

**CONSULTATION CONCLUSION**  
PROPOSAL UNDER ISSUE 15 OF THE  
2008 COMBINED CONSULTATION PAPER

**July 2009**



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

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## EXECUTIVE SUMMARY

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1. This paper presents the results of a public consultation on our proposal to deal with self-construction of assets. We proposed to amend the notifiable transaction Rules to exclude any construction of fixed assets by an issuer for its own use in the ordinary and usual course of its business. For greater clarity, the proposal would not exempt issuers from the notifiable transaction Rules where the acquisition of a component of the self-constructed asset is in itself a transaction.
2. A majority of the respondents to the consultation supported our proposal. However, some respondents made substantive comments on the draft Rule amendments which defined “construction of a fixed asset by the issuer for its own use in the ordinary and usual course of business”. Some suggested expanding the proposed exemption to cover a wider scope of construction. Others commented that the draft Rules lacked clarity on how the aggregation requirements would apply to self-construction of assets, and that not exempting the acquired component of the constructed asset was contradictory to the proposal to exempt the self-construction project.
3. Having considered the responses, we decide to implement the proposal to exempt self-construction of assets and revise the Rule amendments to address the respondents’ comments. The revised Rules will disapply the aggregation requirements when an issuer enters into a series of transactions to construct, develop or refurbish an asset for its own use in its ordinary and usual course of business if the sole basis for aggregation is because the series of transactions form parts of one larger asset. We consider that the revised Rules will exempt self-construction of assets as nearly as practicable to the manner intended and discussed in the consultation paper.
4. We have finalised the Rule amendments to implement the proposal. They have been approved by the Board of The Stock Exchange of Hong Kong Limited and the Securities and Futures Commission, and will become effective on 1 September 2009.

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## PART A: INTRODUCTION

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5. On 11 January 2008, The Stock Exchange of Hong Kong Limited (**Exchange**), a wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited (**HKEx**), published a Combined Consultation Paper (**CCP**) on proposals to address 18 substantive policy issues including corporate governance and initial listing criteria, as well as some amendments to improve the clarity, certainty and efficacy of the Listing Rules.

6. The consultation period ended on 7 April 2008. We received a total of 105 submissions from a wide spectrum of respondents. A list of the respondents is provided in the Appendix.

7. The 105 respondents can be grouped into broad categories as follows:

Category	No. of respondents
Listed issuers	58
Professional and industry associations	15
Market practitioners	22
Statutory regulators	2
Individuals and retail investor representative	8
<b>Total</b>	105

8. Except for one respondent who requested the Exchange not to publish its submission, the full text of all the submissions is available on HKEx website at [http://www.hkex.com.hk/consul/response/combined\\_cp.htm](http://www.hkex.com.hk/consul/response/combined_cp.htm).

9. Of the 105 respondents, 61 expressed views on Issue 15 of the CCP. This paper presents the consultation conclusion on Issue 15. Part B of the paper summarizes the main points made by respondents on Issue 15 as well as our response to their comments and conclusion on how to proceed with the proposal. This paper should be read in conjunction with the CCP, a copy of which is posted on the HKEx website.

10. The Rule amendments for self-constructed assets are available on the HKEx website at “Regulatory Framework and Rules - Rules and Guidelines on Listing Matters - Listing Rule Update for Main Board Listing Rules” and “Regulatory Framework and Rules - Rules and Guidelines on Listing Matters - Listing Rule Update/Interpretation for GEM Listing Rules”. They have been approved by the Board of The Stock Exchange of Hong Kong Limited and the Securities and Futures Commission (**SFC**), and will become effective on 1 September 2009.

11. Unless otherwise specified, all the Rule amendments referred to in this paper apply to both the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (**Main Board Rules**) and the Rules Governing the Listing of Securities on the Growth Enterprise Market (**GEM Rules**) (together referred to as the **Listing Rules** or **Rules**).

12. We would like to thank all those who have shared with us their views and suggestions during the consultation process.

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## **PART B: MARKET FEEDBACK AND CONCLUSION**

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13. We set out below the main points made by respondents on Issue 15 as well as our response to their comments and conclusion on how to proceed with the proposal.

### *The proposal*

14. Under Issue 15, we proposed to amend the notifiable transaction Rules to exclude any construction of fixed assets by an issuer for its own use in the ordinary and usual course of its business. For greater clarity, the proposal would not exempt issuers from the notifiable transaction Rules where the acquisition of a component of the self-constructed asset is in itself a transaction.
15. The CCP also presented draft Rules to implement our proposal. These described the factors that the Exchange would consider in determining whether a fixed asset is constructed by an issuer for its own use in the ordinary and usual course of its business, including whether it i) has the expertise to undertake construction and ii) is most relevant and responsible for bringing the assets to the location and condition necessary for it to be capable of operating in the intended manner (**Original Proposed Rules**).

