A.03  
(summarised)

- 14A.01 This Chapter applies to connected transactions entered into by an issuer or its subsidiaries. The connected transaction rules ensure that the interests of shareholders as a whole are taken into account by the issuer when a group enters into a connected transaction.
- 14A.02 Connected transactions include both capital and revenue nature transactions. They may be one-off transactions or continuing transactions.
- 14A.03 The general requirements for connected transactions include disclosures in announcements and annual reports, and shareholders' approval. Persons with material interests cannot vote on the resolution approving the transaction. Continuing connected transactions also require annual reviews by independent non-executive directors and the auditors.
- 14A.04 To reduce issuers' compliance burden, exemptions and waivers from all or some of the connected transaction requirements are available for specific categories of connected transactions. These apply to connected transactions that are immaterial to the group, or specific circumstances where the risk of abuse by connected persons is low.
- 14A.04A The rules in this Chapter have been illustrated with diagrams. If there is any conflict between the rules and the diagrams, the rules prevail.

## DEFINITION OF CONNECTED PERSON

- 14A.05 A “connected person” is:
- 1.01, 14A.11(1) (1) a director, chief executive or substantial shareholder of the issuer or any of its subsidiaries;
  - 14A.11(2) (2) a person who was a director of the issuer or any of its subsidiaries in the last 12 months;
  - 1.01, 14A.11(3) (3) a supervisor of a PRC issuer or any of its subsidiaries;
  - 1.01, 14A.11(4) (4) an associate of any the above persons;
  - (5) a connected subsidiary; or
  - (6) a person deemed to be connected by the Exchange.

**Diagram 1**



- 21.13 14A.06 Where an issuer is an investment company listed under Chapter 21, its connected persons also include an investment manager, investment adviser or custodian (or any connected person of each of them).

### Exceptions

#### *PRC Governmental Body*

- 14A.12A(2), 19A.19 14A.07 The Exchange will not normally treat a PRC Governmental Body as a connected person. The Exchange may request an issuer to explain its relationship with a PRC Governmental Body and why it should not be treated as a connected person. If the Exchange decides to treat the PRC Governmental Body as a connected person, the issuer must comply with any additional requirements requested by the Exchange.

#### *Depository*

- 1.01 - (c), 19B.03 14A.08 For a listing of depository receipts, a person holding shares of an issuer as a depository will not be treated as:
- (1) an associate of the holder of the depository receipts; or
  - (2) a substantial shareholder or controlling shareholder of the issuer.

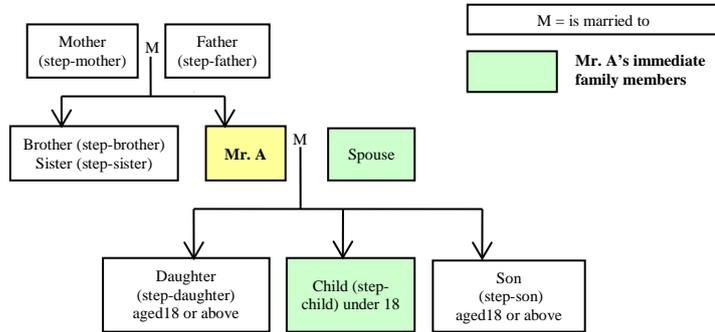
## Definition of associate

14A.09 An “associate” of a connected person described in rule 14A.05(1), (2) or (3) who is an individual includes:

1.01 - (a)(i), (ii),  
19A.04 - (a)(i), (ii)

- (1) (a) his spouse, his (or his spouse’s) child (natural or adopted) or step-child under the age of 18 years (each an “immediate family member”);

**Diagram 2**



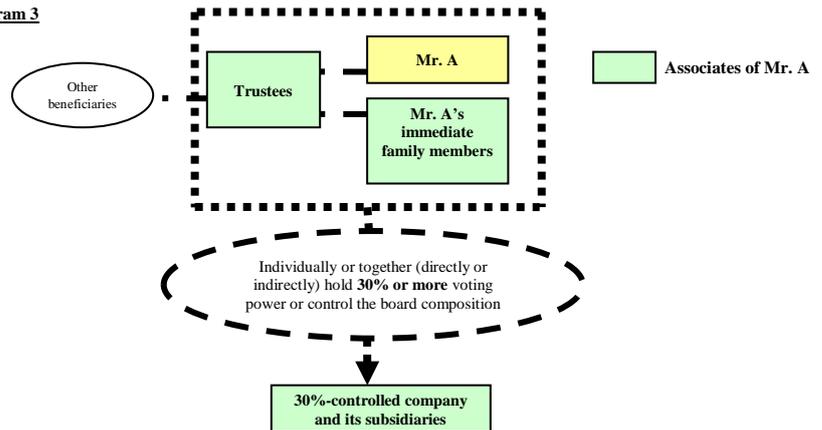
1.01 - (a)(iii),  
19A.04 - (a)(iii)

- (b) the trustees, acting in their capacity as trustee of any trust of which the individual or his immediate family member is a beneficiary or, in the case of a discretionary trust, is (to his knowledge) a discretionary object (the “trustees”); or

1.01 - (a)(v),  
19A.04 - (a)(v)

- (c) a 30%-controlled company held, directly or indirectly, by the individual, his immediate family members and/or the trustees (individually or together), or any of its subsidiaries; or

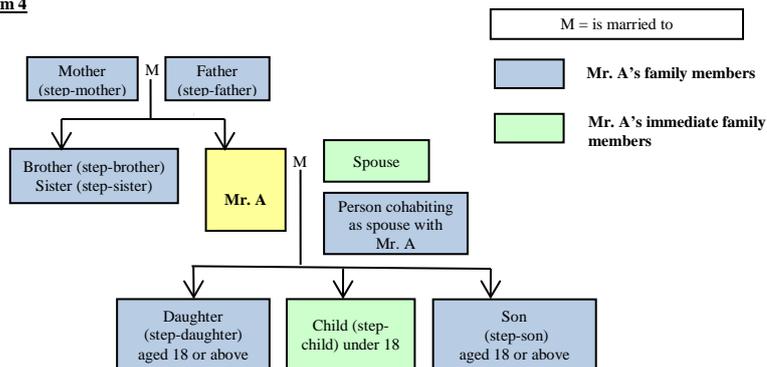
**Diagram 3**



14A.11(4)(b)(i)

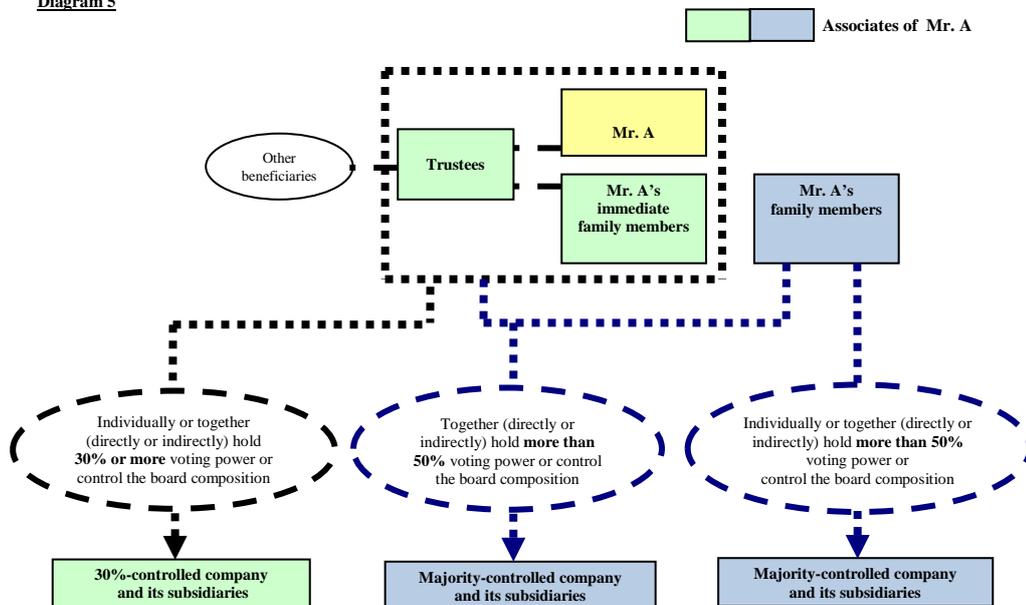
- (2) (a) a person cohabiting with him as a spouse, or his child, step-child, parent, step-parent, brother, step-brother, sister or step-sister (each a “family member”); or

**Diagram 4**



- (b) a majority-controlled company held, directly or indirectly, by the family members (individually or together), or held by the family members together with the individual, his immediate family members and/or the trustees, or any of its subsidiaries.

**Diagram 5**



14A.11(4)(b)(ii),  
14A.11(4) – N3

LD76-5,  
FAQ Series 10  
No. 12

14A.10 An “associate” of a connected person described in rule 14A.05(1), (2) or (3) which is a company includes:

1.01 - (b)(i),  
19A.04 - (b)(i)

(1) its subsidiary or holding company, or a fellow subsidiary of the holding company (together the “group companies”);

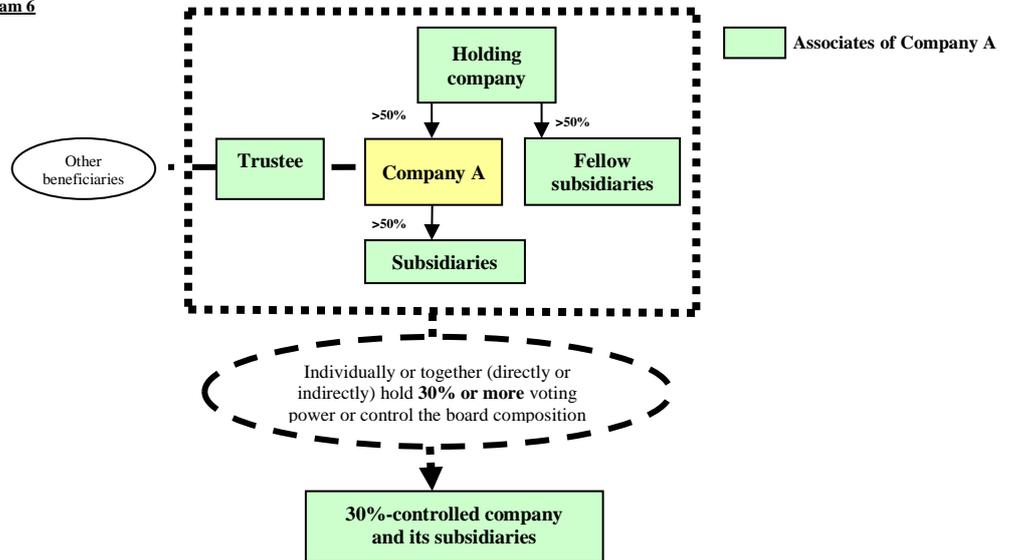
1.01 - (b)(ii),  
19A.04 - (b)(ii)

(2) the trustees, acting in their capacity as trustees of any trust of which the company is a beneficiary or, in the case of a discretionary trust, is (to its knowledge) a discretionary object (the “trustees”); or

1.01 - (b)(iv),  
19A.04 - (b)(iv)

(3) a 30%-controlled company held, directly or indirectly, by the company, the group companies, and/or the trustees (individually or together), or any subsidiary of that 30%-controlled company.

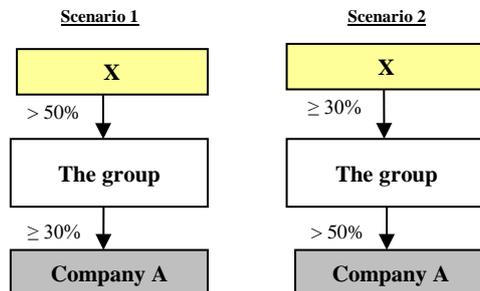
**Diagram 6**



14A.11(4) – NI  
LD100-1

14A.11 A company will not be regarded as a person’s associate only because the person holds an interest in the company through his/its shareholding in the group.

**Diagram 7**



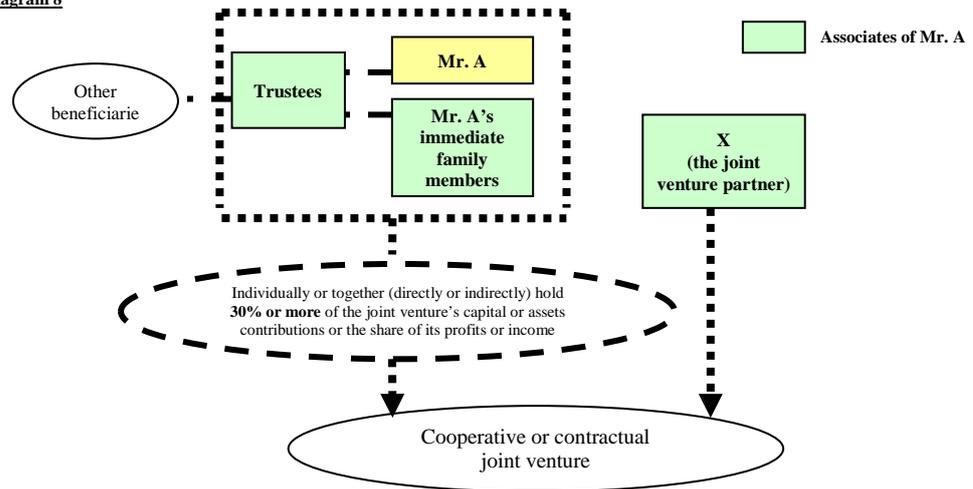
• Company A is not an associate of X because X only has an indirect interest in it through the group

For PRC issuers only, a person's associates include any joint venture partner of a cooperative or contractual joint venture (whether or not it is a separate legal entity) where:

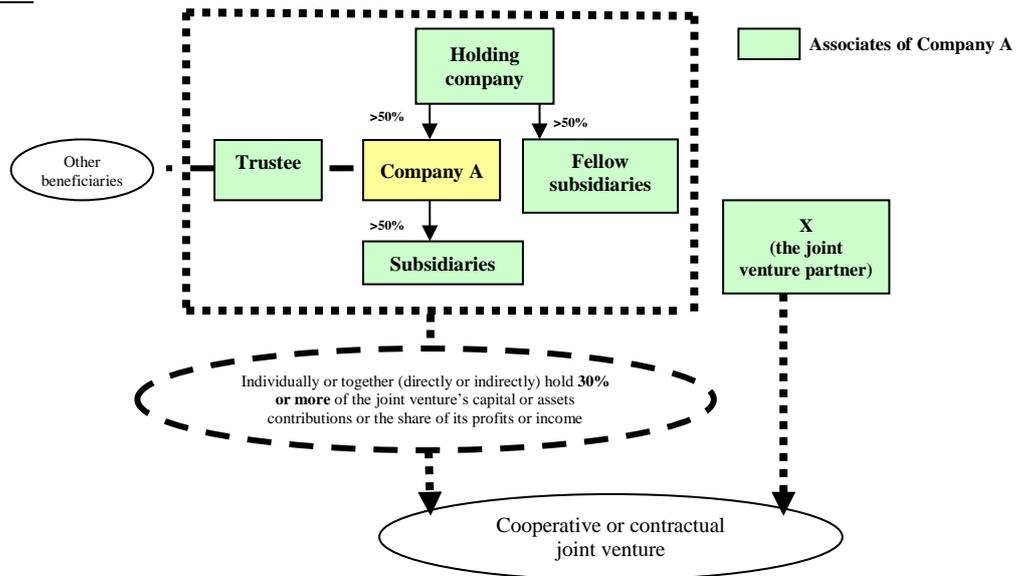
- (1) the person (being an individual), his immediate family members and/or the trustees; or
- (2) the person (being a company), its group companies and/or the trustees,

together directly or indirectly hold 30% (or an amount that would trigger a mandatory general offer or establish legal or management control over a business enterprise under the PRC law) or more in the joint venture's capital or assets contributions, or the contractual share of its profits or other income.

**Diagram 8**



**Diagram 9**



## Definition of connected subsidiary

14A.13 A “connected subsidiary” is:

14A.11(5)

(1) a non wholly-owned subsidiary of the issuer where any connected person(s) at the issuer level, individually or together, can exercise or control the exercise of 10% or more of the voting power at the subsidiary’s general meeting. This 10% excludes any indirect interest in the subsidiary which is held by the connected person(s) through the issuer; or

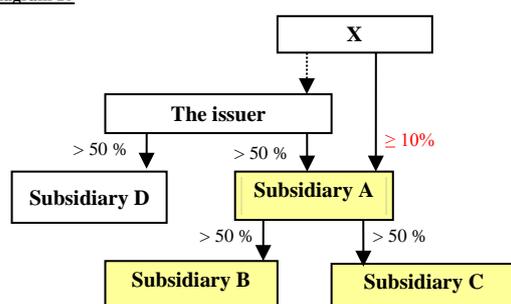
14A.11(6)

(2) any subsidiary of a non wholly-owned subsidiary referred to in (1) above.

14A.31(1A)

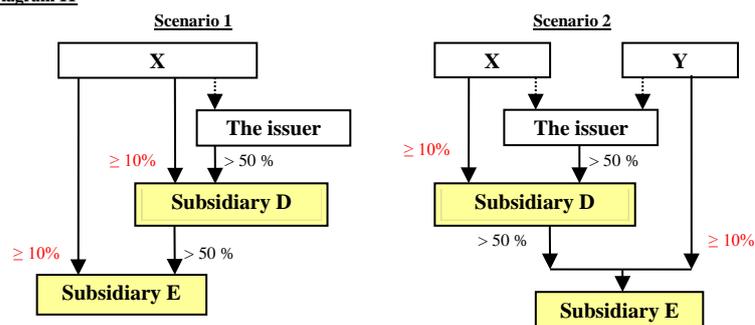
14A.14 If an issuer’s subsidiaries are connected persons only because they are the subsidiaries of a connected subsidiary, transactions between these subsidiaries will not be treated as connected transactions.

**Diagram 10**



- X is a connected person at the issuer level, and he/it has a 10% (or more) shareholding in Subsidiary A.  
→ Subsidiary A is a connected subsidiary. (See rule 14A.13(1))
- Subsidiaries B and C are subsidiaries of Subsidiary A.  
→ Subsidiaries B and C are also connected subsidiaries. (See rule 14A.13(2))
- Transactions between the issuer/Subsidiary D with Subsidiary A/B/C are connected transactions.
- Transactions between any of Subsidiaries A, B and C are not connected transactions if Subsidiaries B and C are connected solely because of their relationship with Subsidiary A. (See rule 14A.14)

**Diagram 11**



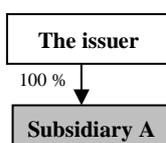
- X and Y are connected persons at the issuer level.  
→ Subsidiaries D and E are connected subsidiaries.
- Subsidiary E is a subsidiary of Subsidiary D. However, the exemption in rule 14A.14 does not apply to transactions between them because Subsidiary E is a connected subsidiary not only because of its relationship with Subsidiary D but also its relationship with X or Y.

14A.15 A subsidiary of the issuer is not a connected person if:

14A.12

(1) it is wholly-owned by the issuer; or

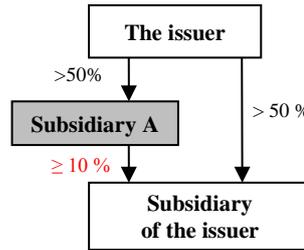
**Diagram 12**



14A.12A

- (2) it falls under the definition of connected person only because it is:
- (a) a substantial shareholder of another subsidiary of the issuer; or

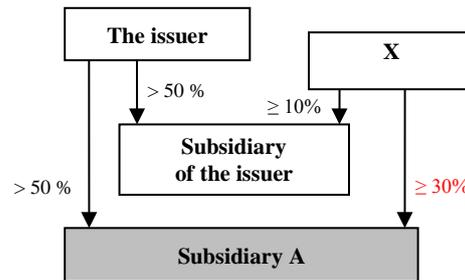
Diagram 13



- Subsidiary A is a substantial shareholder of another subsidiary of the issuer. However, this relationship will not make Subsidiary A a connected person of the issuer.

- (b) an associate of a director (or a person who was in past 12 months a director), a chief executive, a substantial shareholder or a supervisor of any subsidiary of the issuer.

Diagram 14



- X is a substantial shareholder of a subsidiary of the issuer.
- X holds 30% (or more) shareholding in Subsidiary A.
- Subsidiary A is an associate of X. However, this relationship will not make Subsidiary A a connected person of the issuer because X is only a connected person at the subsidiary level.

### Deemed connected persons

14A.06

14A.16 The Exchange has the power to deem any person to be an issuer's connected person.

14A.11(4)(a)

14A.17 A deemed connected person of an issuer includes a person:

- (1) who has entered, or proposes to enter, into:
- (a) a transaction with the group; and
- (b) an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with a connected person described in rule 14A.05(1), (2) or (3) with respect to the transaction; and
- (2) who, in the Exchange's opinion, should be considered as a connected person.

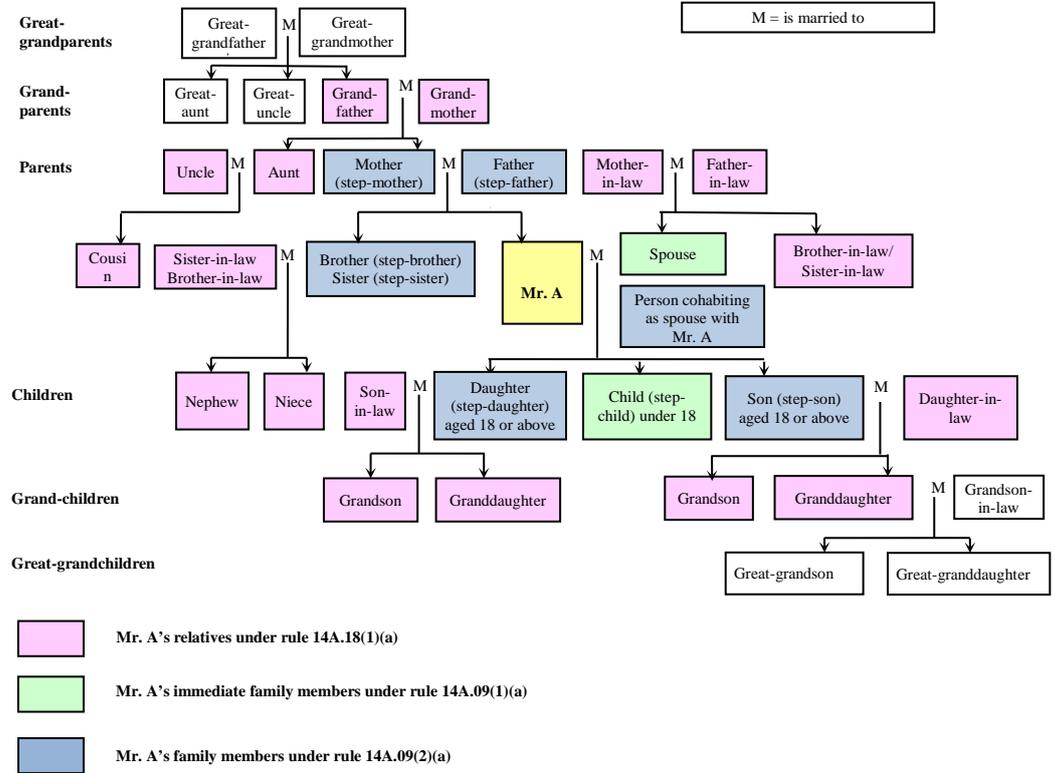
14A.18 A deemed connected person also includes a person:

(1) who is:

14A.11(4)(c)(i)

(a) a father in-law, mother-in-law, son-in-law, daughter-in-law, brother-in-law, sister-in-law, grandparent, grandchild, uncle, aunt, cousin, nephew or niece (each a “relative”) of a connected person as described in rule 14A.05(1), (2) or (3); or

Diagram 15

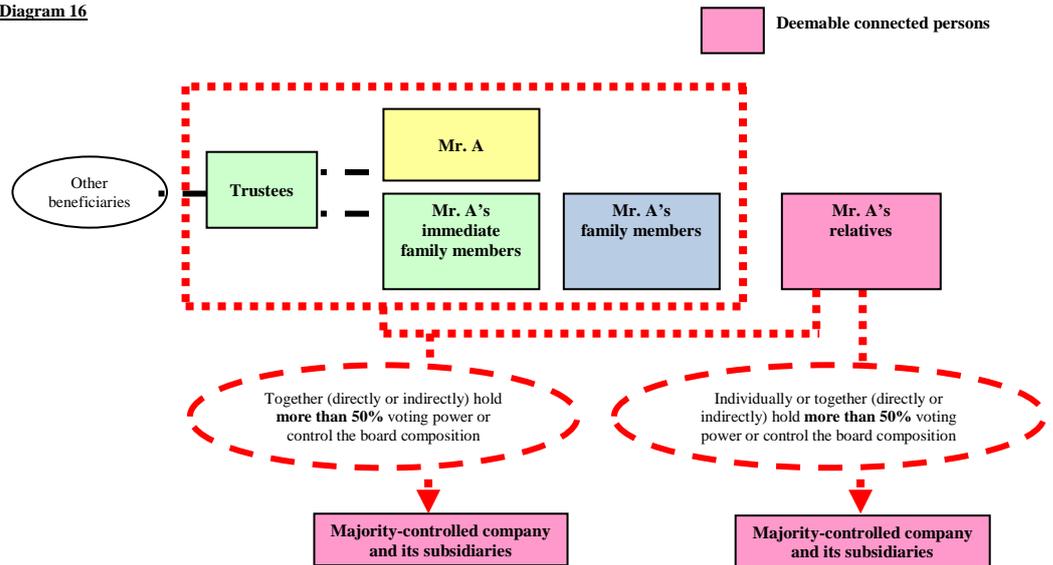


14A.11(4)(c)(ii),  
14A.11(4) – N3

LD76-5,  
FAQ Series 10  
No. 13

(b) a majority-controlled company held, directly or indirectly, by the relatives (individually or together) or held by the relatives together with the connected person as described in rule 14A.05(1), (2) or (3), the trustees, his immediate family members and/or family members, or any subsidiary of that majority-controlled company; and

Diagram 16



- (2) whose association with the connected person is such that, in the Exchange's opinion, the proposed transaction should be subject to the connected transaction requirements.