### *Comments received*

16. A majority of the respondents supported our proposal. However, we also received substantive comments on the Original Proposed Rules.
17. Seven respondents disagreed that the Original Proposed Rules would implement the proposal discussed in the CCP.
- One of the substantive comments was that the factors described in the draft rules for determining “self-constructed assets” were too narrow. Some respondents took the view that it should not matter whether the issuer was building the fixed asset itself or engaged a third party to build it as long as the issuer had the expertise to commission the building of the fixed asset and to provide the specification. Two respondents suggested expanding the proposed exemption to assets constructed by third parties for the issuer’s own use.
  - If the entire self-construction project were to be excluded from the definition of transaction, the acquisition of a component of the constructed asset should also be exempt. Our intention not to exempt the acquired component of the constructed asset (e.g. land) was viewed as contradictory to the proposal to exempt self-construction of assets. A respondent also noted that our intention to carve out the acquired component from the proposed exemption was not clearly reflected in the draft rules although cited in the CCP.
  - The draft rules did not clarify how the aggregation rules would apply to a series of transactions related to the self-construction of assets.

18. Following the consultation period, we sought further views from six interested groups (including respondents who gave substantive comments on Issue 15 and other market participants) on revising the Rule amendments to enable the implementation of the proposal discussed in the CCP. Three groups of participants supported revising the Rule amendments to disapply the aggregation requirements to self-construction of assets (see paragraph 21 below). The other groups expressed dissenting views as they continued to believe that the Rule amendments should provide an exemption for all self-used assets whether constructed by the issuers or third parties.

### *Our response*

19. We note that in the context of self-construction, there is a wide range in terms of an issuer's involvement in and control over the construction process, the risks it assumes and the degree of expertise it possesses. The terms of the construction contract are subject to negotiation and may vary significantly in respect of the same matter. While we proposed to exempt "self-construction" of assets, we have come to the view that there are significant difficulties in providing an unambiguous and clear definition of "self-construction" by issuers.
20. We also take note of the comment on how the aggregation rules may apply to self-construction of assets, and the anomaly arising from the Original Proposed Rules. The notifiable transaction framework treats each agreement for acquiring assets as a transaction. Self-construction of assets generally involves a series of transactions, and a self-constructed asset would be subject to the notifiable transaction requirements because the transactions are aggregated on the basis that they form parts of one asset. It is necessary and appropriate to amend the Rules to clarify how the aggregation requirements apply to self-construction of assets.
21. We have revised the Rule amendments to disapply the aggregation requirements when an issuer enters into a series of transactions to construct, develop or refurbish an asset for its own use in its ordinary and usual course of business if the sole basis for aggregation is because the series of transactions form parts of one larger asset (**Revised Rules**). Given the operation of the Revised Rules, it is not necessary to separately define and exclude "self-constructed assets" from the definition of "transaction" in the Revised Rules.
22. Under the Revised Rules, agreements for acquiring components of the self-constructed asset will not be aggregated. Each individual agreement that is not material (i.e. below the size test thresholds) will be exempt from the notifiable transaction requirements. If an individual agreement is material in itself, it will still be subject to the notifiable transaction requirements. The Revised Rules resolve the contradiction that an acquired component of the constructed asset is not exempt, while the entire construction project may be exempt as a notifiable transaction.
23. The Revised Rules exempt self-construction of assets as nearly as practicable to the manner intended and discussed in the CCP. A self-construction project generally involves a series of transactions undertaken by an issuer. The issuer has some involvement in the construction process (for example by being the general contractor) and bears the related risk. It would likely have internal expertise and the project is part of its core business. The Revised Rules acknowledge this process and disapply the requirements to aggregate the series of transactions. Consistent with our views

stated in the CCP, the Revised Rules follow the principle that natural growth in an issuer's business are better left to the management's judgement, particularly when it has the expertise.

24. We have considered and decided not to adopt the respondents' comment to extend the exemption to construction of assets by third parties for an issuer's own use. When an issuer has the internal expertise and constructs the asset itself, it bears the risk of construction and there are genuine reasons for exempting the constructed asset from the notifiable transaction requirements. If a third party is contracted to build the asset, the risk of bringing the asset to completion is shifted to the contractor. This is in substance an acquisition of asset which falls outside the policy intent of the proposal discussed in the CCP.

#### ***Consultation conclusion***

25. We have adopted the proposal to exempt self-construction of assets and revised the Rule amendments to disapply the aggregation requirements when an issuer enters into a series of transactions to construct, develop or refurbish an asset for its own use in its ordinary and usual course of business if the sole basis for aggregation is because the series of transactions form parts of one larger asset.