14A.11(4)(c)

14A.19 The issuer must inform the Exchange of any proposed transaction with the person unless it is exempt from all of the connected transaction requirements. It must provide information to the Exchange to demonstrate whether or not the transaction should be subject to connected transaction requirements.

### WHAT ARE CONNECTED TRANSACTIONS

14A.20 Connected transactions include transactions with connected persons, and transactions with third parties that may confer benefits to connected persons through their interests in the entities involved in the transactions.

14A.10(13)

14A.21 "Transactions" include both capital and revenue nature transactions, whether or not conducted in the group's ordinary and usual course of business. This includes the following types of transactions:

- (1) any buying or selling of assets by a group including a deemed disposal;
- (2) (a) a group granting, accepting, exercising, transferring or terminating an option to buy or sell assets or to subscribe for securities; or

14A.10(13)(b),  
14A.68

*Note: Terminating an option is not a transaction if it is made under the terms of the original agreement and does not involve payment of any penalty, damages or other compensation by the group.*

- (b) a group deciding not to exercise an option to buy or sell assets or to subscribe for securities;
- (3) entering into or terminating finance leases or operating leases;

- (4) providing or receiving financial assistance. "Financial assistance" includes granting credit, lending money, or providing an indemnity against obligations under a loan, or guaranteeing or providing security for a loan;
- (5) entering into an agreement or arrangement to set up a joint venture in any form (e.g. a partnership or a company), or any other form of joint arrangement;
- (6) issuing new securities of the issuer or its subsidiaries;
- (7) providing, receiving or sharing services; or
- (8) buying or selling raw materials, intermediate products and/or finished goods.

### Transactions with connected persons

14A.13(1)(a),  
14A.13(2)(a)(i),  
14A.13(2)(b)(i)

14A.22 Any transaction between a group and a connected person is a connected transaction.

### Financial assistance to/from commonly held entities

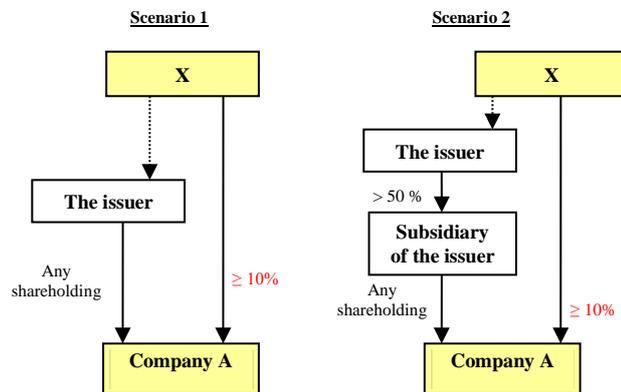
14A.13(2)(a)(ii),  
14A.13(2)(b)(ii),  
14A.13(3), (4)

14A.23 Financial assistance provided by a group to, or received by a group from, a commonly held entity is a connected transaction.

14A.24 A "commonly held entity" is a company whose shareholders include:

- (1) a member of the group; and
- (2) any connected person(s) at the issuer level who, individually or together, can exercise or control the exercise of 10% or more of the voting power at the company's general meeting. This 10% excludes any indirect interest held by the person(s) through the issuer.

Diagram 17



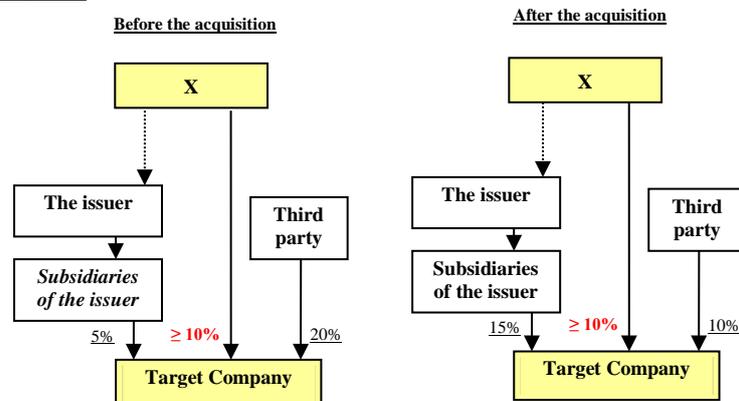
- X is a connected person at the issuer level
- Both the group and X are shareholders of Company A, and X holds 10% (or more) of shareholding in Company A.
  - Company A is a commonly held entity.
  - Financial assistance provided by the group to, or received by the group from, Company A is a connected transaction.

## Transactions with third parties

14A.13(1)(b)(i) 14A.25 A group buying or selling an interest in a company (the “target company”) from or to a person who is not a connected person is a connected transaction if the target company’s substantial shareholder:

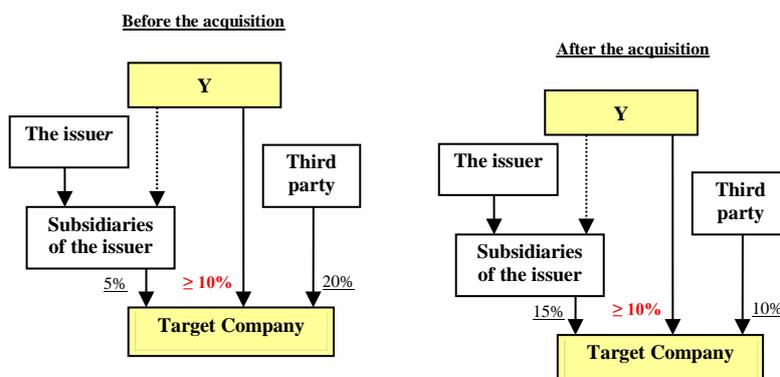
- (1) is, or is proposed to be, a controller. A “controller” is a director, chief executive or controlling shareholder of the issuer or any of its subsidiaries; or
- (2) is, or will, as a result of the transaction, become, an associate of a controller or proposed controller.

**Diagram 18**



- X is a (proposed) controller of the issuer.
- X is a substantial shareholder of the Target Company.
- The group’s acquisition of an interest in the Target Company from the third party is a connected transaction.
- The group’s disposal of an interest in the Target Company to the third party or any other third party is also a connected transaction.

**Diagram 19**



- Y is a (proposed) controller of the issuer’s subsidiary or subsidiaries
- Y is a substantial shareholder of the Target Company.
- The group’s acquisition of an interest in the Target Company from the third party is a connected transaction.
- The group’s disposal of an interest in the Target Company to the third party or any other third party is also a connected transaction.

14A.13(1)(b)(i) 14A.26 The Exchange may aggregate the interests of the controller and his/its associates in the target company to decide whether they together are the target company’s substantial shareholder.

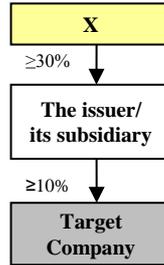
14A.13(1)(b)(i) 14A.27 Buying or selling the target company’s assets is also a connected transaction if these assets account for 90% or more of the target company’s net assets or total assets.

14A.28 Rule 14A.25 or 14A.27 does not apply to an issuer's proposed acquisition or disposal if:

14A.13(1)(b)(i)  
- N1, N2

- (1) the controller or his/its associate(s) is/are together the target company's substantial shareholders only because of their indirect shareholdings in the target company held through the group; or

**Diagram 20**

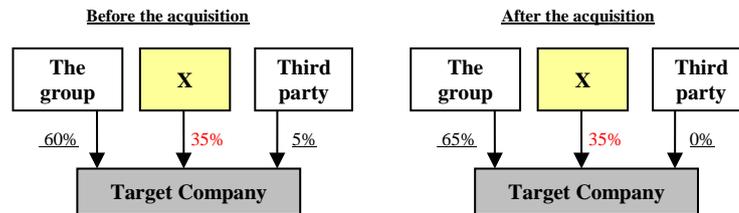


- X is a controller of the issuer or its subsidiary or subsidiaries.
  - X only has an indirect interest in the Target Company through the group.
- The group's acquisition or disposal of an interest in the Target Company from or to any third party (who is not a connected person) is not a connected transaction.

14A.13(1)(b)(i)  
- N3, N4

- (2) (a) the target company is, or will be, a subsidiary of the issuer;
- (b) the target company's substantial shareholder is a controller or proposed controller only because of his/its relationship with the target company; and
- (c) the substantial shareholder's interest in the target company does not increase (in the case of an acquisition) or change (in the case of a disposal) as a result of the proposed transaction or any related arrangement.

**Diagram 21**



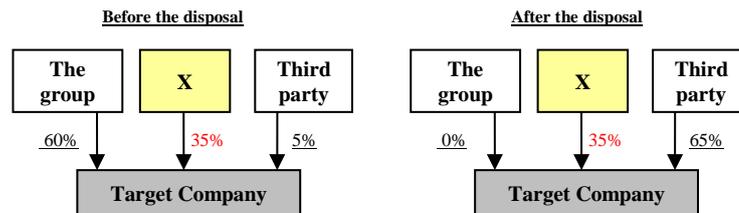
- The Target Company is a subsidiary of the issuer.
  - X is a substantial shareholder of the Target Company.
  - X is a controller of the group only because he is a controlling shareholder and/or director of the Target Company.
  - There is no change in X's interest in the Target Company as a result of the transaction.
- The group's acquisition of an interest in the Target Company from the third party (who is not a connected person) is not a connected transaction.

**Diagram 22**



- The Target Company will become a subsidiary of the issuer after the acquisition.
  - X is a substantial shareholder of the Target Company.
  - X will be a controller of the group only because he is, and will remain, a controlling shareholder and/or director of the Target Company.
  - There is no change in X's interest in the Target Company as a result of the transaction.
- The group's acquisition of an interest in the Target Company from the third party (who is not a connected person) is not a connected transaction.

**Diagram 23**



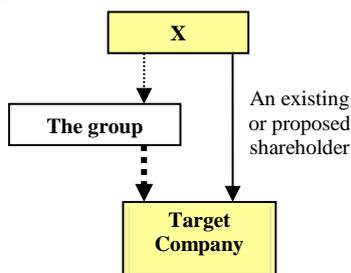
- The Target Company is a subsidiary of the issuer.
  - X is a substantial shareholder of the Target Company.
  - X is a controller of the group only because he is a controlling shareholder and/or director of the Target Company.
  - There is no change in X's interest in the Target Company as a result of the transaction.
- The group's disposal of an interest in the Target Company to the third party (who is not a connected person) is not a connected transaction.

14A.29 A transaction between a group and a person who is not a connected person is a connected transaction if it involves:

14A.13(1)(b)(ii)

- (1) the group acquiring an interest in a company (or an option to acquire such interest) of which the controller (or his/its associate) is, or will become, a shareholder, and the interest is:
  - (a) of a fixed income nature;
  - (b) shares to be acquired on less favourable terms than those granted to the controller or the associate;
  - (c) shares which are of a different class from those held or to be granted to the controller or the associate; or

**Diagram 24**

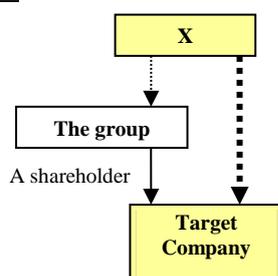


- X is a controller of the issuer or its subsidiary or subsidiaries.
  - X is, or will become, a shareholder of the Target Company.
  - The group proposes to acquire an interest in the Target Company which is (i) of a fixed income nature, (ii) on terms less favourable than those available to X; or (iii) shares of a different class from those held or to be acquired by X.
- The group's acquisition of the interest in the Target Company is a connected transaction.

14A.13(1)(b)(iii), (iv)

- (2) the controller (or his/its associate) subscribing for shares in a company of which the group is a shareholder, and
- the shares being subscribed are of a different class from those held by the group; or
  - the shares are to be subscribed on specially favourable terms to the controller (or his/its associate).

**Diagram 25**



- X is a controller of the issuer or its subsidiary or subsidiaries
  - The group is a shareholder of the Target Company.
  - The group enters into a transaction with a third party which involves X subscribing for shares in the Target Company which are (i) of a different class from those held by the group; or (ii) to be subscribed on specially favourable terms to X
- The group's transaction with the third party is a connected transaction.

14A.13(1)(b)(ii), (iii), (iv) – N

14A.30 Rule 14A.29 does not apply if the group and the controller (or his/its associate) acquire or subscribe for shares in a company where the terms of the acquisition or subscription have been approved by shareholders under this Chapter.

**Definition of continuing connected transaction**

14A.14

14A.31 Continuing connected transactions are connected transactions involving the provision of goods or services or financial assistance, which are carried out on a continuing or recurring basis and are expected to extend over a period of time. They are usually transactions in the group's ordinary and usual course of business.

**REQUIREMENTS FOR CONNECTED TRANSACTIONS**

14A.16, 14A.17

14A.32 This section sets out the requirements for connected transactions.

14A.33 Exemptions or waivers from all or some of the requirements are available for certain type of connected transactions. See rules 14A.74 to 14A.110.

**Written agreement**

14A.04, 14A.35(1)

14A.34 The group must enter into a written agreement for a connected transaction.

## Announcement

14A.47(2),  
14A.56

14A.35 The issuer must announce the connected transaction as soon as practicable after its terms have been agreed. See rule 14A.70 for the content requirements.

*Note: If the connected transaction is subsequently terminated or there is any material variation of its terms or material delay in the completion, the issuer must announce this fact as soon as practicable.*

## Shareholders' approval

14A.18,  
14A.35(4),  
14A.52,  
14A.54

14A.36 The connected transaction must be conditional on shareholders' approval at a general meeting held by the issuer. Any shareholder who has a material interest in the transaction must abstain from voting on the resolution.

14A.43,  
14A.53

14A.37 The Exchange may waive the general meeting requirement and accept a written shareholders' approval, subject to the conditions that:

- (1) no shareholder of the issuer is required to abstain from voting if a general meeting is held to approve the transaction; and
- (2) the approval is given by a shareholder or a closely allied group of shareholders who (together) hold more than 50% of the voting rights in the general meeting.

14A.43 - N2

14A.38 If the issuer discloses inside information to any shareholder in confidence to solicit the written approval, it must ensure that the shareholder is aware that he must not deal in the securities before the information has been made available to the public.

14A.21

14A.39 If the connected transaction requires shareholders' approval, the issuer must (1) set up an independent board committee; and (2) appoint an independent financial adviser.

## Independent board committee

14A.21,  
13.39(6), (7)

14A.40 The independent board committee must, taking into account the recommendation of an independent financial adviser, advise the issuer's shareholders:

- (1) whether the terms of the connected transaction are fair and reasonable;
- (2) whether the connected transaction is in the interests of the issuer and its shareholders as a whole; and
- (3) how to vote on the connected transaction.

13.39(6)(c)

14A.41 The independent board committee should consist only of independent non-executive directors who do not have a material interest in the transaction.

13.39(6)(c),  
14A.58 - N

14A.42 If all the independent non-executive directors have a material interest in the transaction, an independent board committee will not be formed. The independent financial adviser must then make its recommendation to the shareholders directly.

14A.58(3)(c),  
13.39(7)(a)

14A.43 If an independent board committee is formed, the circular should include a letter from the independent board committee containing its opinion and recommendation.

*Independent financial adviser*

13.39(6)(b),  
14A.21,  
14A.23

14A.44 The issuer must appoint an independent financial adviser acceptable to the Exchange to make recommendations to the independent board committee and shareholders on the matters in rules 14A.45(1) to (4). The independent financial adviser will give its opinion based on the written agreement for the transaction.

14A.22,  
14A.58(3)(d),  
13.39(6)(b), (7)(b)

14A.45 The circular should include a letter from the independent financial adviser containing its opinion and recommendation. The independent financial adviser's letter must also set out the reasons for its opinion, the key assumptions made, the factors that it has taken into consideration in forming the opinion, and a statement whether:

- (1) the terms of the connected transaction are fair and reasonable;
- (2) the connected transaction is on normal commercial terms and in the group's ordinary and usual course of business;
- (3) the connected transaction is in the interests of the issuer and its shareholders as a whole; and
- (4) the independent shareholders should vote in favour of the connected transaction.

**Circular**

14A.49

14A.46 The issuer must send a circular to its shareholders:

- (1) at the same time as or before the issuer gives notice of the general meeting if the connected transaction is to be approved by shareholders in a general meeting; or
- (2) within 15 business days after publication of the announcement in any other cases. The issuer may apply for a waiver from this requirement if it requires additional time to prepare the circular.

*Note: See rules 14A.70 and 14A.71 for the content requirements.*

14A.49,  
14A.58,  
14A.59  
14A.56(10)

14A.47 The issuer must announce the expected date of distribution of the circular, and if this is more than 15 business days after the publication of the announcement, the reasons why this is so.

14A.47A

14A.48 If the issuer expects a delay in distribution of the circular by the date previously announced, it must announce this fact, the reason for the delay and the new expected date of distribution of the circular before the original despatch date.

*Supplementary circular or announcement*

14A.49

14A.49 If the issuer is aware of any material information relating to the connected transaction after it has issued the circular, it must publish this information in a supplementary circular or announcement at least 10 business days before the date of the general meeting to consider the transaction. The meeting must be adjourned by the chairman or, if that is not permitted by the issuer's constitutional documents, by resolution to that effect if it is necessary for the compliance with the 10 business day requirement. (See rule 13.73 for the factors that the issuer should consider when deciding whether to issue a supplementary circular or announcement.)

## Annual reporting

- 14A.35(3),  
14A.45,  
14A.46
- 14A.50 The issuer must disclose its connected transactions conducted during the financial year in its annual report. See rules 14A.72 and 14A.73 for the content requirements.

### Requirements for continuing connected transactions

- 14A.51 The following additional requirements apply to a continuing connected transaction.

#### *Terms of an agreement*

- 14A.35(1)
- 14A.52 A written agreement for a continuing connected transaction must contain the basis for calculating the payments to be made. Examples include sharing of costs incurred by the parties, unit prices for goods or services provided, annual rental for leasing a property, or management fees based on a percentage of the total construction cost.

- 14A.35(1)
- LD88-1,  
FAQ Series 7  
No.49 and 50
- 14A.53 The period for the agreement must be fixed and reflect normal commercial terms. It must not exceed 3 years except in special circumstances where the nature of the transaction requires a longer period. In this case, the issuer must appoint an independent financial adviser to explain why the agreement requires a longer period and to confirm that it is normal business practice for agreements of this type to be of such duration.

#### *Annual cap*

- 14A.35(2)
- LD88-1
- 14A.35(2)
- 14A.52
- 14A.54 The issuer must set an annual cap (the “cap”) for the continuing connected transaction. The cap must be:
- (1) expressed in monetary terms;
  - (2) determined by reference to previous transactions and figures in the group’s published information. If there were no previous transactions, the cap must be set based on reasonable assumptions; and
  - (3) approved by shareholders if the transaction requires shareholders’ approval.

#### *Changes to annual cap or terms of agreement*

- 14A.36
- FAQ Series 7  
No. 52
- 14A.55 The issuer must re-comply with the announcement and shareholders’ approval requirements before:
- (1) the cap is exceeded; or
  - (2) it proposes to renew the agreement or to effect a material change to its terms.

*Note: The revised or new cap(s) will be used to calculate the percentage ratios for classifying the continuing connected transaction.*

*Annual review by independent non-executive directors and auditors*

- 14A.37      14A.56      The issuer's independent non-executive directors must review the continuing connected transactions every year and confirm in the annual report whether the transactions have been entered into:
- (1)      in the group's ordinary and usual course of business;
  - (2)      on normal commercial terms; and
  - (3)      according to the agreement governing them on terms that are fair and reasonable and in the interests of the issuer's shareholders as a whole.
- 14A.38      14A.57      The auditors must provide a letter to the issuer's board of directors confirming whether the continuing connected transactions:
- (1)      have been approved by the issuer's board of directors;
  - (2)      are in compliance with the group's pricing policies if the transactions involve provision of goods or services by the group;
  - (3)      are in accordance with the agreement governing the transactions; and
  - (4)      have not exceeded the cap.
- Note: A confirmation provided by the auditors according to Practice Note 740 issued by the Hong Kong Institute of Certified Public Accountants is acceptable under this rule.*
- 14A.38      14A.58      The issuer must provide a copy of the auditors' letter to the Exchange at least 10 business days before the bulk printing of its annual report.
- 14A.39      14A.59      The issuer must allow, and ensure that the counterparties to the continuing connected transactions allow, the auditors sufficient access to their records for the purpose of reporting on the transactions.
- 14A.40      14A.60      The issuer must promptly notify the Exchange and publish an announcement if the independent non-executive directors and/or the auditors cannot confirm the matters as required. The Exchange may require the issuer to re-comply with the announcement and shareholders' approval requirements and may impose additional conditions.

*When a continuing transaction subsequently becomes connected*

- 14A.61 If the group has entered into an agreement with fixed terms for:
- 14A.41 (1) a continuing transaction, and the transaction subsequently becomes a continuing connected transaction, or
  - 14A.33 – N2 (2) a continuing connected transaction exempt under the “insignificant subsidiary exemption” (see rules 14A.98 to 14A.101) or the “passive investor exemption” (see rules 14A.102 and 14A.103), and the transaction subsequently cannot meet the conditions for the exemption,
- the issuer must:
- (a) as soon as practicable after becoming aware of this fact, comply with the annual review and disclosure requirements including publishing an announcement and annual reporting if the group continues to conduct the transaction under the agreement; and
  - (b) when the agreement is renewed or its terms are varied, comply with all connected transaction requirements.

**Other requirements relating to connected transactions**

*Options*

- 14A.62 If the group grants an option to a connected person and the group does not have discretion to exercise the option, the transaction is classified as if the option has been exercised (see rule 14A.80(1)). In addition, the issuer must announce the following subsequent events as soon as practicable:
- 14A.69(2), (3)(c) (1) any exercise or transfer of the option by the option holder; and/or
  - 14A.69(3)(a), (b) (2) (if the option is not exercised in full), the option holder notifying the group that it will not exercise the option, or the expiry of the option, whichever is earlier.

*Guaranteed profits or net tangible assets*

- 14A.57, 14A.59(10) 14A.63 The following apply if the group acquires a company or business from a connected person, and the connected person guarantees the profits or net tangible assets or other matters regarding the financial performance of the company or business.
- 14A.57, 14A.59(10) 14A.64 If the actual amount is less than the amount guaranteed, the issuer must disclose the following in an announcement and in its next annual report:
- (1) the shortfall and any adjustment in the consideration for the transaction;
  - (2) whether the connected person has fulfilled its obligations under the guarantee;
  - (3) whether the group has exercised any option to sell the company or business back to the connected person or other rights it held under the terms of the guarantee, and the reasons for its decision; and

- (4) the independent non-executive directors' opinion:
  - (a) whether the connected person has fulfilled its obligations; and
  - (b) whether the group's decision to exercise or not to exercise any options or rights set out in rule 14A.64(3) is fair and reasonable and in the interests of the shareholders as a whole.

*When a proposed transaction becomes connected*

- 14A.61,  
14A.62
- 14A.65 If a connected transaction is also a notifiable transaction, the issuer must also comply with the requirements in Chapter 14.
- 14A.66 If an issuer has entered into an agreement for a proposed transaction which is conditional on shareholders' approval in general meeting and the proposed transaction becomes a connected transaction before the shareholders' approval, the issuer must comply with the connected transaction requirements. Where a notice of meeting to approve the proposed transaction has been sent to shareholders, the issuer must issue a further announcement and a supplementary circular to disclose that the transaction has become a connected transaction and the parties that are required to abstain from voting. The circular must also contain information required for a connected transaction circular.

*Checklists*

- 14A.09
- 14A.67 The issuer must complete and submit any checklists for connected transactions prescribed by the Exchange from time to time.

**CONTENT REQUIREMENTS**

- 14A.68 This section sets out the information that an issuer must disclose in its announcements, circulars and annual reports.

**Announcements**

- 14A.69 An announcement for a connected transaction must contain at least:
- 14A.56(1) (1) the information set out in rules 14.58 to 14.60 (contents of announcements for notifiable transactions);
- 14A.56(2) (2) the connected relationship between the parties to the transaction, and the connected person's interests in the transaction;
- 14A.56(1) (3) the independent non-executive directors' views on the transaction if no shareholders' approval is required. This includes whether the transaction is on normal commercial terms, whether its terms are fair and reasonable, and whether it is in the interests of the issuer and its shareholders as a whole;
- 14A.56(4) (4) if the transaction is a continuing connected transaction, the amount of its cap. If a circular is not required, the issuer should also disclose how it determines and calculates the cap, including the assumptions and the amounts of previous transactions which form the basis of the cap;

- 14A.73(2) (5) if the transaction is a qualified property acquisition exempt from the shareholders' approval requirement (see rule 14A.104):
- (a) the details of the acquisition;
  - (b) the details of the joint venture, including its terms and status, its dividend and distribution policy, its financial and capital commitment, and the issuer's share in it; and
  - (c) information to demonstrate that the exemption conditions have been met;
- 14A.56(5) (6) if the transaction involves the group acquiring assets from a connected person, the original acquisition cost of the assets to the connected person;
- 14A.56(6) (7) if the transaction involves the group disposing of assets which it has held for 12 months or less, the group's original acquisition cost of the assets;
- 14A.56(8) (8) if the announcement contains a profit forecast of the group or a company which is, or will become, the issuer's subsidiary, the information set out in rule 14.62 (requirements for profit forecast in notifiable transaction announcement);
- 14A.56(9) (9) if no circular is required, a statement whether any directors of the issuer have a material interest in the transaction and, if so, whether they have abstained from voting on the board resolution;
- 14A.56(3) (10) a statement that the transaction is subject to independent shareholders' approval, if applicable;
- 14A.56(7) (11) if the transaction is, or will be, approved by way of shareholders' written approval, details of the shareholders giving the approval (including their names and shareholdings in the issuer) and the relationship between the shareholders; and
- 14A.56(10) (12) if a circular is required, the expected date of distribution of the circular, and, if this is more than 15 business days after the publication of the announcement, the reasons why this is so.

### Circulars

14A.70 A circular for a connected transaction must:

- 14A.58(1) (1) provide a clear and adequate explanation of its subject matter and demonstrate the advantages and disadvantages of the transaction for the group;
- 14A.58(2) (2) where practicable, include a numerical evaluation;
- 14A.58(3)(a) (3) contain all information necessary to allow the issuer's shareholders to make a properly informed decision; and
- 14A.58(3)(b) (4) contain a heading drawing attention to the importance of the document and advising shareholders who are in any doubt to consult appropriate independent advisers on the appropriate course of action.

14A.71 The circular must contain at least:

- 14A.59(1) (1) the Exchange's disclaimer statement (see rule 14.88) on its front cover or inside front cover;
- 14A.59(2)(a), (b), (c), (f), (13) to (16) (2) the information required to be disclosed in the announcement for the transaction;
- 14A.59(2)(a) (3) the identity and activities of the parties to the transaction and their ultimate beneficial owner(s);
- 14A.59(2)(d), (e) (4) the name of the connected person concerned, his/its relationship with any controller and the name and office held by that controller;
- 14A.59(9)  
FAQ Series 9 No. 21 (5) if the transaction is a continuing connected transaction, how the issuer determines and calculates the cap, including the assumptions and the amounts of previous transactions which form the basis of the cap;
- 14A.59(7), (8) (6) a letter from each of the independent financial adviser and, if applicable, the independent board committee containing its opinion and recommendation on the transaction (see rules 14A.43 and 14A.45);
- 14A.59(6), 14A.73(3)  
FAQ Series 7 No. 54 (7) if the transaction involves the acquisition or disposal of any property interests or a company whose assets consist solely or mainly of property, a valuation and information on the property if required under rule 5.03. This rule does not apply to property acquired under a qualified property acquisition;
- 14A.59(6)  
FAQ Series 7 No. 55 and 56 (8) if the primary significance of the asset (except for property interests) being acquired or disposed of is its capital value, an independent valuation of the asset;
- 14A.59(17) (9) if the transaction involves an acquisition or disposal of a company or business engaging in an infrastructure project, a business valuation report on that company or business and/or traffic study report on the project. The report(s) must clearly set out:
- (a) all significant underlying assumptions including the discount rate or growth rate used; and
- (b) a sensitivity analysis based on different discount rates and growth rates.
- If the business valuation is based on a profit forecast, the accounting policies and calculations for the underlying forecasts must be examined and reported on by the auditors or reporting accountants. Any financial adviser mentioned in the circular must also report on the underlying forecasts.
- 14A.59(10) (10) if the transaction involves the group acquiring a company or business from a connected person, details of:
- (a) any guarantee of the profits or net tangible assets or other matters regarding the financial performance of the company or business provided by the connected person, and a statement by the issuer that it will comply with the disclosure requirements (see rule 14A.64) if the actual amount is less than the amount guaranteed.

- (b) any option granted to the group to sell the company or business back to the connected person and/or other rights given to the group;
- 14A.59(18) (11) a statement whether any directors of the issuer have a material interest in the transaction and, if so, whether they have abstained from voting on the board resolution;
- 14A.59(5) (12) a statement that any shareholder with a material interest in the transaction will not vote and the information required in rule 2.17;
- 14A.59(3) (13) the information set out in the following paragraphs of Appendix 1, Part B:
- 1 — issuer's name
  - 2 — directors' responsibility
  - 5 — expert statements
  - 10 — securities to be issued (if applicable)
  - 29(2) — requirements if there is a profit forecast
  - 32 — no material adverse change
  - 39 — directors' service contracts
  - 40 — directors' interests in assets
  - 43(2)(a) & (c) — documents on display
- 14A.59(4) (14) information regarding directors' and chief executive's interests in the issuer described in paragraphs 34 and 38 of Appendix 1, Part B, and Practice Note 5;
- 14A.59(11) (15) information regarding the competing interests of each of the group's directors and his associates as would be required to be disclosed under rule 8.10 as if each of them was a controlling shareholder; and
- 14A.59(19) (16) any additional information requested by the Exchange.

### Annual reports

- 14A.45, 14A.46 14A.72 The issuer's annual report must contain the following information on the connected transactions conducted in that financial year (including continuing connected transactions under agreements signed in previous years):
- (1) the transaction date;
  - (2) the parties to the transaction and a description of their connected relationship;
  - (3) a brief description of the transaction and its purpose;
  - (4) the total consideration and terms;
  - (5) the nature of the connected person's interest in the transaction;
  - (6) for continuing connected transactions,
    - (a) a confirmation from the issuer's independent non-executive directors on the matters set out in rule 14A.56; and
    - (b) a statement from the issuer's board of directors whether the auditors have confirmed the matters set out in rule 14A.57.
- 14A.37, 14A.38

- 14A.73 When the issuer discloses in its annual report information of any related party transaction under the accounting standards for preparing its financial statements, it must specify whether the transaction is a connected transaction under this Chapter and whether it has complied with the requirements in this Chapter.

### EXEMPTIONS

- 14A.74 Exemptions from the connected transaction requirements are available for the following types of transactions:

- (1) de minimis transactions (rule 14A.77);
- (2) financial assistance (rules 14A.88 to 14A.91);
- (3) issues of new securities by the issuer or its subsidiary (rule 14A.92);
- (4) dealings in securities on stock exchanges (rule 14A.93);
- (5) repurchases of securities by the issuer or its subsidiary (rule 14A.94);
- (6) directors' service contracts (rule 14A.95);
- (7) buying or selling of consumer goods or services (rules 14A.96);
- (8) sharing of administrative services (rule 14A.97) ;
- (9) transactions with persons connected with insignificant subsidiaries (rules 14A.98 to 14A.101);
- (10) transactions with associates of passive investors (rules 14A.102 and 14A.103); and
- (11) qualified property acquisitions (rules 14A.104 to 14A.106).

- 14A.75 The exemptions are broadly divided into two categories: (1) fully exempt from shareholders' approval, annual review and all disclosure requirements; and (2) exempt from shareholders' approval requirement.

- 14A.76 The Exchange has the power to specify that an exemption will not apply to a particular transaction.

### De minimis transactions

- 14A.77 This exemption applies to a connected transaction (other than an issue of new securities by the issuer) conducted on normal commercial terms.

- (1) The transaction is fully exempt if all the percentage ratios (other than the profits ratio) are:
  - (a) less than 0.1%;
  - (b) less than 1% and the transaction is a connected transaction only because it involves connected person(s) at the subsidiary level;  
or

(c) less than 5% and the total consideration (or in the case of any financial assistance, the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity) is less than HK\$1,000,000.

14A.32,  
14A.34,  
14A.66(2)

(2) The transaction is exempt from circular (including independent financial advice) and shareholders' approval requirements if all the percentage ratios (other than the profits ratio) are:

(a) less than 5%; or

(b) less than 25% and the total consideration (or in the case of any financial assistance, the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity) is less than HK\$10,000,000.

*Percentage ratio calculations*

14A.78 The methods of percentage ratio calculations set out in Chapter 14 (notifiable transactions) also apply to connected transactions in this Chapter subject to the modifications described rules 14A.79 to 14A.80.

14A.33(3)

14A.79 For continuing connected transactions, the issuer should calculate the assets ratio, revenue ratio and consideration ratio using the annual cap as the numerator. If the agreement for the transaction covers over 1 year, the transaction will be classified based on the largest annual cap during the term of the agreement.

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14A.68

14A.80 The following applies when calculating percentage ratios for connected transactions involving options:

14A.69(1)

(1) if the group grants an option to a connected person and the group does not have discretion to exercise the option, it is classified as if the option has been exercised. The percentage ratios are calculated based on the consideration for the transaction (which includes the premium and the exercise price of the option), the value of the underlying assets, and the revenue attributable to the assets (See rule 14A.62 for the disclosure requirement when the option holder exercises or transfers the option, or when the option expires);

14A.70(1)

(2) if the group acquires or accepts an option granted by a connected person where the group has discretion to exercise the option, it is classified based on the amount of the premium payable by the group. However, if the premium represents 10% or more of the sum of the premium and the exercise price, the transaction will be classified as if the option has been exercised (see rule 14A.80(1));

14A.70(2)

(3) if the group exercises an option granted by a connected person, it is classified based on the exercise price, the value of the underlying assets, and the revenue attributable to the assets. If the option is exercised in stages, the Exchange may require aggregation of the transactions;

14A.70(3)

(4) if the group transfers an option granted by a connected person to a third party or decides not to exercise the option, it is classified as if the option has been exercised. The percentage ratios are calculated based on the exercise price, the value of the underlying assets, and the revenue attributable to the assets, and (if applicable) the premium for transferring the option; and

14A.71

- (5) if the actual monetary value of the premium, the exercise price, the value of the underlying assets and the revenue attributable to the assets have not been determined when the group grants or acquires/accepts the option:
- (a) the issuer must demonstrate to the Exchange's satisfaction the highest possible monetary value for calculating the percentage ratios and classifying the transaction. If the issuer is unable to do so, it may be required to comply with all the connected transaction requirements for the transaction; and
  - (b) the issuer must inform the Exchange when the actual monetary value has been determined. If the transaction falls under a higher classification based on the actual monetary value, the issuer must as soon as reasonably practicable announce this fact and comply with the requirements applicable to the higher classification.

*Note: The requirements in this rule are the same as the requirements applicable to options under Chapter 14 (notifiable transactions), except that*

- 1. *Under Chapter 14, the issuer may, at the time of the group acquiring or accepting an option granted by a third party, seek shareholders' approval for its exercise of the option in the future. This is not allowed under this Chapter.*
- 2. *Under Chapter 14, transfer of an option by the group is a transaction which is classified based on the consideration for transferring the option. Under this Chapter, the transfer is classified as if the option is exercised.*
- 3. *Non-exercise of an option is not a transaction under Chapter 14.*

*Exception to percentage ratio calculations*

FAQ Series 7  
No. 45

- 14A.81 If any percentage ratio produces an anomalous result or is inappropriate to the activity of the issuer, the Exchange may disregard the ratio and consider alternative test(s) provided by the issuer. The issuer should seek prior consent of the Exchange if it wishes to apply this rule.

*Aggregation of transactions*

14A.25

- 14A.82 The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they were all entered into or completed within a 12-month period or are otherwise related. The issuer must comply with the applicable connected transaction requirements based on the classification of the connected transactions when aggregated. The aggregation period will cover 24 months if the connected transactions are a series of acquisitions of assets being aggregated which may constitute a reverse takeover.

14A.26

- 14A.83 Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:
- (1) they are entered into by the group with the same party, or parties who are connected with one another;
  - (2) they involve the acquisition or disposal of parts of one asset, or interests in a company or group of companies; or

- (3) they together lead to substantial involvement by the group in a new business activity.

14A.27 14A.84 The Exchange may aggregate all continuing connected transactions with a connected person.

14A.27A 14A.85 An issuer must consult the Exchange before the group enters into any connected transaction if:

- (1) the transaction and any other connected transactions entered into or completed by the group in the last 12 months fall under any of the circumstances described in rule 14A.83; or

- (2) the transaction and any other transactions entered into by the group involve the acquisition of assets from a person or group of persons or any of their associates within 24 months after the person(s) gain control (as defined in the Takeovers Code) of the issuer.

14A.86 The issuer must provide information to the Exchange on whether it should aggregate the transactions.

14A.87 The Exchange may aggregate an issuer's connected transactions even if the issuer has not consulted the Exchange.

### Financial assistance

#### *Financial assistance provided by the group*

LD76-1,  
FAQ Series 1  
No. 55

14A.88 For any financial assistance provided by a banking company in its ordinary and usual course of business to a connected person or commonly held entity:

- (1) the transaction is fully exempt if it is conducted on normal commercial terms (or better to the banking company);

- (2) the transaction is fully exempt if it is not conducted on normal commercial terms (or better to the banking company) but all the percentage ratios (other than the profits ratio) are:

- (a) less than 0.1%;
- (b) less than 1% and the transaction is a connected transaction only because it involves connected person(s) at the subsidiary level; or
- (c) less than 5% and the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity is less than HK\$1,000,000; or

14A.66(1) (3) the transaction is exempt from circular (including independent financial advice) and shareholders' approval requirements if it is not conducted on normal commercial terms (or better to the banking company) but all the percentage ratios (other than the profits ratio) are:

- (a) less than 5%; or

- (b) less than 25% and the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity is less than HK\$10,000,000.

14A.10(1) 14A.89 A “banking company” is an issuer or its subsidiary which is a bank, a restricted licence bank or a deposit taking company as defined in the Banking Ordinance, or a bank under an appropriate overseas authority.

14A.65(3) 14A.90 Financial assistance provided by a group to a connected person or commonly held entity is fully exempt if it is conducted:

- (1) on normal commercial terms (or better to the group); and
- (2) in proportion to the equity interest directly held by the issuer or its subsidiary in the connected person or the commonly held entity. Any guarantee given by the group must be on a several (and not a joint and several) basis.

14A.64

*Financial assistance received by the group*

14A.65(4) 14A.91 Financial assistance received by a group from a connected person or commonly held entity is fully exempt if:

- (1) it is conducted on normal commercial terms (or better to the group); and
- (2) it is not secured by the group’s assets.

**Issue of new securities by an issuer or its subsidiary**

14A.92 An issue of new securities by an issuer or its subsidiary to a connected person is fully exempt if:

14A.31(3)(a) (1) the connected person receives a pro rata entitlement to the issue as a shareholder;

(2) the connected person subscribes for the securities in a rights issue or open offer:

14A.31(3)(c) – N2 (a) through excess application (see rule 7.21(1) or 7.26A(1)); or

14A.31(3)(c) (b) in his/its capacity as an underwriter or sub-underwriter of the rights issue or open offer, and rule 7.21 or 7.26A (arrangements to dispose of any excess securities) has been complied with. In this case, the listing document must contain the terms and conditions of the underwriting arrangement;

14A.31(3)(c) – N1

*Note: Any commission and fees payable by the group to the connected person for the underwriting arrangement are not exempt under this exemption.*

14A.31(3)(b) (3) the securities are issued to the connected person under:

- (a) a share option scheme that complies with Chapter 17; or

- (b) a share option scheme adopted by the issuer before its securities first start dealing on the Exchange, and where the Exchange has approved the listing of the securities to be issued under the scheme; or

14A.31(3)(d)

- (4) the securities are issued under a “top-up placing and subscription” that meets the following conditions:
  - (a) the new securities are issued to the connected person:
    - (i) after it has reduced its holding in the same class of securities by placing them to independent third parties under a placing agreement; and
    - (ii) within 14 days from the date of the placing agreement;
  - (b) the number of new securities issued to the connected person does not exceed the number of securities placed by it; and
  - (c) the new securities are issued at a price not less than the placing price. The placing price may be adjusted for the expenses of the placing.

*Note: An issue of new securities by a subsidiary of the issuer may be fully or partially exempt as a de minimis transaction.*

#### **Dealings in securities on stock exchanges**

14A.31(4)

- 14A.93 Dealing in securities of a target company (i.e. a connected transaction described in rule 14A.25) by the group is fully exempt if it meets the following conditions:
- (1) the dealing in the securities is conducted as part of the group’s ordinary and usual course of business;
  - (2) the securities are listed on the Exchange or a recognised stock exchange;
  - (3) the dealing is carried out on the Exchange or a recognised stock exchange, or if not, no consideration passes to or from a connected person; and
  - (4) the transaction is not made for the purpose of conferring a direct or indirect benefit upon any connected person who is a substantial shareholder of the target company.

#### **Repurchases of own securities**

14A.31(5)

- 14A.94 Repurchases of own securities by an issuer or its subsidiary from a connected person is fully exempt if it is made:
- (1) on the Exchange or a recognised stock exchange, except where the connected person knowingly sells the securities to the group; or
  - (2) in a general offer made under the Code on Share Repurchases.

#### **Directors’ service contracts**

14A.31(6)

- 14A.95 A director entering into a service contract with the issuer or its subsidiary is fully exempt.

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### **Buying or selling consumer goods or consumer services**

14A.31(7),  
14A.33(1)

14A.96 A group buying consumer goods or services as a customer from, or selling consumer goods or services to, a connected person on normal commercial terms in the ordinary and usual course of business is fully exempt if it meets the following conditions:

- (1) the goods or services must be of a type ordinarily supplied for private use or consumption;
- (2) they must be for the buyer's own consumption or use, and not be:
  - (a) processed into the buyer's products, or for resale; or
  - (b) used by the buyer for any of its businesses or contemplated businesses. This condition does not apply if the group is the buyer and there is an open market and transparency in the pricing of the goods or services;
- (3) they must be consumed or used by the buyer in the same state as when they were bought;
- (4) the total consideration or value of the goods or services must be less than 1% of the group's total revenue or total purchases, as published in its latest audited accounts; and
- (5) the transaction must be made on no more favourable terms to the connected person, or no less favourable terms to the group than those available from independent third parties.

*Note: Examples of consumer goods and services are:*

- (1) *Meals consumed by a director at a restaurant owned by the group.*
- (2) *A director buying groceries for his own use at a retail store operated by the group.*
- (3) *Utilities provided by the group to a director's apartment.*
- (4) *Utilities provided by a connected person to the group where the prices are published or publicly quoted and apply to other independent consumers.*

### **Shared administrative services**

14A.31(8),  
14A.33(2)

14A.97 Administrative services shared between the group and a connected person on a cost basis are fully exempt, provided that the costs are identifiable and are allocated to the parties involved on a fair and equitable basis.

*Note: Examples of shared administrative services are shared secretarial, legal and staff training services.*

### Transactions with persons connected with insignificant subsidiaries

14A.31(9),  
14A.33(4)

14A.98 A connected transaction on normal commercial terms is fully exempt if it meets the following conditions:

- (1) it is a connected transaction because it involves a person who is connected solely because of his/its relationship with the issuer's insignificant subsidiary/subsidiaries; and
- (2) the consideration ratio of the transaction is less than 10%. This condition applies only if:
  - (a) the subsidiary (or any of its subsidiaries) is a party to the transaction, or the securities or assets of the subsidiary (or any of its subsidiaries) are the subject of the transaction; and
  - (b) the transaction is of a capital nature.

14A.31(9),  
14A.33(4)

14A.99 An "insignificant subsidiary" is the issuer's subsidiary whose total assets, profits and revenue are less than:

- (1) 10% under the percentage ratios for each of the latest three financial years (or if less, the period since the incorporation or establishment of the subsidiary); or
- (2) 5% under the percentage ratios for the latest financial year.

14A.100 If the person is connected with two or more subsidiaries of the issuer, the Exchange will aggregate the subsidiaries' total assets, profits and revenue to determine whether they are together "insignificant subsidiaries" of the issuer.

14A.101 When calculating the percentage ratios, 100% of the subsidiaries' total assets, profits and revenue will be used. If the percentage ratio produces an anomalous result, the Exchange may disregard the calculation and consider alternative test(s) provided by the issuer.

### Transactions with associates of passive investors

14A.31(10),  
14A.33(5)

14A.102 A connected transaction conducted between the group and an associate of a passive investor is fully exempt if it meets the following conditions:

- (1) the passive investor is a connected person only because it is a substantial shareholder of the issuer and/or any of its subsidiaries;
- (2) the passive investor
  - (a) is not a controlling shareholder of the issuer or its subsidiaries;
  - (b) does not have any representative on the board of directors of the issuer or its subsidiaries, and is not involved in the management of the group, including any influence over the group's management through negative control (e.g. its veto rights) on material matters of the group;
  - (c) is independent of the directors, chief executive, controlling shareholder(s) and any other substantial shareholder(s) of the issuer or its subsidiaries; and

- (3) the transaction is of a revenue nature in the group's ordinary and usual course of business, and conducted on normal commercial terms.

14A.103 A "passive investor" is a substantial shareholder of the issuer and/or any of its subsidiaries that:

- (1) is a sovereign fund, or a unit trust or mutual fund authorised by the Securities and Futures Commission or an appropriate overseas authority; and
- (2) has a wide spread of investments other than the securities of the group and the associate that enters into the transaction with the group.

#### **Qualified property acquisitions**

14A.72

14A.104 The formation of a joint venture by a qualified issuer and a qualified connected person to make a qualified property acquisition is exempt from shareholders' approval requirements if:

- (1) the project will be single purpose, relating to the acquisition and/or development of a specific property, and consistent with the purpose specified in the auction or tender document;
- (2) the joint venture arrangement is on an arm's length basis and on normal commercial terms;
- (3) the joint venture agreement contains clause(s) to the effect that the joint venture may not, without its partners' unanimous consent:
  - (a) change the nature or scope of its business, and, if there are changes, they must be consistent with the scope or purpose specified in the auction or tender document; or
  - (b) enter into any transactions which are not on an arm's length basis; and
- (4) the independent board committee and independent financial adviser have confirmed that:
  - (a) the acquisition is in the group's ordinary and usual course of business; and
  - (b) the acquisition and the joint venture, including its financing and profit distribution arrangements, are on normal commercial terms, are fair and reasonable and in the interests of the issuer and its shareholders as a whole.

14A.10(10A)

14A.105 A qualified connected person is a connected person of the qualified issuer solely because he/it is a substantial shareholder (or its associate) in one or more of the qualified issuer's non wholly-owned subsidiaries formed to participate in property projects, each of which is single purpose and project specific. This person may or may not have representation on the board of the subsidiary/subsidiaries.

14A.73(1),  
14A.73(2) –  
Note

- 14A.106 The issuer shall announce the transaction as soon as practicable after receiving notification of the success of the bid by the joint venture. If any details of the acquisitions or the joint venture required to be disclosed are not available when the issuer publishes the initial announcement, it must publish subsequent announcement(s) to disclose the details as soon as practicable after they have been agreed or finalized.

#### **WAIVERS**

14A.07,  
14A.44

- 14A.107 The Exchange may waive any requirements under this Chapter in individual cases, subject to any conditions that it may impose.

#### **Transactions relating to non-executive directors**

14A.42(1)

- 14A.108 The Exchange may waive the circular and shareholders' approval requirements for a connected transaction with a non-executive director of the issuer or its subsidiaries if:

- (1) the transaction is connected only because of the interest of a non-executive director;
- (2) the director does not control the group, and his principal business interest is not the group; and
- (3) the issuer's auditor or an acceptable financial adviser has given the opinion that the transaction is fair and reasonable to the shareholders as a whole.

#### **Provision of guarantees to connected subsidiaries or commonly held entities for public sector contracts awarded by tender**

14A.42(2)

- 14A.109 The Exchange may waive all or some of the connected transaction requirements for a joint and several guarantee or indemnity provided by the group to a third party creditor for the obligations of a connected subsidiary or a commonly held entity if:

- (1) the guarantee/indemnity is required for a government or public sector contract awarded by tender;
- (2) each of the other shareholders of the connected subsidiary or commonly held entity has given a similar joint and several guarantee or indemnity to the third party creditor; and
- (3) each of the other shareholders of the connected subsidiary or commonly held entity has agreed to indemnify the group for the liability guaranteed, or indemnified at least in proportion to its equity interest in the subsidiary or entity. The issuer must satisfy the Exchange that such shareholder indemnity is sufficient.

#### **Continuing connected transactions of new applicants**

14A.42(3)

- 14A.110 The Exchange may waive the announcement, circular and shareholders' approval requirements for continuing connected transactions entered into by a new applicant or its subsidiaries. The new applicant must disclose in the listing document its sponsor's opinion on whether the transactions are in the group's ordinary and usual course of business, on normal commercial terms, are fair and reasonable and in the interests of the shareholders as a whole.

## DEFINITIONS

14A.111 In this Chapter, the following definitions apply:

- (1) a **"30%-controlled company"** means a company held by a person who can
  - (a) exercise or control the exercise of 30% (or an amount for triggering a mandatory general offer under the Takeovers Code, or for PRC issuers only, an amount for triggering a mandatory general offer or establishing legal or management control over a business enterprise under the PRC law) or more of the voting power at general meetings; or
  - (b) control the composition of a majority of the board of directors;
- (2) an **"associate"** has the meaning in rules 14A.09 to 14A.12;
- (3) a **"banking company"** has the meaning in rule 14A.89;
- (4) a **"closely allied group of shareholders"** has the meaning in rule 14.45;
- (5) a **"commonly held entity"** has the meaning in rule 14A.24;
- (6) a **"connected person"** has the meaning in rules 14A.05 to 14A.08;
- (7) a **"connected person at the issuer level"** includes
  - (a) a director, chief executive, substantial shareholder of an issuer;
  - (b) a supervisor of a PRC issuer;
  - (c) a person who was a director of the issuer in the last 12 months; or
  - (d) an associate of any of the above persons;
- (8) a **"connected person at the subsidiary level"** means a person who is a connected person only because of the person's connection with the issuer's subsidiary or subsidiaries;
- (9) a **"connected subsidiary"** has the meaning in rule 14A.13;
- (10) a **"connected transaction"** has the meaning in rules 14A.22 to 14A.31;
- (11) a **"continuing connected transaction"** has the meaning in rule 14A.31;
- (12) a **"controller"** has the meaning in rule 14A.25(1);

- 14A.10(13)(a) (13) a “**deemed disposal**” has the meaning in rule 14.29;
- (14) a company is “**directly held**” by an individual or an entity means that the individual or the entity has a direct ownership interest in the company;
- (15) a “**family member**” has the meaning in rule 14A.09(2)(a);
- (16) “**financial assistance**” has the meaning in rule 14A.21(4);
- (17) “**financial assistance provided in the ordinary and usual course of business**” means financial assistance provided by a banking company;
- 14A.10(6), (7) (18) a “**group**” means an issuer and its subsidiaries, or any of them;
- (19) an “**immediate family member**” has the meaning in rule 14A.09(1)(a);
- (20) a company is “**indirectly held**” by an individual or an entity means that the individual or the entity has an indirect ownership interest in the company through (in the case of an individual) his majority-controlled company/ companies or (in the case of an entity) its subsidiary/ subsidiaries;
- (21) an “**insignificant subsidiary**” or “**insignificant subsidiaries**” has the meaning in rule 14A.99 to 14A.101;
- 14A.10(6), (7) (22) an “**issuer**” means a company or other legal person whose securities (including depositary receipts) are listed;
- (23) a “**majority-controlled company**” means a company held by a person who can exercise or control the exercise of more than 50% of the voting power at general meetings, or control the composition of a majority of the board of directors;
- (24) “**material interest**” in a transaction has the meaning in rules 2.15 and 2.16;
- (25) a “**monetary advantage**” has the meaning in rule 14.12;
- 14A.10(8) (26) “**normal commercial terms**” are terms which a party could obtain if the transaction were on an arm’s length basis or terms no less favourable to the group than terms available to or from independent third parties;
- 14A.67 (27) an “**option**” and terms related to it (including “**exercise price**”, “**premium**” and “**expiration**”) have the meaning in rule 14.72;
- 14A.10(9) (28) “**ordinary and usual course of business**” of an entity means the entity’s existing principal activities or an activity wholly necessary for its principal activities;

- (29) a “**passive investor**” has the meaning in rule 14A.103;
- 14A.10(10) (30) “**percentage ratios**” has the meaning in rule 14.04(9);
- 14A.56(8) (31) a “**profit forecast**” has the meaning in rule 14.61;
- (32) a “**PRC Governmental Body**” has the meaning in rule 19A.04;
- 14A.10(10A) (33) a “**qualified connected person**” has the meaning in rule 14A.105;
- 14A.10(10B) (34) a “**qualified issuer**” has the meaning in rule 14.04(10B);
- 14A.10(10C) (35) a “**qualified property acquisition**” has the meaning in rule 14.04(10C);
- 14A.10(11) (36) a “**recognised stock exchange**” – a regulated, regularly operating, open stock market recognised for this purpose by the Exchange;
- (37) a “**relative**” has the meaning in rule 14A.18(1)(a);
- (38) a “**transaction**” has the meaning in rule 14A.21; and
- (39) a “**trustees**” has the meaning in rule 14A.09(1)(b) or 14A.10(2).

**(II) Consequential amendments to other parts of the Rules  
(marked up against existing Rules)**

**Chapter 1**

**GENERAL**

**INTERPRETATION**

...

1.01 Throughout this book, the following terms, save where the context otherwise requires, have the following meanings:

...

**“associate”**

...

*Notes (1) This definition is modified in the context of connected transactions by virtue of rules 14A.09 to 14A.12 ~~rules 14A.11, 14A.12 and 14A.12A.~~*

*(2) In the case of a PRC issuer, its directors, supervisors, chief executive and substantial shareholders, the definition is amended to have the same meaning as in rule 19A.04.*

...

**“connected person”**

...

*Note This definition is modified in the context of connected transactions by virtue of rules 14A.05 to 14A.08 ~~case of Chapter 14A only by the provisions of rules 14A.11, 14A.12 and 14A.12A.~~*

...

# Chapter 13

## EQUITY SECURITIES

### CONTINUING OBLIGATIONS

...

#### Meetings of Shareholders

- 13.39 (1) ...
- ...
- (6) In relation to any ~~connected transactions pursuant to Chapter 14A,~~ transactions that are subject to independent shareholders' approval pursuant to the Exchange Listing Rules or spin-off proposals that are subject to approval of the shareholders of the issuer pursuant to paragraph 3(e) of Practice Note 15 of the Exchange Listing Rules,
- (a) the issuer shall establish an independent board committee (which shall consist only of independent non-executive directors) to advise shareholders as to whether the terms of the relevant transaction or arrangement are fair and reasonable and whether such a transaction or arrangement is in the interests of the issuer and its shareholders as a whole and to advise shareholders on how to vote, taking into account the recommendations of the independent financial adviser appointed under rule 13.39(6)(b);
  - (b) the issuer shall appoint an independent financial adviser acceptable to the Exchange to make recommendations to the independent board committee and the shareholders as to whether the terms of the relevant transaction or arrangement are fair and reasonable and whether such a transaction or arrangement is in the interests of the issuer and its shareholders as a whole and to advise shareholders on how to vote; and
  - (c) the independent board committee shall not consist of any independent nonexecutive directors who have a material interest in the relevant transaction or arrangement. The independent board committee may consist of only one independent non-executive director if all other independent non-executive directors have a material interest in the relevant transaction or arrangement. If all the independent non-executive directors have a material interest in the relevant transaction or arrangement, no independent board committee can be formed. In that event, the independent financial adviser shall make its recommendation to the shareholders only in the manner prescribed under rule 13.39(7)(b).

- (7) In relation to any ~~connected transactions pursuant to Chapter 14A~~, transactions that are subject to independent shareholders' approval pursuant to the Exchange Listing Rules or spin-off proposals that are subject to approval of the shareholders of the issuer pursuant to paragraph 3 (e) of Practice Note 15 of the Exchange Listing Rules, the circular to shareholders must contain at least:
- (a) if applicable, a separate letter from the independent board committee advising shareholders as to whether the terms of the relevant transaction or arrangement are fair and reasonable and whether such a transaction or arrangement is in the interests of the issuer and its shareholders as a whole and advising shareholders on how to vote, taking into account the recommendations of the independent financial adviser; and
  - (b) a separate letter from the independent financial adviser containing its recommendation to the independent board committee and shareholders (or, if applicable, to the shareholders only) as to whether the terms of the relevant transaction or arrangement are fair and reasonable and whether such a transaction or arrangement is in the interests of the issuer and its shareholders as a whole and advising shareholders on how to vote. Such letter must set out the reasons for and the key assumptions made and factors taken into consideration in forming that opinion.
- (8) For any connected transactions, the requirements relating to the opinion and recommendation of the independent board committee and the independent financial adviser are set out in Chapter 14A.

*Note: "Independent shareholders" under paragraphs (7) and (8) of this rule 13.39 means any shareholders other than controlling shareholders of the issuer and their associates or, where there are no controlling shareholders, any shareholders other than directors (excluding independent non-executive directors) and the chief executive of the issuer and their respective associates.*

...

#### **Independent financial advisers**

- 13.80 An independent financial adviser appointed under rule 13.39(6)(b), rule 14A.44 or rule 19.05(6)(a)(iii) must take all reasonable steps to satisfy itself that:
- (1) it has a reasonable basis for making the statement required by rule 14A.45 paragraphs (1) to (5) of rule 14A.22; and
  - (2) without limiting the generality of paragraph (1) above, there is no reason to believe any of the following information is not true or omits a material fact:
    - (a) any information relied on by the independent financial adviser in forming its opinion; or
    - (b) any information relied on by any third party expert on whose opinion or advice the independent financial adviser relies in forming its opinion.

- Notes: 1. ...
2. *The Exchange expects the independent financial adviser will ensure the letter referred to at ~~rule 14A.45~~ ~~rule 14A.22~~ takes account of the following principles:*

(a) ...

...

13.81 The issuer must:

- (1) afford any independent financial adviser it appoints pursuant to rule 13.39(6)(b), rule 14A.44 or rule 19.05(6)(iii) full access at all time to all persons, premises and documents relevant to the independent financial adviser's performance of its duties as set out in the Exchange Listing Rules. In particular, ...

...

## Chapter 19A

### EQUITY SECURITIES

#### ISSUERS INCORPORATED IN THE PEOPLE'S REPUBLIC OF CHINA

...

#### Definitions and Interpretation

19A.04 The following terms, save where the context otherwise requires, have the following meanings:-

**“associate”**

...

*Note 1 This definition is modified in the context of connected transactions by virtue of rules 14A.09 to 14A.12 ~~rules 14A.11, 14A.12 and 14A.12A.~~*

*Note 2 Under rule 19A.19 the Exchange may from time to time determine that certain persons or entities should be treated as connected person of a PRC issuer for the purposes of the connected transaction provisions of Chapter 14A.*

...

19A.19 In addition to the requirement of rule 19A.14, the Exchange may from time to time determine that certain persons or entities should be treated as connected persons of a PRC issuer for purposes of the connected transaction provisions of Chapter 14A. ~~However, the Exchange will normally not treat a PRC Governmental Body (see definition in rule 19A.04) as a connected person of a PRC issuer. If requested by the Exchange a PRC issuer must make written representations to the Exchange explaining its legal, commercial or other relationships with various associates or other persons or entities and must satisfy the Exchange that such persons or entities should not be treated as connected persons for the above purposes, or if the Exchange determines that such persons or entities should be treated as connected persons, then the PRC issuer must agree to comply with any additional obligations arising from such treatment as may be requested by the Exchange.~~

...

## **Chapter 21**

### **INVESTMENT VEHICLES**

#### **INVESTMENT COMPANIES**

...

21.13 The Listing Agreement for an investment company will state that the provisions of Chapter 14 will not apply to investment companies save for rule 14.06(3), 14.06(4), 14.34 to 14.37, 14.38A, 14.40 to 14.46, 14.48 to 14.53 (for very substantial disposals), 14.58, 14.60 to 14.63, 14.66 to 14.68, 14.70 to 17.77, 14.85 and 14.86. For the purposes of Chapter 14A ~~rule 14A.13~~, any investment manager, investment adviser or custodian (or any connected person thereof) shall be regarded as a connected person of the issuer.

...

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**APPENDIX II: DRAFT RULE AMENDMENTS FOR PROPOSALS DESCRIBED IN CHAPTERS IV, V AND VI**

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**Amendments to Chapter 14A (marked up against the draft Chapter 14A in Appendix I)**

**Chapter 14A**

**EQUITY SECURITIES**

**CONNECTED TRANSACTIONS**

**INTRODUCTION**

**Cross-references to existing Rules or guidance materials**

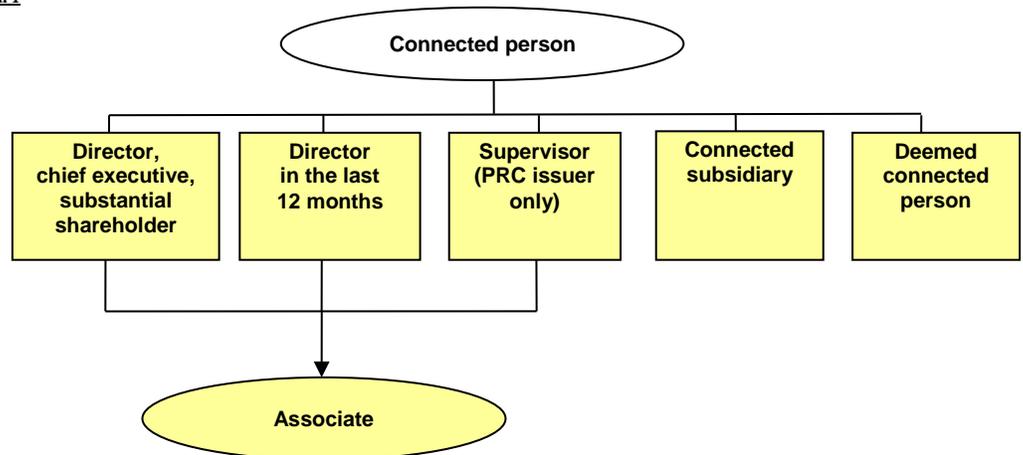
14A.01,  
14A.02,  
14A.03  
(summarised)

- 14A.01 This Chapter applies to connected transactions entered into by an issuer or its subsidiaries. The connected transaction rules ensure that the interests of shareholders as a whole are taken into account by the issuer when a group enters into a connected transaction.
- 14A.02 Connected transactions include both capital and revenue nature transactions. They may be one-off transactions or continuing transactions.
- 14A.03 The general requirements for connected transactions include disclosures in announcements and annual reports, and shareholders' approval. Persons with material interests cannot vote on the resolution approving the transaction. Continuing connected transactions also require annual reviews by independent non-executive directors and the auditors.
- 14A.04 To reduce issuers' compliance burden, exemptions and waivers from all or some of the connected transaction requirements are available for specific categories of connected transactions. These apply to connected transactions that are immaterial to the group, or specific circumstances where the risk of abuse by connected persons is low.
- 14A.04A The rules in this Chapter have been illustrated with diagrams. If there is any conflict between the rules and the diagrams, the rules prevail.

## DEFINITION OF CONNECTED PERSON

- 14A.05 A “connected person” is:
- 1.01, 14A.11(1) (1) a director, chief executive or substantial shareholder of the issuer or any of its subsidiaries;
  - 14A.11(2) (2) a person who was a director of the issuer or any of its subsidiaries in the last 12 months;
  - 1.01, 14A.11(3) (3) a supervisor of a PRC issuer or any of its subsidiaries;
  - 1.01, 14A.11(4) (4) an associate of any the above persons;
  - (5) a connected subsidiary; or
  - (6) a person deemed to be connected by the Exchange.

Diagram 1



- 21.13 14A.06 Where an issuer is an investment company listed under Chapter 21, its connected persons also include an investment manager, investment adviser or custodian (or any connected person of each of them).

### Exceptions

#### Persons connected with insignificant subsidiaries

Proposal C(1)

14A.06A Rules 14A.05(1) to (3) do not include a director, chief executive, substantial shareholder or supervisor of the issuer’s insignificant subsidiary/subsidiaries. For this purpose:

- (1) an “insignificant subsidiary” is a subsidiary whose total assets, profits and revenue compared to the group’s are less than:
  - (a) 10% under the percentage ratios for each of the latest three financial years (or if less, the period since the incorporation or establishment of the subsidiary); or
  - (b) 5% under the percentage ratios for the latest financial year;

- (2) if the person is connected with two or more subsidiaries of the issuer, the Exchange will aggregate the subsidiaries' total assets, profits and revenue to determine whether they are together "insignificant subsidiaries" of the issuer; and
- (3) when calculating the percentage ratios, 100% of the subsidiary's total assets, profits and revenue will be used. If the percentage ratio produces an anomalous result, the Exchange may disregard the calculation and consider alternative test(s) provided by the issuer.

*PRC Governmental Body*

14A.12A(2),  
19A.19

14A.07 The Exchange will not normally treat a PRC Governmental Body as a connected person. The Exchange may request an issuer to explain its relationship with a PRC Governmental Body and why it should not be treated as a connected person. If the Exchange decides to treat the PRC Governmental Body as a connected person, the issuer must comply with any additional requirements requested by the Exchange.

*Depository*

1.01 - (c),  
19B.03

14A.08 For a listing of depository receipts, a person holding shares of an issuer as a depository will not be treated as:

- (1) an associate of the holder of the depository receipts; or
- (2) a substantial shareholder or controlling shareholder of the issuer.

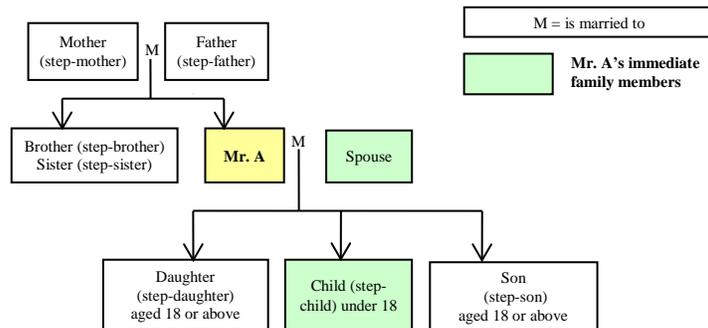
**Definition of associate**

1.01 - (a)(i), (ii),  
19A.04 - (a)(i), (ii)

14A.09 An "associate" of a connected person described in rule 14A.05(1), (2) or (3) who is an individual includes:

- (1) (a) his spouse, his (or his spouse's) child (natural or adopted) or step-child under the age of 18 years (each an "immediate family member");

Diagram 2



1.01 - (a)(iii),  
19A.04 - (a)(iii)

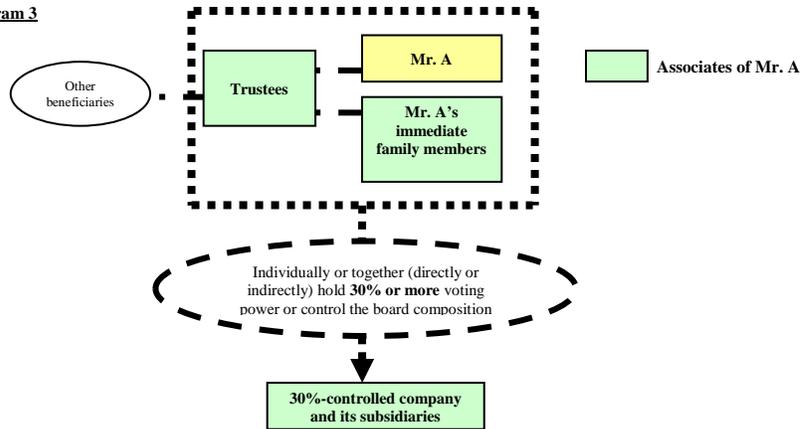
- (b) the trustees, acting in their capacity as trustee of any trust of which the individual or his immediate family member is a beneficiary or, in the case of a discretionary trust, is (to his knowledge) a discretionary object (other than a trust which is an employees' share scheme or occupational pension scheme and the connected persons' interests in the scheme are less than 10%) (the "trustees"); or

Proposal C(2)

1.01 - (a)(v),  
19A.04 - (a)(v)

- (c) a 30%-controlled company held, directly or indirectly, by the individual, his immediate family members and/or the trustees (individually or together), or any of its subsidiaries; or

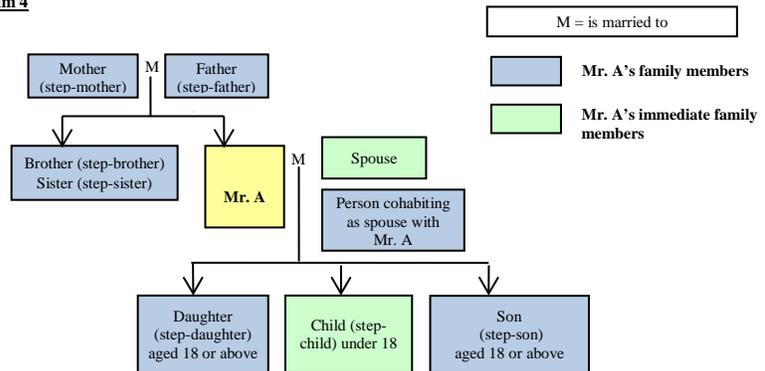
Diagram 3



14A.11(4)(b)(i)

- (2) (a) a person cohabiting with him as a spouse, or his child, step-child, parent, step-parent, brother, step-brother, sister or step-sister (each a "family member"); or

Diagram 4

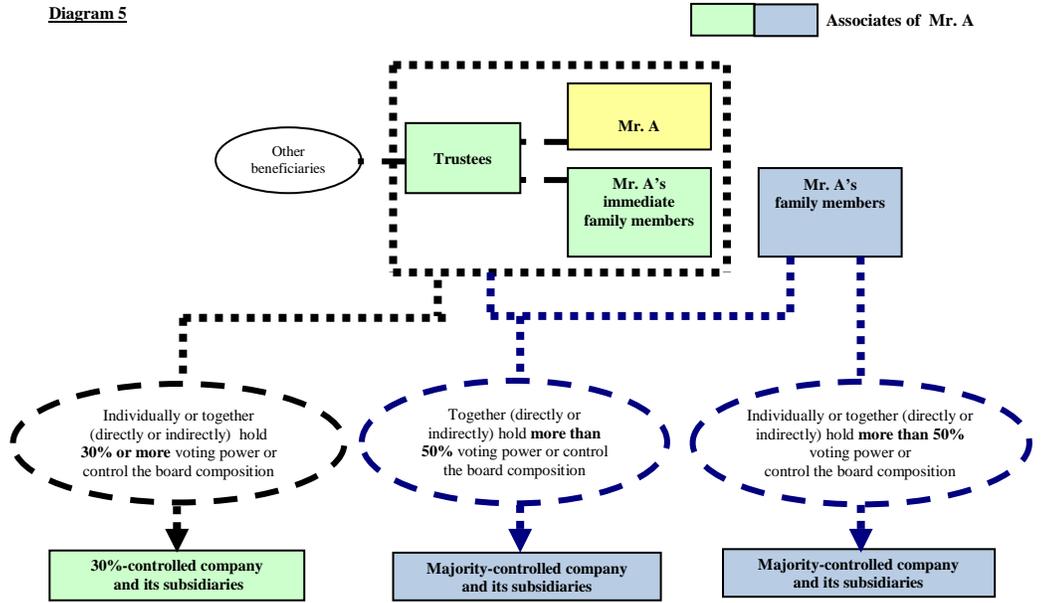


14A.11(4)(b)(ii),  
14A.11(4) - N3

- (b) a majority-controlled company held, directly or indirectly, by the family members (individually or together), or held by the family members together with the individual, his immediate family members and/or the trustees, or any of its subsidiaries.

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**Diagram 5**



14A.10 An “associate” of a connected person described in rule 14A.05(1), (2) or (3) which is a company includes:

1.01 - (b)(i),  
19A.04 - (b)(i)

(1) its subsidiary or holding company, or a fellow subsidiary of the holding company (together the “group companies”);

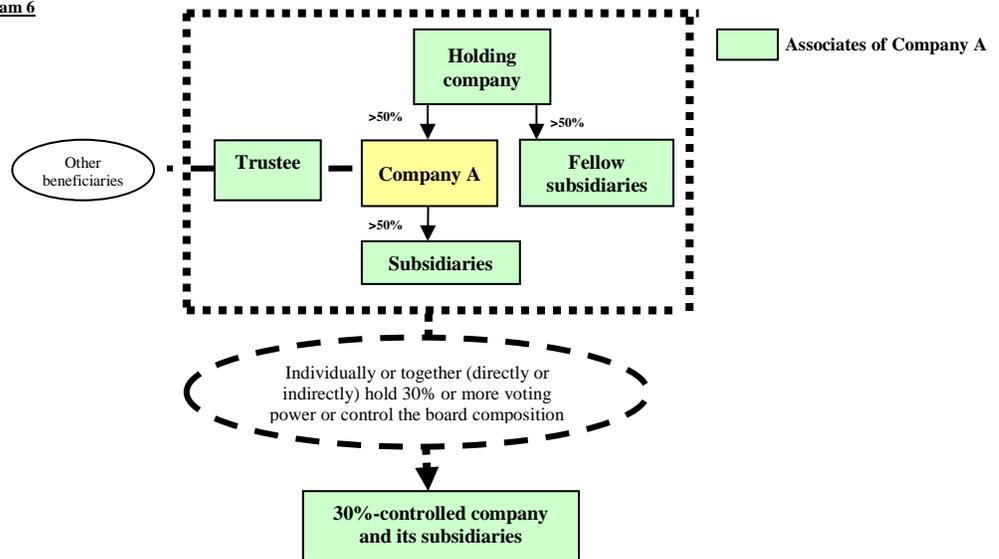
1.01 - (b)(ii),  
19A.04 - (b)(ii)

(2) the trustees, acting in their capacity as trustees of any trust of which the company is a beneficiary or, in the case of a discretionary trust, is (to its knowledge) a discretionary object (the “trustees”); or

1.01 - (b)(iv),  
19A.04 - (b)(iv)

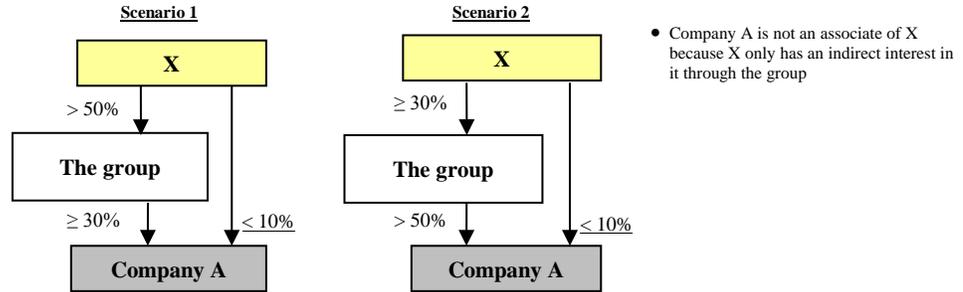
(3) a 30%-controlled company held, directly or indirectly, by the company, the group companies, and/or the trustees (individually or together), or any of its subsidiaries.

**Diagram 6**



14A.11 A company will not be regarded as a person’s associate only because the person holds an interest in the company through his/its shareholding in the group. It will be regarded as an associate if the person and his/its associate(s) together have an interest in the company in addition to those held through the group of 10% or more.

Diagram 7

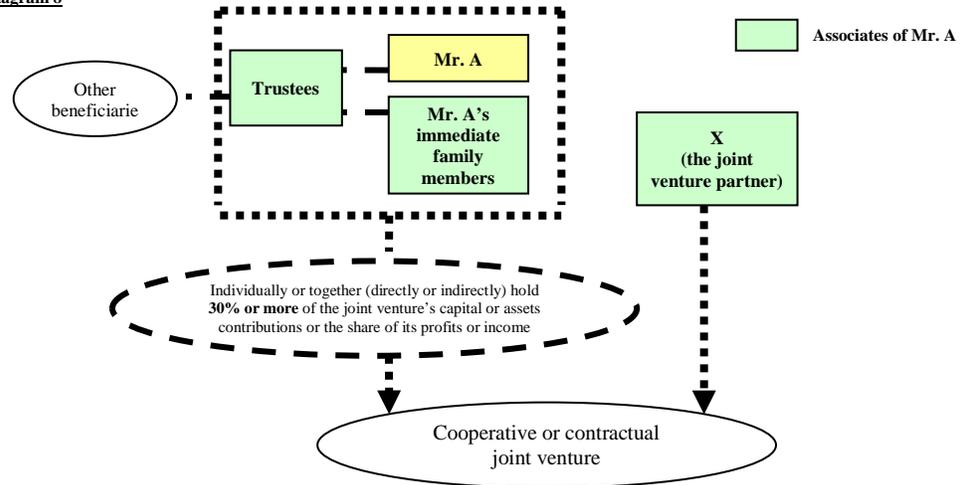


14A.12 For PRC issuers only, a person’s associates include any joint venture partner of a cooperative or contractual joint venture (whether or not it is a separate legal entity) where:

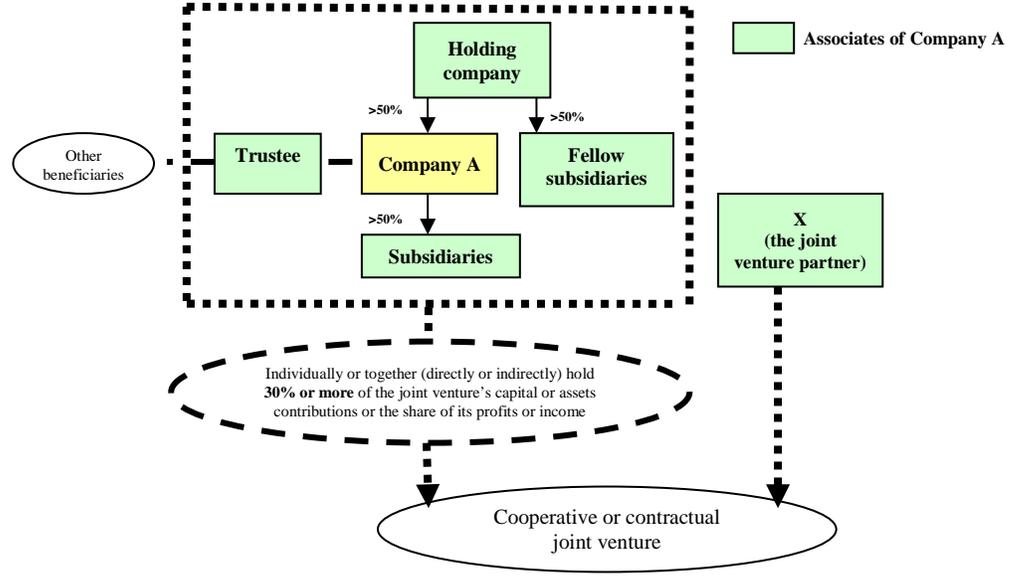
- (1) the person (being an individual), his immediate family members and/or the trustees; or
- (2) the person (being a company), its group companies and/or the trustees,

together directly or indirectly hold 30% (or an amount that would trigger a mandatory general offer or establish legal or management control over a business enterprise under the PRC law) or more in the joint venture’s capital or assets contributions, or the contractual share of its profits or other income.

Diagram 8



**Diagram 9**



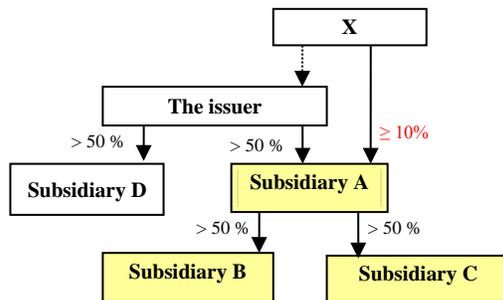
**Definition of connected subsidiary**

14A.13 A “connected subsidiary” is:

- 14A.11(5) (1) a non wholly-owned subsidiary of the issuer where any connected person(s) at the issuer level, individually or together, can exercise or control the exercise of 10% or more of the voting power at the subsidiary’s general meeting. This 10% excludes any indirect interest in the subsidiary which is held by the connected person(s) through the issuer; or
- 14A.11(6) (2) any subsidiary of a non wholly-owned subsidiary referred to in (1) above.

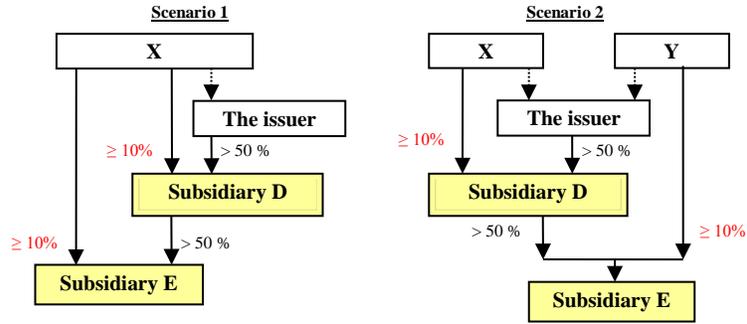
14A.31(1A) 14A.14 If an issuer’s subsidiaries are connected persons only because they are the subsidiaries of a connected subsidiary, transactions between these subsidiaries will not be treated as connected transactions.

**Diagram 10**



- X is a connected person at the issuer level, and he/it has a 10% (or more) shareholding in Subsidiary A.  
→ Subsidiary A is a connected subsidiary. (See rule 14A.13(1))
- Subsidiaries B and C are subsidiaries of Subsidiary A.  
→ Subsidiaries B and C are also connected subsidiaries. (See rule 14A.13(2))
- Transactions between the issuer/Subsidiary D with Subsidiary A/B/C are connected transactions.
- Transactions between any of Subsidiaries A, B and C are not connected transactions if Subsidiaries B and C are connected solely because of their relationship with Subsidiary A. (See rule 14A.14)

**Diagram 11**



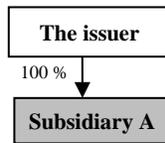
- X and Y are connected persons at the issuer level.
- Subsidiaries D and E are connected subsidiaries.
- Subsidiary E is a subsidiary of Subsidiary D. However, the exemption in rule 14A.14 does not apply to transactions between them because Subsidiary E is a connected subsidiary not only because of its relationship with Subsidiary D but also its relationship with X or Y.

14A.15 A subsidiary of the issuer is not a connected person if:

14A.12

- (1) it is wholly-owned by the issuer; or

**Diagram 12**

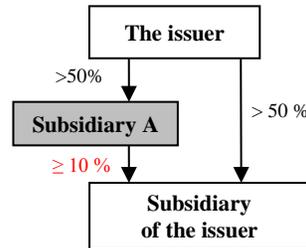


14A.12A

- (2) it falls under the definition of connected person only because it is:

- (a) a substantial shareholder of another subsidiary of the issuer; or

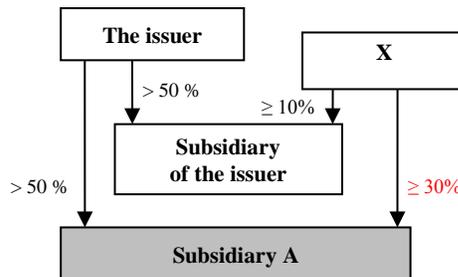
**Diagram 13**



- Subsidiary A is a substantial shareholder of another subsidiary of the issuer. However, this relationship will not make Subsidiary A a connected person of the issuer.

- (b) an associate of a director (or a person who was in past 12 months a director), a chief executive, a substantial shareholder or a supervisor of any subsidiary of the issuer.

**Diagram 14**



- X is a substantial shareholder of a subsidiary of the issuer.
- X holds 30% (or more) shareholding in Subsidiary A.
- Subsidiary A is an associate of X. However, this relationship will not make Subsidiary A a connected person of the issuer because X is only a connected person at the subsidiary level.

## Deemed connected persons

14A.06

14A.16 The Exchange has the power to deem any person to be an issuer's connected person.

14A.16A The Exchange will deem a person to be an issuer's connected person if the Exchange considers that:

Proposal B

(1) he/it is a shadow director or de facto controlling shareholder of the issuer;  
or

(2) he/it is accustomed to acting according to the directions or instructions of any connected person described in rules 14A.05(1) to (5).

14A.11(4)(a)

14A.17 A deemed connected person of an issuer includes a person:

(1) who has entered, or proposes to enter, into:

(a) a transaction with the group; and

(b) an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with a connected person described in rule 14A.05(1), (2) or (3) with respect to the transaction; and

(2) who, in the Exchange's opinion, should be considered as a connected person.

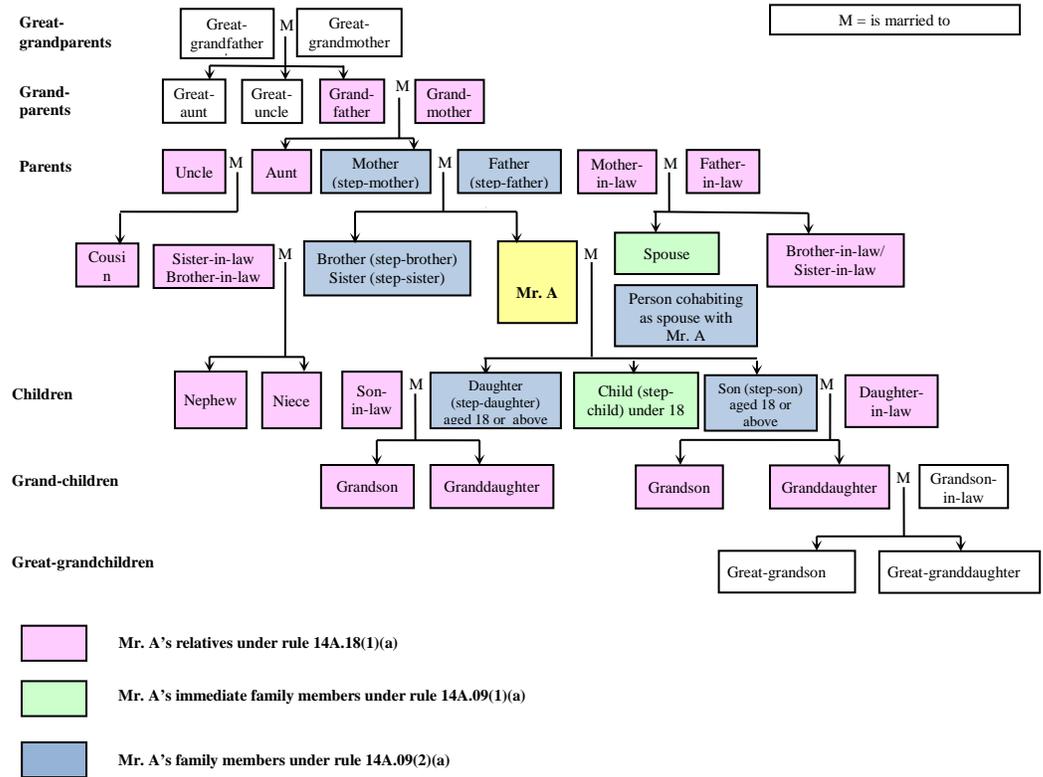
14A.18 A deemed connected person also includes a person:

(1) who is:

14A.11(4)(c)(i)

(a) a father in-law, mother-in-law, son-in-law, daughter-in-law, brother-in-law, sister-in-law, grandparent, grandchild, uncle, aunt, cousin, nephew or niece (each a "relative") of a connected person as described in rule 14A.05(1), (2) or (3); or

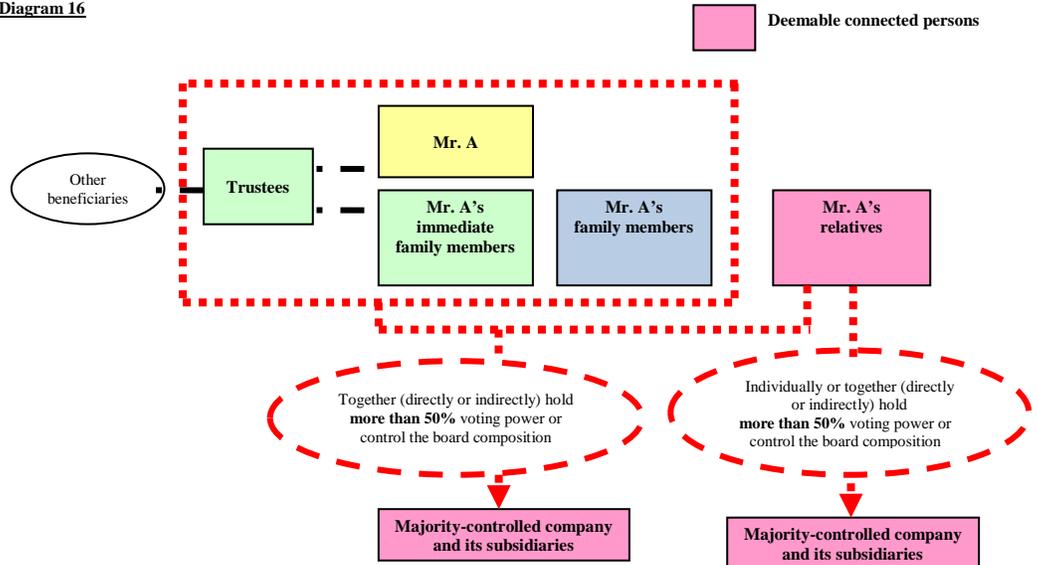
Diagram 15



- (b) a majority-controlled company held, directly or indirectly, by the relatives (individually or together) or held by the relatives together with the connected person as described in rule 14A.05(1), (2) or (3), the trustees, his immediate family members and/or family members, or any subsidiary of that majority-controlled company; and

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Diagram 16



- (2) whose association with the connected person is such that, in the Exchange's opinion, the proposed transaction should be subject to the connected transaction requirements.

14A.11(4)(c)

14A.19 The issuer must inform the Exchange of any proposed transaction with the person described in rule 14A.17(1) or 14A.18(1) unless it is exempt from all of the connected transaction requirements. It must provide information to the Exchange to demonstrate whether or not the transaction should be subject to connected transaction requirements.

Drafting  
changes

### WHAT ARE CONNECTED TRANSACTIONS

14A.20 Connected transactions include transactions with connected persons, and transactions with third parties that may confer benefits to connected persons through their interests in the entities involved in the transactions.

14A.10(13)

14A.21 "Transactions" include both capital and revenue nature transactions, whether or not conducted in the group's ordinary and usual course of business. This includes the following types of transactions:

- (1) any buying or selling of assets by a group including a deemed disposal;
- (2) (a) a group granting, accepting, exercising, transferring or terminating an option to buy or sell assets or to subscribe for securities; or

*Note: Terminating an option is not a transaction if it is made under the terms of the original agreement and ~~does not involve payment of any penalty, damages or other compensation by the group~~ the group has no discretion over the termination.*

Proposal G(2)

14A.10(13)(b),  
14A.68

- (b) a group deciding not to exercise an option to buy or sell assets or to subscribe for securities;
- (3) entering into or terminating finance leases or operating leases;
- (4) providing or receiving financial assistance. "Financial assistance" includes granting credit, lending money, or providing an indemnity against obligations under a loan, or guaranteeing or providing security for a loan;
- (5) entering into an agreement or arrangement to set up a joint venture in any form (e.g. a partnership or a company), or any other form of joint arrangement;
- (6) issuing new securities of the issuer or its subsidiaries;
- (7) providing, receiving or sharing services; or
- (8) buying or selling raw materials, intermediate products and/or finished goods.

### Transactions with connected persons

14A.13(1)(a),  
14A.13(2)(a)(i),  
14A.13(2)(b)(i)

14A.22 Any transaction between a group and a connected person is a connected transaction.

## Financial assistance to/from commonly held entities

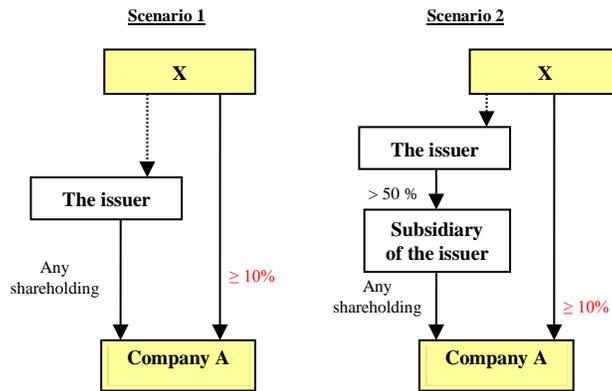
14A.13(2)(a)(ii),  
14A.13(2)(b)(ii),  
14A.13(3), (4)

14A.23 Financial assistance provided by a group to, or received by a group from, a commonly held entity is a connected transaction.

14A.24 A “commonly held entity” is a company whose shareholders include:

- (1) a member of the group; and
- (2) any connected person(s) at the issuer level who, individually or together, can exercise or control the exercise of 10% or more of the voting power at the company’s general meeting. This 10% excludes any indirect interest held by the person(s) through the issuer.

Diagram 17



- X is a connected person at the issuer level
- Both the group and X are shareholders of Company A, and X holds 10% (or more) of shareholding in Company A.
- Company A is a commonly held entity.
- Financial assistance provided by the group to, or received by the group from, Company A is a connected transaction.

## Transactions with third parties

14A.13(1)(b)(i)

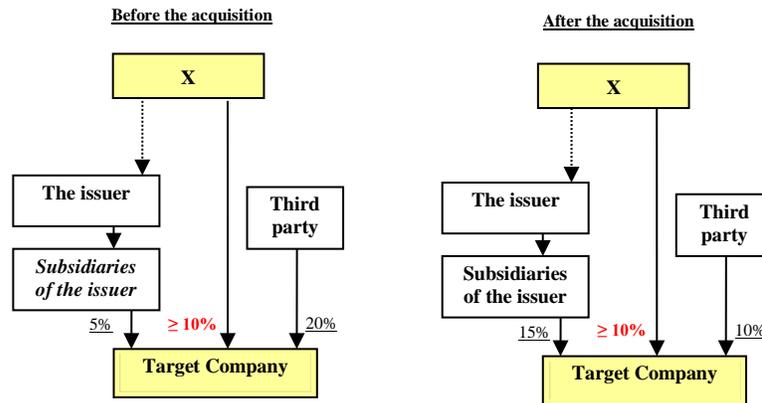
14A.25 A group buying ~~or selling~~ an interest in a company (the “target company”) from ~~or to~~ a person who is not a connected person is a connected transaction if the target company’s substantial shareholder:

Proposal E(b)

- (1) is, or is proposed to be, a controller. A “controller” is a director, chief executive or controlling shareholder of the issuer ~~or any of its subsidiaries;~~ or
- (2) is, or will, as a result of the transaction, become, an associate of a controller or proposed controller.

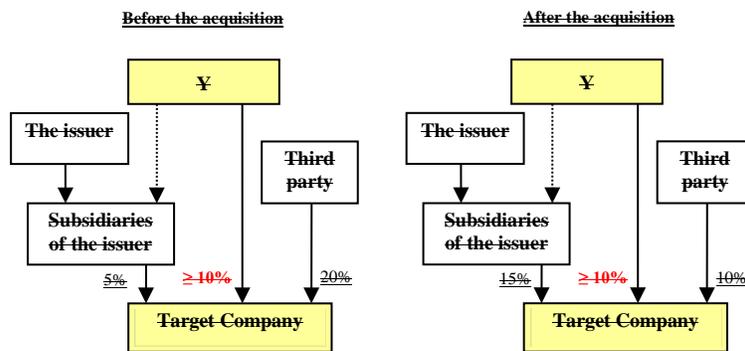
Proposal E(a)

Diagram 18



- X is a (proposed) controller of the issuer.
- X is a substantial shareholder of the Target Company.
- The group's acquisition of an interest in the Target Company from the Third Party is a connected transaction.
- The group's disposal of an interest in the Target Company to the Third Party or any other third party is also a connected transaction.

Diagram 19



- Y is a (proposed) controller of the issuer's subsidiary or subsidiaries.
- Y is a substantial shareholder of the Target Company.
- The group's acquisition of an interest in the Target Company from the Third Party is a connected transaction.
- The group's disposal of an interest in the Target Company to the Third Party or any other third party is also a connected transaction.

14A.13(1)(b)(i) 14A.26 The Exchange may aggregate the interests of the controller and his/its associates in the target company to decide whether they together are the target company's substantial shareholder.

14A.13(1)(b)(i) 14A.27 Buying or selling the target company's assets is also a connected transaction if these assets account for 90% or more of the target company's net assets or total assets.

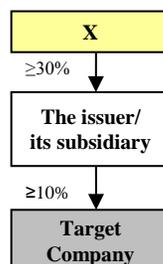
Proposal E(b)

14A.28 Rule 14A.25 or 14A.27 does not apply to an issuer's proposed acquisition or disposal if:

Proposal E(b)

14A.13(1)(b)(i) - N1, N2 (1) — the controller or his/its associate(s) is/are together the target company's substantial shareholders only because of their indirect shareholdings in the target company held through the group, or

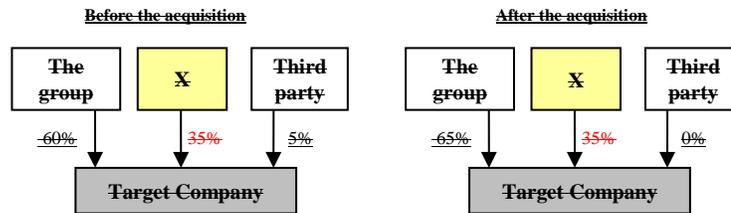
Diagram 20



- X is a controller of the issuer or its subsidiary or subsidiaries.
- X only has an indirect interest in the Target Company through the group.
- The group's acquisition or disposal of an interest in the Target Company from or to any third party (who is not a connected person) is not a connected transaction.

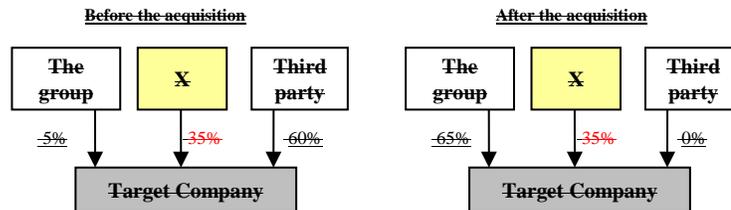
- (2) (a) the target company is, or will be, a subsidiary of the issuer;
- (b) the target company's substantial shareholder is a controller or proposed controller only because of his/its relationship with the target company; and
- (c) the substantial shareholder's interest in the target company does not increase (in the case of an acquisition) or change (in the case of a disposal) as a result of the proposed transaction or any related arrangement.

**Diagram 21**



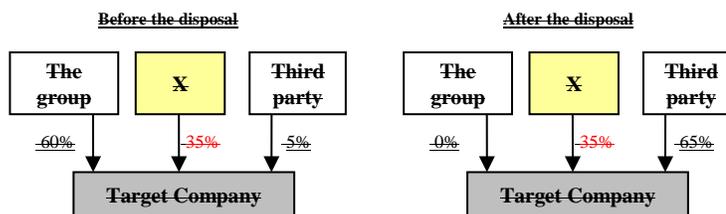
- The Target Company is a subsidiary of the issuer.
  - X is a substantial shareholder of the Target Company.
  - X is a controller of the group only because he is a controlling shareholder and/or director of the Target Company.
  - There is no change in X's interest in the Target Company as a result of the transaction.
- The group's acquisition of an interest in the Target Company from the Third party (who is not a connected person) is not a connected transaction.

**Diagram 22**



- The Target Company will become a subsidiary of the issuer after the acquisition.
  - X is a substantial shareholder of the Target Company.
  - X will be a controller of the group only because he is, and will remain, a controlling shareholder and/or director of the Target Company.
  - There is no change in X's interest in the Target Company as a result of the transaction.
- The group's acquisition of an interest in the Target Company from the third party (who is not a connected person) is not a connected transaction.

**Diagram 23**



- The Target Company is a subsidiary of the issuer.
  - X is a substantial shareholder of the Target Company.
  - X is a controller of the group only because he is a controlling shareholder and/or director of the Target Company.
  - There is no change in X's interest in the Target Company as a result of the transaction.
- The group's disposal of an interest in the Target Company to the third party (who is not a connected person) is not a connected transaction.

14A.29 A transaction between a group and a person who is not a connected person is a connected transaction if it involves:

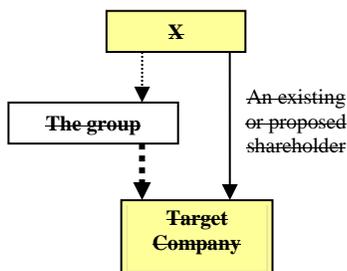
Proposal E(c)

14A.13(1)(b)(ii)

(1) — the group acquiring an interest in a company (or an option to acquire such interest) of which the controller (or his/its associate) is, or will become, a shareholder, and the interest is:

- (a) — of a fixed income nature;
- (b) — shares to be acquired on less favourable terms than those granted to the controller or the associate;
- (c) — shares which are of a different class from those held or to be granted to the controller or the associate; or

**Diagram 24**



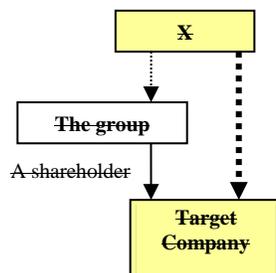
- X is a controller of the issuer or its subsidiary or subsidiaries.
  - X is, or will become, a shareholder of the Target Company.
  - The group proposes to acquire an interest in the Target Company which is (i) of a fixed income nature, (ii) on terms less favourable than those available to X; or (iii) shares of a different class from those held or to be acquired by X.
- The group's acquisition of the interest in the Target Company is a connected transaction.

14A.13(1)(b)(iii), (iv)

(2) — the controller (or his/its associate) subscribing for shares in a company of which the group is a shareholder, and

- (a) — the shares being subscribed are of a different class from those held by the group; or
- (b) — the shares are to be subscribed on specially favourable terms to the controller (or his/its associate).

Diagram 25



- X is a controller of the issuer or its subsidiary or subsidiaries
- The group is a shareholder of the Target Company.
- The group enters into a transaction with a third party which involves X subscribing for shares in the Target Company which are (i) of a different class from those held by the group; or (ii) to be subscribed on specially favourable terms to X
- The group's transaction with the third party is a connected transaction.

14A.13(1)(b)(ii),  
(iii), (iv) – N

14A.30 ~~Rule 14A.29 does not apply if the group and the controller (or his/its associate) acquire or subscribe for shares in a company where the terms of the acquisition or subscription have been approved by shareholders under this Chapter.~~

Proposal E(c)

### Definition of continuing connected transaction

14A.14

14A.31 Continuing connected transactions are connected transactions involving the provision of goods or services or financial assistance, which are carried out on a continuing or recurring basis and are expected to extend over a period of time. They are usually transactions in the group's ordinary and usual course of business.

### REQUIREMENTS FOR CONNECTED TRANSACTIONS

14A.16,  
14A.17

14A.32 This section sets out the requirements for connected transactions.

14A.33 Exemptions or waivers from all or some of the requirements are available for certain type of connected transactions. See rules 14A.74 to 14A.110A.

Proposal F(1)

### Written agreement

14A.04,  
14A.35(1)

14A.34 The group must enter into a written agreement for a connected transaction.

14A.34A The issuer may apply for a waiver to enter into a written agreement if it meets the conditions described in rule 14A.110A.

Proposal F(1)

### Announcement

14A.47(2),  
14A.56

14A.35 The issuer must announce the connected transaction as soon as practicable after its terms have been agreed. See rule 14A.70 for the content requirements.

*Note: If the connected transaction is subsequently terminated or there is any material variation of its terms or material delay in the completion, the issuer must announce this fact as soon as practicable.*

### Shareholders' approval

14A.18,  
14A.35(4),  
14A.52,  
14A.54

14A.36 The connected transaction must be conditional on shareholders' approval at a general meeting held by the issuer. Any shareholder who has a material interest in the transaction must abstain from voting on the resolution.

- 14A.43, 14A.53
- 14A.37 The Exchange may waive the general meeting requirement and accept a written shareholders' approval, subject to the conditions that:
- (1) no shareholder of the issuer is required to abstain from voting if a general meeting is held to approve the transaction; and
  - (2) the approval is given by a shareholder or a closely allied group of shareholders who (together) hold more than 50% of the voting rights in the general meeting.

14A.43 - N2

14A.38 If the issuer discloses inside information to any shareholder in confidence to solicit the written approval, it must ensure that the shareholder is aware that he must not deal in the securities before the information has been made available to the public.

14A.21

14A.39 If the connected transaction requires shareholders' approval, the issuer must (1) set up an independent board committee; and (2) appoint an independent financial adviser.

*Independent board committee*

- 14A.21, 13.39(6), (7)
- 14A.40 The independent board committee must, taking into account the recommendation of an independent financial adviser, advise the issuer's shareholders:
- (1) whether the terms of the connected transaction are fair and reasonable;
  - (2) whether the connected transaction is on normal commercial terms and in the group's ordinary and usual course of business;
  - (3) whether the connected transaction is in the interests of the issuer and its shareholders as a whole; and
  - (4) how to vote on the connected transaction.

Proposal H

13.39(6)(c)

14A.41 The independent board committee should consist only of independent non-executive directors who do not have a material interest in the transaction.

13.39(6)(c), 14A.58 - N

14A.42 If all the independent non-executive directors have a material interest in the transaction, an independent board committee will not be formed. The independent financial adviser must then make its recommendation to the shareholders directly.

14A.58(3)(c), 13.39(7)(a)

14A.43 If an independent board committee is formed, the circular should include a letter from the independent board committee containing its opinion and recommendation.

*Independent financial adviser*

13.39(6)(b), 14A.21, 14A.23

14A.44 The issuer must appoint an independent financial adviser acceptable to the Exchange to make recommendations to the independent board committee and shareholders on the matters in rules 14A.45(1) to (4). The independent financial adviser will give its opinion based on the written agreement for the transaction.

- 14A.22,  
14A.58(3)(d),  
13.39(6)(b), (7)(b)
- 14A.45 The circular should include a letter from the independent financial adviser containing its opinion and recommendation. The independent financial adviser's letter must also set out the reasons for its opinion, the key assumptions made, the factors that it has taken into consideration in forming the opinion, and a statement whether:
- (1) the terms of the connected transaction are fair and reasonable;
  - (2) the connected transaction is on normal commercial terms and in the group's ordinary and usual course of business;
  - (3) the connected transaction is in the interests of the issuer and its shareholders as a whole; and
  - (4) the independent shareholders should vote in favour of the connected transaction.

### **Circular**

- 14A.49
- 14A.46 The issuer must send a circular to its shareholders:
- (1) at the same time as or before the issuer gives notice of the general meeting if the connected transaction is to be approved by shareholders in a general meeting; or
  - (2) within 15 business days after publication of the announcement in any other cases. The issuer may apply for a waiver from this requirement if it requires additional time to prepare the circular.

14A.49,  
14A.58,  
14A.59

*Note: See rules 14A.70 and 14A.71 for the content requirements.*

- 14A.56(10)
- 14A.47 The issuer must announce the expected date of distribution of the circular, and if this is more than 15 business days after the publication of the announcement, the reasons why this is so.

- 14A.47A
- 14A.48 If the issuer expects a delay in distribution of the circular by the date previously announced, it must announce this fact, the reason for the delay and the new expected date of distribution of the circular before the original despatch date.

### *Supplementary circular or announcement*

- 14A.49
- 14A.49 If the issuer is aware of any material information relating to the connected transaction after it has issued the circular, it must publish this information in a supplementary circular or announcement at least 10 business days before the date of the general meeting to consider the transaction. The meeting must be adjourned by the chairman or, if that is not permitted by the issuer's constitutional documents, by resolution to that effect if it is necessary for the compliance with the 10 business day requirement. (See rule 13.73 for the factors that the issuer should consider when deciding whether to issue a supplementary circular or announcement.)

### **Annual reporting**

- 14A.35(3),  
14A.45,  
14A.46
- 14A.50 The issuer must disclose its connected transactions conducted during the financial year in its annual report. See rules 14A.72 and 14A.73 for the content requirements.

## Requirements for continuing connected transactions

14A.51 The following additional requirements apply to a continuing connected transaction.

### *Terms of an agreement*

14A.35(1) 14A.52 A written agreement for a continuing connected transaction must contain the basis for calculating the payments to be made. Examples include sharing of costs incurred by the parties, unit prices for goods or services provided, annual rental for leasing a property, or management fees based on a percentage of the total construction cost.

14A.35(1) 14A.53 The period for the agreement must be fixed and reflect normal commercial terms. It must not exceed 3 years except in special circumstances where the nature of the transaction requires a longer period. In this case, the issuer must appoint an independent financial adviser to explain why the agreement requires a longer period and to confirm that it is normal business practice for agreements of this type to be of such duration.

LD88-1,  
FAQ Series 7  
No.49 and 50

### *Annual cap*

14A.54 The issuer must set an annual cap (the “cap”) for the continuing connected transaction. The cap must be:

14A.35(2)

LD88-1

- (1) (a) expressed in monetary terms; or
- (b) as a percentage of the issuer’s annual revenue or other financial items in its published accounts. This option only applies to continuing connected transactions of a revenue nature in the issuer’s ordinary and usual course of business;
- (2) determined by reference to previous transactions and figures in the group’s published information. If there were no previous transactions, the cap must be set based on reasonable assumptions; and
- (3) approved by shareholders if the transaction requires shareholders’ approval.

Proposal F(2)

14A.35(2)

14A.52

### *Changes to annual cap or terms of agreement*

14A.36 14A.55 The issuer must re-comply with the announcement and shareholders’ approval requirements before:

FAQ Series 7  
No. 52

- (1) the cap is exceeded; or
- (2) it proposes to renew the agreement or to effect a material change to its terms.

*Note: The revised or new cap(s) will be used to calculate the percentage ratios for classifying the continuing connected transaction.*

*Annual review by independent non-executive directors and auditors*

- 14A.37 14A.56 The issuer's independent non-executive directors must review the continuing connected transactions every year and confirm in the annual report whether the transactions have been entered into:
- (1) in the group's ordinary and usual course of business;
  - (2) on normal commercial terms; and
  - (3) according to the agreement governing them on terms that are fair and reasonable and in the interests of the issuer's shareholders as a whole.
- 14A.38 14A.57 The issuer must engage its auditors to report on the continuing connected transaction every year. The auditors must provide a letter to the issuer's board of directors confirming whether anything has come to their attention that causes them to believe that the continuing connected transactions:
- (1) have not been approved by the issuer's board of directors;
  - (2) were not, in all material respects, in accordance ~~are in compliance~~ with the group's pricing policies if the transactions involve provision of goods or services by the group;
  - (3) were not entered into, in all material respects, are in accordance with the relevant agreement governing the transactions; and
  - (4) have ~~not~~ exceeded the cap (if applicable).
- ~~Note: A confirmation provided by the auditors according to Practice Note 740 issued by the Hong Kong Institute of Certified Public Accountants is acceptable under this rule.~~
- 14A.38 14A.58 The issuer must provide a copy of the auditors' letter to the Exchange at least 10 business days before the bulk printing of its annual report.
- 14A.39 14A.59 The issuer must allow, and ensure that the counterparties to the continuing connected transactions allow, the auditors sufficient access to their records for the purpose of reporting on the transactions.
- 14A.40 14A.60 The issuer must promptly notify the Exchange and publish an announcement if the independent non-executive directors and/or the auditors cannot confirm the matters as required. The Exchange may require the issuer to re-comply with the announcement and shareholders' approval requirements and may impose additional conditions.

Proposal F(3)

*When a continuing transaction subsequently becomes connected*

14A.61 If the group has entered into an agreement with fixed terms for:

14A.41

(1) a continuing transaction, and the transaction subsequently becomes a continuing connected transaction, or

14A.33 – N2

(2) a continuing connected transaction exempt under the “insignificant subsidiary exemption” (see rules 14A.98 to 14A.101) or the “passive investor exemption” (see rules 14A.102 and 14A.103), and the transaction subsequently cannot meet the conditions for the exemption,

Proposal C(1)

the issuer must:

(a) as soon as practicable after becoming aware of this fact, comply with the annual review and disclosure requirements including publishing an announcement and annual reporting if the group continues to conduct the transaction under the agreement; and

(b) when the agreement is renewed or its terms are varied, comply with all connected transaction requirements.

**Other requirements relating to connected transactions**

*Options*

14A.62 If the group grants an option to a connected person and the group does not have discretion to exercise the option, the transaction is classified as if the option has been exercised (see rule 14A.80(1)). In addition, the issuer must announce the following subsequent events as soon as practicable:

14A.69(2), (3)(c)

(1) any exercise or transfer of the option by the option holder; and/or

14A.69(3)(a), (b)

(2) (if the option is not exercised in full), the option holder notifying the group that it will not exercise the option, or the expiry of the option, whichever is earlier.

*Guaranteed profits or net tangible assets*

14A.57,  
14A.59(10)

14A.63 The following apply if the group acquires a company or business from a connected person, and the connected person guarantees the profits or net tangible assets or other matters regarding the financial performance of the company or business.

14A.57,  
14A.59(10)

14A.64 If the actual amount is less than the amount guaranteed, the issuer must disclose the following in an announcement and in its next annual report:

(1) the shortfall and any adjustment in the consideration for the transaction;

(2) whether the connected person has fulfilled its obligations under the guarantee;

(3) whether the group has exercised any option to sell the company or business back to the connected person or other rights it held under the terms of the guarantee, and the reasons for its decision; and

- (4) the independent non-executive directors' opinion:
- (a) whether the connected person has fulfilled its obligations; and
  - (b) whether the group's decision to exercise or not to exercise any options or rights set out in rule 14A.64(3) is fair and reasonable and in the interests of the shareholders as a whole.

*When a proposed transaction becomes connected*

14A.61, 14A.62 14A.65 If a connected transaction is also a notifiable transaction, the issuer must also comply with the requirements in Chapter 14.

14A.66 If an issuer has entered into an agreement for a proposed transaction which is conditional on shareholders' approval in general meeting and the proposed transaction becomes a connected transaction before the shareholders' approval, the issuer must comply with the connected transaction requirements. Where a notice of meeting to approve the proposed transaction has been sent to shareholders, the issuer must issue a further announcement and a supplementary circular to disclose that the transaction has become a connected transaction and the parties that are required to abstain from voting. The circular must also contain information required for a connected transaction circular.

*Checklists*

14A.09 14A.67 The issuer must complete and submit any checklists for connected transactions prescribed by the Exchange from time to time.

**CONTENT REQUIREMENTS**

14A.68 This section sets out the information that an issuer must disclose in its announcements, circulars and annual reports.

**Announcements**

14A.69 An announcement for a connected transaction must contain at least:

14A.56(1) (1) the information set out in rules 14.58 to 14.60 (contents of announcements for notifiable transactions);

14A.56(2) (2) the connected relationship between the parties to the transaction, and the connected person's interests in the transaction;

14A.56(1) (3) the independent non-executive directors' views on the transaction matters set out in rule 14A.40 if no shareholders' approval is required. ~~This includes whether the transaction is on normal commercial terms, whether its terms are fair and reasonable, and whether it is in the interests of the issuer and its shareholders as a whole;~~

14A.56(4) (4) if the transaction is a continuing connected transaction, the amount of its cap. If a circular is not required, the issuer should also disclose how it determines and calculates the cap, including the assumptions and the amounts of previous transactions which form the basis of the cap;

- 14A.73(2) (5) if the transaction is a qualified property acquisition exempt from the shareholders' approval requirement (see rule 14A.104):
- (a) the details of the acquisition;
  - (b) the details of the joint venture, including its terms and status, its dividend and distribution policy, its financial and capital commitment, and the issuer's share in it; and
  - (c) information to demonstrate that the exemption conditions have been met;
- 14A.56(5) (6) if the transaction involves the group acquiring assets from a connected person, the original acquisition cost of the assets to the connected person;
- 14A.56(6) (7) if the transaction involves the group disposing of assets which it has held for 12 months or less, the group's original acquisition cost of the assets;
- FAQ Series 9 No. 22
- 14A.56(8) (8) if the announcement contains a profit forecast of the group or a company which is, or will become, the issuer's subsidiary, the information set out in rule 14.62 (requirements for profit forecast in notifiable transaction announcement);
- 14A.56(9) (9) if no circular is required, a statement whether any directors of the issuer have a material interest in the transaction and, if so, whether they have abstained from voting on the board resolution;
- 14A.56(3) (10) a statement that the transaction is subject to independent shareholders' approval, if applicable;
- 14A.56(7) (11) if the transaction is, or will be, approved by way of shareholders' written approval, details of the shareholders giving the approval (including their names and shareholdings in the issuer) and the relationship between the shareholders; and
- 14A.56(10) (12) if a circular is required, the expected date of distribution of the circular, and, if this is more than 15 business days after the publication of the announcement, the reasons why this is so.

### Circulars

14A.70 A circular for a connected transaction must:

- 14A.58(1) (1) provide a clear and adequate explanation of its subject matter and demonstrate the advantages and disadvantages of the transaction for the group;
- 14A.58(2) (2) where practicable, include a numerical evaluation;
- 14A.58(3)(a) (3) contain all information necessary to allow the issuer's shareholders to make a properly informed decision; and
- 14A.58(3)(b) (4) contain a heading drawing attention to the importance of the document and advising shareholders who are in any doubt to consult appropriate independent advisers on the appropriate course of action.

14A.71 The circular must contain at least:

- 14A.59(1) (1) the Exchange's disclaimer statement (see rule 14.88) on its front cover or inside front cover;
- 14A.59(2)(a), (b), (c), (f), (13) to (16) (2) the information required to be disclosed in the announcement for the transaction;
- 14A.59(2)(a) (3) the identity and activities of the parties to the transaction and their ultimate beneficial owner(s);
- 14A.59(2)(d), (e) (4) the name of the connected person concerned, his/its relationship with any controller and the name and office held by that controller;
- 14A.59(9) (5) if the transaction is a continuing connected transaction, how the issuer determines and calculates the cap, including the assumptions and the amounts of previous transactions which form the basis of the cap;
- FAQ Series 9 No. 21
- 14A.59(7), (8) (6) a letter from each of the independent financial adviser and, if applicable, the independent board committee containing its opinion and recommendation on the transaction (see rules 14A.43 and 14A.45);
- 14A.59(6), 14A.73(3) (7) if the transaction involves the acquisition or disposal of any property interests or a company whose assets consist solely or mainly of property, a valuation and information on the property if required under rule 5.03. This rule does not apply to property acquired under a qualified property acquisition;
- FAQ Series 7 No. 54
- 14A.59(6) (8) if the primary significance of the asset (except for property interests) being acquired or disposed of is its capital value, an independent valuation of the asset;
- FAQ Series 7 No. 55 and 56
- 14A.59(17) (9) if the transaction involves an acquisition or disposal of a company or business engaging in an infrastructure project, a business valuation report on that company or business and/or traffic study report on the project. The report(s) must clearly set out:
- (a) all significant underlying assumptions including the discount rate or growth rate used; and
- (b) a sensitivity analysis based on different discount rates and growth rates.
- If the business valuation is based on a profit forecast, the accounting policies and calculations for the underlying forecasts must be examined and reported on by the auditors or reporting accountants. Any financial adviser mentioned in the circular must also report on the underlying forecasts.
- 14A.59(10) (10) if the transaction involves the group acquiring a company or business from a connected person, details of:
- (a) any guarantee of the profits or net tangible assets or other matters regarding the financial performance of the company or business provided by the connected person, and a statement by the issuer that it will comply with the disclosure requirements (see rule 14A.64) if the actual amount is less than the amount guaranteed.

- (b) any option granted to the group to sell the company or business back to the connected person and/or other rights given to the group;
- 14A.59(18) (11) a statement whether any directors of the issuer have a material interest in the transaction and, if so, whether they have abstained from voting on the board resolution;
- 14A.59(5) (12) a statement that any shareholder with a material interest in the transaction will not vote and the information required in rule 2.17;
- 14A.59(3) (13) the information set out in the following paragraphs of Appendix 1, Part B:
- 1 — issuer's name
  - 2 — directors' responsibility
  - 5 — expert statements
  - 10 — securities to be issued (if applicable)
  - 29(2) — requirements if there is a profit forecast
  - 32 — no material adverse change
  - 39 — directors' service contracts
  - 40 — directors' interests in assets
  - 43(2)(a) & (c) — documents on display
- 14A.59(4) (14) information regarding directors' and chief executive's interests in the issuer described in paragraphs 34 and 38 of Appendix 1, Part B, and Practice Note 5;
- 14A.59(11) (15) information regarding the competing interests of each of the group's directors and his associates as would be required to be disclosed under rule 8.10 as if each of them was a controlling shareholder; and
- 14A.59(19) (16) any additional information requested by the Exchange.

FAQ Series 1 No. 54

### Annual reports

- 14A.45, 14A.46 14A.72 The issuer's annual report must contain the following information on the connected transactions conducted in that financial year (including continuing connected transactions under agreements signed in previous years):
- (1) the transaction date;
  - (2) the parties to the transaction and a description of their connected relationship;
  - (3) a brief description of the transaction and its purpose;
  - (4) the total consideration and terms;
  - (5) the nature of the connected person's interest in the transaction;
  - (6) for continuing connected transactions,
    - (a) a confirmation from the issuer's independent non-executive directors on the matters set out in rule 14A.56; and
    - (b) a statement from the issuer's board of directors whether the auditors have confirmed the matters set out in rule 14A.57.
- 14A.37, 14A.38

14A.73 When the issuer discloses in its annual report information of any related party transaction under the accounting standards for preparing its financial statements, it must specify whether the transaction is a connected transaction under this Chapter and whether it has complied with the requirements in this Chapter.

### EXEMPTIONS

14A.74 Exemptions from the connected transaction requirements are available for the following types of transactions:

- (1) de minimis transactions (rule 14A.77);
- (2) financial assistance (rules 14A.88 to 14A.91A);
- (3) issues of new securities by the issuer or its subsidiary (rule 14A.92);
- (4) dealings in securities on stock exchanges (rule 14A.93);
- (5) repurchases of securities by the issuer or its subsidiary (rule 14A.94);
- (6) directors' service contracts and insurance (rules 14A.95 and 14A.95A);
- (7) buying or selling of consumer goods or services (rules 14A.96);
- (8) sharing of administrative services (rule 14A.97) ;
- (9) ~~transactions with persons connected with insignificant subsidiaries (rules 14A.98 to 14A.101);~~  
transactions with connected persons at the subsidiary level (rules 14A.101A and 14A.101B);
- (10) transactions with associates of passive investors (rules 14A.102 and 14A.103); and
- (11) qualified property acquisitions (rules 14A.104 to 14A.106).

Proposal K

Proposal K

Proposal C(1)

Proposal A(2)

14A.75 The exemptions are broadly divided into two categories: (1) fully exempt from shareholders' approval, annual review and all disclosure requirements; and (2) exempt from shareholders' approval requirement.

14A.76 The Exchange has the power to specify that an exemption will not apply to a particular transaction.

## De minimis transactions

14A.77 This exemption applies to a connected transaction (other than an issue of new securities by the issuer) conducted on normal commercial terms.

14A.31(2),  
14A.33(3),  
14A.65(2)(b)

- (1) The transaction is fully exempt if all the percentage ratios (other than the profits ratio) are:
  - (a) less than 0.1%;
  - (b) less than 1% and the transaction is a connected transaction only because it involves connected person(s) at the subsidiary level; or
  - (c) less than 5% and the total consideration (or in the case of any financial assistance, the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity) is less than HK\$1,000,000.

14A.32,  
14A.34,  
14A.66(2)

- (2) The transaction is exempt from circular (including independent financial advice) and shareholders' approval requirements if all the percentage ratios (other than the profits ratio) are:
  - (a) less than 5%; or
  - (b) less than 25% and the total consideration (or in the case of any financial assistance, the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity) is less than HK\$10,000,000.

### *Percentage ratio calculations*

14A.78 The methods of percentage ratio calculations set out in Chapter 14 (notifiable transactions) also apply to connected transactions in this Chapter subject to the modifications described rules 14A.79 to 14A.80.

14A.33(3)

14A.79 For continuing connected transactions, the issuer should calculate the assets ratio, revenue ratio and consideration ratio using the annual cap as the numerator. If the agreement for the transaction covers over 1 year, the transaction will be classified based on the largest annual cap during the term of the agreement.

FAQ Series 7  
No. 46 to 48

14A.68

14A.80 The following applies when calculating percentage ratios for connected transactions involving options:

14A.69(1)

- (1) if the group grants an option to a connected person and the group does not have discretion to exercise the option, it is classified as if the option has been exercised. The percentage ratios are calculated based on the consideration for the transaction (which includes the premium and the exercise price of the option), the value of the underlying assets, and the revenue attributable to the assets (See rule 14A.62 for the disclosure requirement when the option holder exercises or transfers the option, or when the option expires.);

14A.70(1)

- (2) if the group acquires or accepts an option granted by a connected person where the group has discretion to exercise the option, it is classified based on the amount of the premium payable by the group. However, if the premium represents 10% or more of the sum of the premium and the exercise price, the transaction will be classified as if the option has been exercised (see rule 14A.80(1));

14A.70(2)

- (3) if the group exercises an option granted by a connected person, it is classified based on the exercise price, the value of the underlying assets, and the revenue attributable to the assets. If the option is exercised in stages, the Exchange may require aggregation of the transactions;

14A.70(3)

- (4) if the group transfers an option granted by a connected person to a third party, terminates the option or decides not to exercise the option;

Proposal G(2)

(a) it is classified as if the option has been exercised. The percentage ratios are calculated based on the exercise price, the value of the underlying assets, and the revenue attributable to the assets, and (if applicable) the premium for transferring the option, or the amount receivable or payable by the group for terminating the option;

(b) the Exchange may allow the issuer to disregard the percentage ratios calculated under paragraph (a) above and to classify the transaction using the asset and consideration ratios calculated based on the higher of:

Proposals  
G(1) and G(2)

(i) the difference between the exercise price and the value of the assets subject to the option; and

(ii) any amount payable or receivable by the group.

These alternative tests would be allowed only if the assets' valuation is provided by an independent expert using generally acceptable methodologies, and the issuer's independent non-executive directors and an independent financial adviser have confirmed that the transfer, termination or non-exercise of the option is fair and reasonable and in the interests of the issuer and its shareholders as a whole. In any event, the issuer must announce the transfer, termination or non-exercise of the option with the views of the independent non-executive directors and the independent financial adviser; and

14A.71

- (5) if the actual monetary value of the premium, the exercise price, the value of the underlying assets and the revenue attributable to the assets have not been determined when the group grants or acquires/accepts the option:

(a) the issuer must demonstrate to the Exchange's satisfaction the highest possible monetary value for calculating the percentage ratios and classifying the transaction. If the issuer is unable to do so, it may be required to comply with all the connected transaction requirements for the transaction; and

(b) the issuer must inform the Exchange when the actual monetary value has been determined. If the transaction falls under a higher classification based on the actual monetary value, the issuer must as soon as reasonably practicable announce this fact and comply with the requirements applicable to the higher classification.

*Note: The requirements in this rule are the same as the requirements applicable to options under Chapter 14 (notifiable transactions), except that*

1. *Under Chapter 14, the issuer may, at the time of the group acquiring or accepting an option granted by a third party, seek shareholders' approval for its exercise of the option in the future. This is not allowed under this Chapter.*
2. *Under Chapter 14, transfer or termination of an option by the group is a transaction which is classified based on the consideration for transferring the option or the amount receivable or payable by the group. Under this Chapter, the transfer or termination is classified as if the option is exercised.*
3. *Non-exercise of an option is not a transaction under Chapter 14.*

Proposals  
G(1) and G(2)

*Exception to percentage ratio calculations*

FAQ Series 7  
No. 45

- 14A.81 If any percentage ratio produces an anomalous result or is inappropriate to the activity of the issuer, the Exchange may disregard the ratio and consider alternative test(s) provided by the issuer. The issuer should seek prior consent of the Exchange if it wishes to apply this rule.

*Aggregation of transactions*

14A.25

- 14A.82 The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they were all entered into or completed within a 12-month period or are otherwise related. The issuer must comply with the applicable connected transaction requirements based on the classification of the connected transactions when aggregated. The aggregation period will cover 24 months if the connected transactions are a series of acquisitions of assets being aggregated which may constitute a reverse takeover.

14A.26

- 14A.83 Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:
- (1) they are entered into by the group with the same party, or parties who are connected with one another;
  - (2) they involve the acquisition or disposal of parts of one asset, or interests in a company or group of companies; or
  - (3) they together lead to substantial involvement by the group in a new business activity.

14A.27

- 14A.84 The Exchange may aggregate all continuing connected transactions with a connected person.

14A.27A

- 14A.85 An issuer must consult the Exchange before the group enters into any connected transaction if:
- (1) the transaction and any other connected transactions entered into or completed by the group in the last 12 months fall under any of the circumstances described in rule 14A.83; or
  - (2) the transaction and any other transactions entered into by the group involve the acquisition of assets from a person or group of persons or any

of their associates within 24 months after the person(s) gain control (as defined in the Takeovers Code) of the issuer.

14A.86 The issuer must provide information to the Exchange on whether it should aggregate the transactions.

14A.87 The Exchange may aggregate an issuer's connected transactions even if the issuer has not consulted the Exchange.

### Financial assistance

#### *Financial assistance provided by the group*

LD76-1,  
FAQ Series 1  
No. 55

14A.88 For any financial assistance provided by a banking company in its ordinary and usual course of business to a connected person or commonly held entity:

(1) the transaction is fully exempt if it is conducted on normal commercial terms (or better to the banking company);

(2) the transaction is fully exempt if it is not conducted on normal commercial terms (or better to the banking company) but all the percentage ratios (other than the profits ratio) are:

(a) less than 0.1%;

(b) less than 1% and the transaction is a connected transaction only because it involves connected person(s) at the subsidiary level; or

(c) less than 5% and the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity is less than HK\$1,000,000; or

(3) the transaction is exempt from circular (including independent financial advice) and shareholders' approval requirements if it is not conducted on normal commercial terms (or better to the banking company) but all the percentage ratios (other than the profits ratio) are:

(a) less than 5%; or

(b) less than 25% and the total value of the financial assistance plus any monetary advantage to the connected person or commonly held entity is less than HK\$10,000,000.

14A.65(1)

14A.65(2)(a)

14A.66(1)

14A.10(1)

14A.89 A "banking company" is an issuer or its subsidiary which is a bank, a restricted licence bank or a deposit taking company as defined in the Banking Ordinance, or a bank under an appropriate overseas authority.

- 14A.65(3) 14A.90 Financial assistance provided by a group to a connected person or commonly held entity is fully exempt if it is conducted:
- (1) on normal commercial terms (or better to the group); and
  - (2) in proportion to the equity interest directly held by the issuer or its subsidiary in the connected person or the commonly held entity. Any guarantee given by the group must be on a several (and not a joint and several) basis.

*Financial assistance received by the group*

- 14A.65(4) 14A.91 Financial assistance received by a group from a connected person or commonly held entity is fully exempt if:
- (1) it is conducted on normal commercial terms (or better to the group); and
  - (2) it is not secured by the group's assets.

*The group providing indemnity for a director*

Proposal K
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14A.91A Providing an indemnity for a director of the issuer or its subsidiaries is fully exempt if:

- (1) the indemnity is for liabilities that may be incurred in the course of the director performing his duties; and
- (2) the indemnity is in a form permitted under the laws of the jurisdictions where the company providing the indemnity is incorporated.

**Issue of new securities by an issuer or its subsidiary**

- 14A.92 An issue of new securities by an issuer or its subsidiary to a connected person is fully exempt if:
- 14A.31(3)(a) (1) the connected person receives a pro rata entitlement to the issue as a shareholder;
  - (2) the connected person subscribes for the securities in a rights issue or open offer:
    - 14A.31(3)(c) – N2 (a) through excess application (see rule 7.21(1) or 7.26A(1)); or
    - 14A.31(3)(c) (b) in his/its capacity as an underwriter or sub-underwriter of the rights issue or open offer, and rule 7.21 or 7.26A (arrangements to dispose of any excess securities) has been complied with. In this case, the listing document must contain the terms and conditions of the underwriting arrangement;
    - 14A.31(3)(c) – N1

*Note: Any commission and fees payable by the group to the connected person for the underwriting arrangement are not exempt under this exemption.*

14A.31(3)(b)

- (3) the securities are issued to the connected person under:
- (a) a share option scheme that complies with Chapter 17; or
  - (b) a share option scheme adopted by the issuer before its securities first start dealing on the Exchange, and where the Exchange has approved the listing of the securities to be issued under the scheme; or

14A.31(3)(d)

- (4) the securities are issued under a “top-up placing and subscription” that meets the following conditions:
- (a) the new securities are issued to the connected person:
    - (i) after it has reduced its holding in the same class of securities by placing them to independent third parties under a placing agreement; and
    - (ii) within 14 days from the date of the placing agreement;
  - (b) the number of new securities issued to the connected person does not exceed the number of securities placed by it; and
  - (c) the new securities are issued at a price not less than the placing price. The placing price may be adjusted for the expenses of the placing.

*Note: An issue of new securities by a subsidiary of the issuer may be fully or partially exempt as a de minimis transaction.*

#### **Dealings in securities on stock exchanges**

14A.31(4)

14A.93

Dealing in securities of a target company (i.e. a connected transaction described in rule 14A.25) by the group is fully exempt if it meets the following conditions:

- (1) the dealing in the securities is conducted as part of the group’s ordinary and usual course of business;
- (2) the securities are listed on the Exchange or a recognised stock exchange;
- (3) the dealing is carried out on the Exchange or a recognised stock exchange, or if not, no consideration passes to or from a connected person; and
- (4) the transaction is not made for the purpose of conferring a direct or indirect benefit upon any connected person who is a substantial shareholder of the target company.

## Repurchases of own securities

- 14A.31(5) 14A.94 Repurchases of own securities by an issuer or its subsidiary from a connected person is fully exempt if it is made:
- (1) on the Exchange or a recognised stock exchange, except where the connected person knowingly sells the securities to the group; or
  - (2) in a general offer made under the Code on Share Repurchases.

## Service contracts and insurance for directors

- 14A.31(6) 14A.95 A director entering into a service contract with the issuer or its subsidiary is fully exempt.

LD 76-4

- ~~14A.95A~~ ~~Purchase and maintenance of insurance for a director of the issuer or its subsidiaries against liabilities to third parties that may be incurred in the course of performing his duties are fully exempt if it is in the form permitted under the laws of the jurisdictions where the company purchasing the insurance is incorporated.~~

Proposal K

## Buying or selling consumer goods or consumer services

- 14A.31(7),  
14A.33(1) 14A.96 A group buying consumer goods or services as a customer from, or selling consumer goods or services to, a connected person on normal commercial terms in the ordinary and usual course of business is fully exempt if it meets the following conditions:

- (1) the goods or services must be of a type ordinarily supplied for private use or consumption;
- (2) they must be for the buyer's own consumption or use, and not be:
  - (a) processed into the buyer's products, or for resale; or
  - (b) used by the buyer for any of its businesses or contemplated businesses. This condition does not apply if the group is the buyer and there is an open market and transparency in the pricing of the goods or services;
- (3) they must be consumed or used by the buyer in the same state as when they were bought; and
- ~~(4) the total consideration or value of the goods or services must be less than 1% of the group's total revenue or total purchases, as published in its latest audited accounts; and~~
- ~~(4)~~ (4) the transaction must be made on no more favourable terms to the connected person, or no less favourable terms to the group than those available from independent third parties.

Proposal J

*Note: Examples of consumer goods and services are:*

- (1) *Meals consumed by a director at a restaurant owned by the group.*
- (2) *A director buying groceries for his own use at a retail store operated by the group.*
- (3) *Utilities provided by the group to a director's apartment.*

- (4) *Utilities provided by a connected person to the group where the prices are published or publicly quoted and apply to other independent consumers.*

#### **Shared administrative services**

14A.31(8),  
14A.33(2)

14A.97 Administrative services shared between the group and a connected person on a cost basis are fully exempt, provided that the costs are identifiable and are allocated to the parties involved on a fair and equitable basis.

*Note: Examples of shared administrative services are shared secretarial, legal and staff training services.*

#### **Transactions with persons connected with insignificant subsidiaries**

Proposal C(1)

14A.31(9),  
14A.33(4)

14A.98 ~~A connected transaction on normal commercial terms is fully exempt if it meets the following conditions:~~

- ~~(1) it is a connected transaction because it involves a person who is connected solely because of his/its relationship with the issuer's insignificant subsidiary/subsidiaries; and~~
- ~~(2) the consideration ratio of the transaction is less than 10%. This condition applies only if:~~
- ~~(a) the subsidiary (or any of its subsidiaries) is a party to the transaction, or the securities or assets of the subsidiary (or any of its subsidiaries) are the subject of the transaction; and~~
- ~~(b) the transaction is of a capital nature.~~

14A.31(9),  
14A.33(4)

14A.99 ~~An "insignificant subsidiary" is the issuer's subsidiary whose total assets, profits and revenue are less than:~~

- ~~(1) 10% under the percentage ratios for each of the latest three financial years (or if less, the period since the incorporation or establishment of the subsidiary); or~~
- ~~(2) 5% under the percentage ratios for the latest financial year.~~

14A.100 ~~If the person is connected with two or more subsidiaries of the issuer, the Exchange will aggregate the subsidiaries' total assets, profits and revenue to determine whether they are together "insignificant subsidiaries" of the issuer.~~

14A.101 ~~When calculating the percentage ratios, 100% of the subsidiaries' total assets, profits and revenue will be used. If the percentage ratio produces an anomalous result, the Exchange may disregard the calculation and consider alternative test(s) provided by the issuer.~~

#### **Transactions with connected persons at the subsidiary level**

14A.101A A connected transaction between the group and a connected person at the subsidiary level on normal commercial terms is exempt from the circular (including independent financial advice) and shareholders' approval requirements.

Proposal  
A(2)(a)

14A.101B A connected transaction between the group and a connected person at the subsidiary level on normal commercial terms is fully exempt if:

- (1) the transaction is a connected transaction only because of the person's relationship with the issuer's subsidiary/subsidiaries; and
- (2) the subsidiary (or any of its subsidiaries) is not a party to the transaction.

#### **Transactions with associates of passive investors**

14A.31(10),  
14A.33(5)

14A.102 A connected transaction conducted between the group and an associate of a passive investor is fully exempt if it meets the following conditions:

- (1) the passive investor is a connected person only because it is a substantial shareholder of the issuer and/or any of its subsidiaries;
- (2) the passive investor
  - (a) is not a controlling shareholder of the issuer or its subsidiaries;
  - (b) does not have any representative on the board of directors of the issuer or its subsidiaries, and is not involved in the management of the group, including any influence over the group's management through negative control (e.g. its veto rights) on material matters of the group;
  - (c) is independent of the directors, chief executive, controlling shareholder(s) and any other substantial shareholder(s) of the issuer or its subsidiaries; and
- (3) the transaction is of a revenue nature in the group's ordinary and usual course of business, and conducted on normal commercial terms.

14A.103 A "passive investor" is a substantial shareholder of the issuer and/or any of its subsidiaries that:

- (1) is a sovereign fund, or a unit trust or mutual fund authorised by the Securities and Futures Commission or an appropriate overseas authority; and
- (2) has a wide spread of investments other than the securities of the group and the associate that enters into the transaction with the group.

#### **Qualified property acquisitions**

14A.72

14A.104 The formation of a joint venture by a qualified issuer and a qualified connected person to make a qualified property acquisition is exempt from shareholders' approval requirements if:

- (1) the project will be single purpose, relating to the acquisition and/or development of a specific property, and consistent with the purpose specified in the auction or tender document;
- (2) the joint venture arrangement is on an arm's length basis and on normal commercial terms;
- (3) the joint venture agreement contains clause(s) to the effect that the joint venture may not, without its partners' unanimous consent:

- (a) change the nature or scope of its business, and, if there are changes, they must be consistent with the scope or purpose specified in the auction or tender document; or
  - (b) enter into any transactions which are not on an arm's length basis; and
- (4) the independent board committee and independent financial adviser have confirmed that:
- (a) the acquisition is in the group's ordinary and usual course of business; and
  - (b) the acquisition and the joint venture, including its financing and profit distribution arrangements, are on normal commercial terms, are fair and reasonable and in the interests of the issuer and its shareholders as a whole.

14A.10(10A) 14A.105 A qualified connected person is a connected person of the qualified issuer solely because he/it is a substantial shareholder (or its associate) in one or more of the qualified issuer's non wholly-owned subsidiaries formed to participate in property projects, each of which is single purpose and project specific. This person may or may not have representation on the board of the subsidiary/subsidiaries.

14A.73(1),  
14A.73(2) –  
Note 14A.106 The issuer shall announce the transaction as soon as practicable after receiving notification of the success of the bid by the joint venture. If any details of the acquisitions or the joint venture required to be disclosed are not available when the issuer publishes the initial announcement, it must publish subsequent announcement(s) to disclose the details as soon as practicable after they have been agreed or finalized.

#### WAIVERS

14A.07,  
14A.44 14A.107 The Exchange may waive any requirements under this Chapter in individual cases, subject to any conditions that it may impose.

#### Transactions relating to non-executive directors

14A.108 The Exchange may waive the circular and shareholders' approval requirements for a connected transaction with a non-executive director of the issuer or its subsidiaries if:

- 14A.42(1)
- (1) the transaction is connected only because of the interest of a non-executive director;
  - (2) the director does not control the group, and his principal business interest is not the group; and
  - (3) the issuer's auditor or an acceptable financial adviser has given the opinion that the transaction is fair and reasonable to the shareholders as a whole.

**Provision of guarantees to connected subsidiaries or commonly held entities  
for public sector contracts awarded by tender**

- 14A.42(2) 14A.109 The Exchange may waive all or some of the connected transaction requirements for a joint and several guarantee or indemnity provided by the group to a third party creditor for the obligations of a connected subsidiary or a commonly held entity if:
- (1) the guarantee/indemnity is required for a government or public sector contract awarded by tender;
  - (2) each of the other shareholders of the connected subsidiary or commonly held entity has given a similar joint and several guarantee or indemnity to the third party creditor; and
  - (3) each of the other shareholders of the connected subsidiary or commonly held entity has agreed to indemnify the group for the liability guaranteed, or indemnified at least in proportion to its equity interest in the subsidiary or entity. The issuer must satisfy the Exchange that such shareholder indemnity is sufficient.

**Continuing connected transactions of new applicants**

- 14A.42(3) 14A.110 The Exchange may waive the announcement, circular and shareholders' approval requirements for continuing connected transactions entered into by a new applicant or its subsidiaries. The new applicant must disclose in the listing document its sponsor's opinion on whether the transactions are in the group's ordinary and usual course of business, on normal commercial terms, are fair and reasonable and in the interests of the shareholders as a whole.

**Written agreement for continuing connected transactions**

14A.110A The Exchange may waive the requirement under rule 14A.34 if the issuer can demonstrate to the Exchange's satisfaction that it is impracticable or unduly burdensome for the group to enter into a written agreement for continuing connected transactions. Factors which the Exchange will consider include the issuer's relationship with the connected person, and the nature of the continuing connected transactions including whether they are of a revenue nature in the group's ordinary and usual course of business and the frequency or regularity of transactions. The issuer must satisfy the following conditions:

Proposal F(1)

- (1) the issuer must seek a mandate for the transactions from its shareholders (or from its board if the transactions are exempt from the shareholders' approval requirement);
- (2) the mandate period must not exceed 3 years;
- (3) the issuer must comply with all the connected transaction requirements which are applicable to continuing connected transactions conducted under a written agreement. The issuer's announcement and, if applicable, circular must disclose the terms of the mandate which must include a framework for determining the terms of the transactions; and
- (4) the issuer must re-comply with the announcement and shareholders' approval requirements if it proposes to renew the mandate or effect a material change to its terms.

## DEFINITIONS

14A.111 In this Chapter, the following definitions apply:

- (1) a “**30%-controlled company**” means a company held by a person who can:
  - (a) exercise or control the exercise of 30% (or an amount for triggering a mandatory general offer under the Takeovers Code, or for PRC issuers only, an amount for triggering a mandatory general offer or establishing legal or management control over a business enterprise under the PRC law) or more of the voting power at general meetings; or
  - (b) control the composition of a majority of the board of directors;
- (2) an “**associate**” has the meaning in rules 14A.09 to 14A.12;
- (3) a “**banking company**” has the meaning in rule 14A.89;
- (4) a “**closely allied group of shareholders**” has the meaning in rule 14.45;
- (5) a “**commonly held entity**” has the meaning in rule 14A.24;
- (6) a “**connected person**” has the meaning in rules 14A.05 to 14A.08;
- (7) a “**connected person at the issuer level**” includes
  - (a) a director, chief executive, substantial shareholder of an issuer;
  - (b) a supervisor of a PRC issuer;
  - (c) a person who was a director of the issuer in the last 12 months; or
  - (d) an associate of any of the above persons;
- (8) a “**connected person at the subsidiary level**” means a person who is a connected person only because of the person’s connection with the issuer’s subsidiary or subsidiaries;
- (9) a “**connected subsidiary**” has the meaning in rule 14A.13;
- (10) a “**connected transaction**” has the meaning in rules 14A.22 to 14A.31;
- (11) a “**continuing connected transaction**” has the meaning in rule 14A.31;
- (12) a “**controller**” has the meaning in rule 14A.25(1);

14A.10(13)(a)

- (13) a “**deemed disposal**” has the meaning in rule 14.29;
- (14) a company is “**directly held**” by an individual or an entity means that the individual or the entity has a direct ownership interest in the company;
- (15) a “**family member**” has the meaning in rule 14A.09(2)(a);
- (16) “**financial assistance**” has the meaning in rule 14A.21(4);
- (17) “**financial assistance provided in the ordinary and usual course of business**” means financial assistance provided by a banking company;

14A.10(6), (7)

- (18) a “**group**” means an issuer and its subsidiaries, or any of them;
- (19) an “**immediate family member**” has the meaning in rule 14A.09(1)(a);
- (20) a company is “**indirectly held**” by an individual or an entity means that the individual or the entity has an indirect ownership interest in the company through (in the case of an individual) his majority controlled company/ companies or (in the case of an entity) its subsidiary/ subsidiaries;
- (21) an “**insignificant subsidiary**” or “**insignificant subsidiaries**” has the meaning in rule ~~14A.06A-14A.99 to 14A.101~~;

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14A.10(6), (7)

- (22) an “**issuer**” means a company or other legal person whose securities (including depositary receipts) are listed;
- (23) a “**majority-controlled company**” means a company held by a person who can exercise or control the exercise of more than 50% of the voting power at general meetings, or control the composition of a majority of the board of directors;
- (24) “**material interest**” in a transaction has the meaning in rules 2.15 and 2.16;
- (25) a “**monetary advantage**” has the meaning in rule 14.12;

14A.10(8)

- (26) “**normal commercial terms**” are terms which a party could obtain if the transaction were on an arm’s length basis or terms no less favourable to the group than terms available to or from independent third parties;

14A.67

- (27) an “**option**” and terms related to it (including “**exercise price**”, “**premium**” and “**expiration**”) have the meaning in rule 14.72;

14A.10(9)

- (28) “**ordinary and usual course of business**” of an entity means the entity’s existing principal activities or an activity wholly necessary for its principal activities;

- (29) a “**passive investor**” has the meaning in rule 14A.103;
- 14A.10(10) (30) “**percentage ratios**” has the meaning in rule 14.04(9);
- 14A.56(8) (31) a “**profit forecast**” has the meaning in rule 14.61;
- (32) a “**PRC Governmental Body**” has the meaning in rule 19A.04;
- 14A.10(10A) (33) a “**qualified connected person**” has the meaning in rule 14A.105;
- 14A.10(10B) (34) a “**qualified issuer**” has the meaning in rule 14.04(10B);
- 14A.10(10C) (35) a “**qualified property acquisition**” has the meaning in rule 14.04(10C);
- 14A.10(11) (36) a “**recognised stock exchange**” – a regulated, regularly operating, open stock market recognised for this purpose by the Exchange;
- (37) a “**relative**” has the meaning in rule 14A.18(1)(a);
- (38) a “**transaction**” has the meaning in rule 14A.21; and
- (39) a “**trustees**” has the meaning in rule 14A.09(1)(b) or 14A.10(2).

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**APPENDIX III: STATISTICAL ANALYSIS OF CONNECTED  
TRANSACTIONS ANNOUNCED BY ISSUERS  
IN 2011**

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1. This appendix analyses connected transactions announced by issuers before and after changes to the connected transaction Rules in 2010 in the following aspects:
  - Connected transactions subject to announcements and/or shareholder approval;
  - Nature of connected persons involved in the transactions; and
  - Nature of the connected transactions.

**(A) Connected transactions subject to announcement and/or shareholder approval**

2. In 2011, there were 1,877 connected transactions announced by issuers (2009: 2,033), representing a decrease of 8% from 2009. Table 1 below sets out the number of those connected transactions which were subject to announcement and/or shareholder approval requirements under Chapter 14A:

**Table 1: Connected transactions subject to announcement and/or shareholder approval requirements**

	<b>2011</b>		<b>2009</b>	
	<u>Number</u>	<u>%</u>	<u>Number</u>	<u>%</u>
<b>No. of connected transactions announced</b>				
- Subject to announcement <b>only</b>	1,255	66.9%	1,195	58.8%
- Subject to announcement and shareholder approval	622	33.1%	838	41.2%
	----- 1,877	100%	----- 2,033	100%
	=====		=====	
<b>No. of issuers involved</b>	584		602	
	=====		=====	
<b>No. of issuers at the beginning of the year</b>	1,413		1,261	
	=====		=====	

3. Table 2 below sets out a breakdown of the connected transactions which were also notifiable transactions under Chapter 14:

**Table 2: Connected transactions which were also notifiable transactions**

By notifiable transaction category	2011		2009	
	<u>Number</u>	<u>%*</u>	<u>Number</u>	<u>%*</u>
Share transactions	1	0.1%	-	-
Discloseable transaction	110	5.8%	173	8.5%
Major transaction	56	3.0%	247	12.1%
Very substantial acquisition/ very substantial disposal	31	1.6%	54	2.7%
Total	----- 198 =====	10.5%	----- 474 =====	23.3%

\* As a percentage of the total connected transactions announced during the year

**(B) Nature of the connected persons involved in the transactions**

4. Table 3 below shows the nature of connected persons involved in the connected transactions announced before and after the 2010 Rule changes:

**Table 3: Nature of connected persons involved in the connected transactions**

By nature of connected persons	2011		2009	
	<u>Number</u>	<u>%</u>	<u>Number</u>	<u>%</u>
Persons connected at the issuer level	1,574	83.8%	1,423	70.0%
Persons connected only at the subsidiary level	248	13.2%	507	24.9%
Others:				
- Connected subsidiaries	24	1.3%	52	2.6%
- Investment managers/ advisers or custodians of investment companies	13	0.7%	6	0.3%
- Commonly held entities	-	-	2	0.1%
- Third parties where the transactions fall under Rule 14A.13(1)(b)	13	0.7%	29	1.4%
- Third parties deemed to be connected by the Exchange	5	0.3%	14	0.7%
Total	----- 1,877 =====	100%	----- 2,033 =====	100%

5. Table 4 below provides further analysis of those transactions with persons connected at the issuer level:

**Table 4: Transactions with persons connected at the issuer level**

		<b>2011</b>		<b>2009</b>	
<b>(i)</b>	<b>Connected person's relationship with the issuer</b>	<b><u>Number</u></b>	<b><u>%*</u></b>	<b><u>Number</u></b>	<b><u>%*</u></b>
	Director of the issuer	162	8.6%	152	7.5%
	Substantial shareholder of the issuer	1,210	64.4%	1,069	52.6%
	Substantial shareholder (and also director) of the issuer	193	10.3%	145	7.1%
	Chief executive of the issuer	-	-	11	0.6%
	Former director of the issuer within the last 12 months	9	0.5%	17	0.8%
	Promoter of the issuer	- #	-	29	1.4%
		<u>1,574</u>	83.8%	<u>1,423</u>	70.0%
<p>* As a percentage of the total connected transactions announced during the year</p> <p># The 2010 Rule changes excluded promoters from the definition of connected person.</p>					
<b>(ii)</b>	<b>Nature of the transactions</b>	<b><u>Number</u></b>	<b><u>%</u></b>	<b><u>Number</u></b>	<b><u>%</u></b>
	Capital transactions (e.g. acquisitions, disposals, financial assistance, etc.)	521	33.1%	517	36.3%
	Revenue transactions	1,053	66.9%	906	63.7%
		<u>1,574</u>	100%	<u>1,423</u>	100%
<b>(iii)</b>	<b>Compliance with Chapter 14A requirements</b>	<b><u>Number</u></b>	<b><u>%</u></b>	<b><u>Number</u></b>	<b><u>%</u></b>
	Subject to announcement only	1,091	69.3%	820	57.6%
	Subject to announcement and shareholder approval requirements	483	30.7%	603	42.4%
		<u>1,574</u>	100%	<u>1,423</u>	100%

6. Table 5 below provides further analysis of those transactions with persons connected only at the subsidiary level:

**Table 5: Transactions with persons connected only at the subsidiary level**

		<b>2011</b>		<b>2009</b>	
<b>(i)</b>	<b>Connected person's relationship with the issuer's subsidiaries</b>	<b><u>Number</u></b>	<b><u>%*</u></b>	<b><u>Number</u></b>	<b><u>%*</u></b>
	Director of the subsidiary	27	1.4%	31	1.5%
	Substantial shareholder of the subsidiary	213	11.3%	449	22.1%
	Substantial shareholder (and also director) of the subsidiary	7	0.4%	21	1.0%
	Chief executive of the subsidiary	1	0.1%	1	0.0%
	Former director of the subsidiary within the last 12 months	-	-	3	0.2%
	Promoter of the subsidiary	- #	-	2	0.1%
		----- 248	13.2%	----- 507	24.9%
		=====		=====	
* As a percentage of the total connected transactions announced during the year					
# The 2010 Rule changes excluded promoters from the definition of connected person.					
<b>(ii)</b>	<b>Association between the connected person and the transacting subsidiary or its holding company</b>	<b><u>Number</u></b>	<b><u>%</u></b>	<b><u>Number</u></b>	<b><u>%</u></b>
	Connected persons had association with the transacting subsidiary or its holding company	90	36.3%	155	30.6%
	Connected persons had <u>no</u> association with the transacting subsidiary or its holding company	158	63.7%	352	69.4%
		----- 248	100%	----- 507	100%
		=====		=====	
<b>(iii)</b>	<b>Nature of the transactions</b>	<b><u>Number</u></b>	<b><u>%</u></b>	<b><u>Number</u></b>	<b><u>%</u></b>
	Capital transactions (e.g. acquisitions, disposals, financial assistance, etc.)	118	47.6%	246	48.5%
	Revenue transactions	130	52.4%	261	51.5%
		----- 248	100%	----- 507	100%
		=====		=====	

	2011		2009	
	<u>Number</u>	<u>%</u>	<u>Number</u>	<u>%</u>
<b>(iv) Compliance with Chapter 14A requirements</b>				
Subject to announcement only	131	52.8%	329	64.9%
Subject to announcement and shareholder approval	117	47.2%	178	35.1%
	-----		-----	
	248	100%	507	100%
	=====		=====	

**(C) Nature of connected transactions**

7. Table 6 below sets out a breakdown of the nature of connected transactions announced by issuers in 2011 and 2009:

**Table 6: Nature of connected transactions**

	2011		2009	
	<u>Number</u>	<u>%</u>	<u>Number</u>	<u>%</u>
<b>Capital transactions</b>				
Acquisitions	276	14.7%	374	18.4%
Disposals	142	7.6%	170	8.4%
Financial assistance	131	7.0%	104	5.1%
Issue of securities	41	2.2%	78	3.8%
Others (e.g. formation of joint venture, grant of options, redemption of convertible bonds)	69	3.6%	95	4.7%
	-----		-----	
	659	35.1%	821	40.4%
	-----		-----	
<b>Revenue transactions</b>				
Sales	161	8.6%	168	8.3%
Purchases	179	9.5%	195	9.6%
Leases	278	14.8%	226	11.1%
Others (e.g. provision or receipt of management, advisory or other services)	600	32.0%	623	30.6%
	-----		-----	
	1,218	64.9%	1,212	59.6%
	-----		-----	
<b>Total</b>	1,877	100%	2,033	100%
	=====		=====	

8. Table 7 below sets out the analysis of continuing connected transactions announced by issuers in 2011 and 2009:

**Table 7: Continuing connected transactions**

	<b>2011</b>		<b>2009</b>	
	<u>Number</u>	<u>%</u>	<u>Number</u>	<u>%</u>
<b>(i) Nature of continuing connected transactions</b>				
Revenue transactions	1,138	94.7%	1,143	97.9%
Financial assistance	64	5.3%	24	2.1%
	----- 1,202 =====	100%	----- 1,167 =====	100%
<b>(ii) Duration of agreements for continuing connected transactions</b>				
Less than 1 year	72	6.0%	39	3.4%
1 year or above, but less than 2 years	156	13.0%	176	15.1%
2 year or above, but less than 3 years	233	19.4%	166	14.2%
3 years	679	56.5%	725	62.1%
More than 3 years	62	5.1%	61	5.2%
	----- 1,202 =====	100%	----- 1,167 =====	100%

\* In 2011, 64% of these agreements (2009: 73%) were related to leases of properties.

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## **APPENDIX IV: PRIVACY POLICY STATEMENT**

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Hong Kong Exchanges and Clearing Limited and from time to time, its subsidiaries, affiliated companies controlling it or under common control with it and its joint ventures (each such entity, from time to time, being “**HKEx**”, “**we**”, “**us**” or an “**affiliate**” for the purposes of this Privacy Policy Statement as appropriate) recognises its responsibilities in relation to the collection, holding, processing, use and/or transfer of personal data under the Personal Data (Privacy) Ordinance (Cap. 486) (“PDPO”). Personal data will be collected only for lawful and relevant purposes and all practicable steps will be taken to ensure that personal data held by HKEx is accurate. HKEx will use your personal data in accordance with this Privacy Policy Statement.

We regularly review this Privacy Policy Statement and may from time to time revise it or add specific instructions, policies and terms. Where any changes to this Privacy Policy Statement are material, we will notify you using the contact details you have provided us with and, as required by the PDPO, give you the opportunity to opt out of these changes by means notified to you at that time. Otherwise, in relation to personal data supplied to us through the HKEx website, continued use by you of the HKEx website shall be deemed to be your acceptance of and consent to this Privacy Policy Statement.

If you have any questions about this Privacy Policy Statement or how we use your personal data, please contact us through one of the communication channels below.

HKEx will take all practicable steps to ensure the security of the personal data and to avoid unauthorised or accidental access, erasure or other use. This includes physical, technical and procedural security methods, where appropriate, to ensure that the personal data may only be accessed by authorized personnel.

Please note that if you do not provide us with your personal data (or relevant personal data relating to persons appointed by you to act on your behalf) we may not be able to provide the information, products or services you have asked for or process your request.

## **Purpose**

From time to time we may collect your personal data such as your name, mailing address, telephone number, email address and login name for the following purposes:

1. to process your applications, subscriptions and registration for our products and services;
2. to perform or discharge the functions of HKEx and any company of which HKEx is the recognised exchange controller (as defined in the Securities and Futures Ordinance (Cap. 571));
3. to provide you with our products and services and administer your account in relation to such products and services;
4. to conduct research and statistical analysis; and
5. other purposes directly relating to any of the above.

## **Direct marketing**

Except to the extent you have already opted out or in future opt out, we may also use your name, mailing address, telephone number and email address to send promotional materials to you and conduct direct marketing activities in relation to our financial services and information services, and related financial services and information services offered by our affiliates.

If you do not wish to receive any promotional and direct marketing materials from HKEx or do not wish to receive particular types of promotional and direct marketing materials or do not wish to receive such materials through any particular means of communication, please contact us through one of the communication channels below.

## **Identity Card Number**

We may also collect your identity card number and process this as required under applicable law or regulation, as required by any regulator having authority over us and, subject to the PDPO, for the purpose of identifying you where it is reasonable for your identity card number to be used for this purpose.

## **Transfers of personal data for direct marketing purposes**

Except to the extent you have already opted out or in future opt out, we may transfer your name, mailing address, telephone number and email address to our affiliates for the purpose of enabling our affiliates to send promotional materials to you and conduct direct marketing activities in relation to their financial services and information services.

## **Other transfers of personal data**

For one or more of the purposes specified above, the personal data may be:

1. transferred to our affiliates and made available to appropriate persons in our affiliates, in Hong Kong or elsewhere and in this regard you consent to the transfer of your data outside of Hong Kong; and
2. supplied to any agent, contractor or third party who provides administrative or other services to HKEx and/or any of our affiliates in Hong Kong or elsewhere.

## **How we use cookies**

If you access our information or services through the HKEx website, you should be aware that cookies are used. Cookies are data files stored on your browser. The HKEx website automatically installs and uses cookies on your browser when you access it. Two kinds of cookies are used on the HKEx website:

***Session Cookies:*** temporary cookies that only remain in your browser until the time you leave the HKEx website, which are used to obtain and store configuration information and administer the HKEx website, including carrying information from one page to another as you browse the site so as to, for example, avoid you having to re-enter information on each page that you visit. Session cookies are also used to compile anonymous statistics about the use of the HKEx website.

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The cookies used in connection with the HKEx website do not contain personal data. You may refuse to accept cookies on your browser by modifying the settings in your browser or internet security software. However, if you do so you may not be able to utilise or activate certain functions available on the HKEx website.

## **Compliance with laws and regulations**

You agree that HKEx and its affiliates may be required to retain, process and/or disclose your personal data in order to comply with applicable laws and regulations, or in order to comply with a court order, subpoena or other legal process, or to comply with a request by a government authority, law enforcement agency or similar body (whether situated in Hong Kong or elsewhere). You also agree that HKEx and its affiliates may need to disclose your personal data in order to enforce any agreement with you, protect our rights, property or safety, or the rights, property or safety of our affiliates and employees.

## **Corporate reorganisation**

As HKEx continues to develop its business, we may reorganise our group structure, undergo a change of control or business combination. In these circumstances it may be the case that your personal data is transferred to a third party who will continue to operate our business or a similar service under either this Privacy Policy Statement or a different privacy policy statement which will be notified to you. Such a third party may be located, and use of your personal data may be made, outside of Hong Kong in connection with such acquisition or reorganisation.

## **Access and correction of personal data**

Under the PDPO, you have the right to ascertain whether HKEx holds your personal data, to obtain a copy of the data, and to correct any data that is inaccurate. You may also request HKEx to inform you of the type of personal data held by it. All data access requests shall be made using the form prescribed by the Privacy Commissioner for Personal Data (“**Privacy Commissioner**”) which may be found on the official website of the Office of the Privacy Commissioner.

Requests for access and correction or for information regarding policies and practices and kinds of data held by HKEx should be addressed in writing and sent by post to us (see contact details below).

A reasonable fee may be charged to offset HKEx's administrative and actual costs incurred in complying with your data access requests.

## **Termination or cancellation**

Should your account with us be cancelled or terminated at any time, we shall cease processing your personal data as soon as reasonably practicable following such cancellation or termination, provided that we may keep copies of your data as is reasonably required for archival purposes, for use in relation to any actual or potential dispute, for the purpose of compliance with applicable laws and regulations and for the purpose of enforcing any agreement we have with you, for protecting our rights, property or safety, or the rights, property or safety of our affiliates and employees.

## **Contact us**

By Post:

Personal Data Privacy Officer  
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1 Harbour View Street  
Central  
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By Email:

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