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## **APPENDIX: LIST OF RESPONDENTS**

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### Listed issuers

1. Aluminium Corporation of China Ltd.
2. Angang Steel Co. Ltd.
3. AviChina Industry & Technology Co. Ltd.
4. Bank of Communications, Company Director and Secretary
5. Bank of Communications, Manager of Directors' Office
6. Beijing Capital International Airport Co. Ltd.
7. Beijing Capital Land Ltd.
8. Beijing North Star Co. Ltd.
9. Beiren Printing Machinery Holdings Ltd.
10. BYD Co. Ltd.
11. Cathay Pacific Airways Ltd.
12. China Coal Energy Co. Ltd.
13. China Communications Construction Co. Ltd.
14. China COSCO Holdings Co. Ltd.
15. China Life Insurance Co. Ltd.
16. China Merchants Bank Co., Ltd.
17. China National Building Material Co. Ltd.
18. China National Materials Co. Ltd.
19. China Petroleum & Chemical Corporation
20. China Railway Group Ltd.
21. China Shipping Container Lines Co., Ltd.
22. CLP Holdings Limited
23. Dalian Port (PDA) Company Limited
24. Dongfang Electric Corporation Ltd.
25. First Tractor Co. Ltd.
26. Great Wall Motor Co. Ltd.
27. Great Wall Technology Co. Ltd.
28. Guangshen Railway Co. Ltd.
29. Harbin Power Equipment Co. Ltd.
30. Hong Kong Aircraft Engineering Co. Ltd.
31. HSBC Holdings plc
32. Hunan Nonferrous Metals Corporation Ltd.
33. Jiangxi Copper Co. Ltd.
34. Jingwei Textile Machinery Co. Ltd.
35. KPI Company Limited
36. Lianhua Supermarket Holdings Co. Ltd.
37. Maanshan Iron & Steel Co. Ltd.
38. Mexan Limited
39. Minmetals Land Limited
40. Nanyang Holdings Ltd.
41. New Focus Auto Tech Holdings Ltd.
42. Northeast Tiger Pharmaceutical Co. Ltd.
43. Shandong Luoxin Pharmacy Stock Co. Ltd.
44. Shandong Molong Petroleum Machinery Co. Ltd.
45. Shanghai Electric Group Co. Ltd.
46. Shanghai Forte Land Co. Ltd.
47. Shanghai Prime Machinery Co. Ltd.



48. Sichuan Xinhua Winshare Chainstore Co., Ltd.
49. Swire Pacific Limited
50. Tong Ren Tang Technologies Co. Ltd.
51. TravelSky Technology Ltd.
52. USI Holdings Ltd.
53. Weiqiao Textile Co. Ltd.
54. Winsor Properties Holdings Limited
55. Yanzhou Coal Mining Co. Ltd.
56. Zhejiang Expressway Co. Ltd.
57. Zhuzhou CSR Times Electric Co., Ltd.
58. A market participant (name not disclosed at the respondent's request)

#### Professional and industry associations

1. Canadian Certified General Accountants Association of Hong Kong
2. Hong Kong Custodian Bank Working Group
3. Hong Kong Federation of Women Lawyers
4. Hong Kong Institute of Certified Public Accountants
5. Hong Kong Stockbrokers Association
6. The Association of Chartered Certified Accountants, Hong Kong
7. The Chamber of Hong Kong Listed Companies
8. The Chartered Institute of Management Accountants, Hong Kong Division
9. The Chinese General Chamber of Commerce
10. The Hong Kong Association of Banks
11. The Hong Kong Institute of Chartered Secretaries
12. The Institute of Accountants in Management
13. The Law Society of Hong Kong
14. The Real Estate Developers Association of Hong Kong
15. A respondent (submission not posted on HKEx's website at the respondent's request)

#### Market practitioners

1. BC Investment Management Corporation
2. *Charltons on behalf of:*
  - Anglo Chinese Corporate Finance, Limited
  - CIMB-GK Securities (HK) Ltd.
  - Quam Limited
  - Somerley Limited
  - SW Kingsway Capital Holdings Limited
  - Taifook Capital Limited
3. Clifford Chance
4. Computershare Hong Kong Investor Services Ltd.
5. Deloitte Touche Tohmatsu
6. Ernst & Young
7. F & C Management Limited
8. *Freshfields on behalf of:*
  - ABN AMBRO BANK N. V., Hong Kong Branch
  - BOCI Asia Limited
  - China International Capital Corporation Limited
  - Citigroup Global Markets Asia Limited
  - Credit Suisse (Hong Kong) Limited
  - Deutsche Bank AG, Hong Kong Branch
  - J. P. Morgan Securities (Asia Pacific) Co. Ltd.
  - Lehman Brothers Asia Limited

Merrill Lynch Far East Limited  
Morgan Stanley Asia Limited  
UBS AG

9. *Herbert Smith and Freshfields on behalf of:*  
ABN AMBRO BANK N. V., Hong Kong Branch  
BOCI Asia Limited  
China International Capital Corporation (Hong Kong) Limited  
Citigroup Global Markets Asia Limited  
Credit Suisse (Hong Kong) Limited  
Deutsche Bank AG, Hong Kong Branch  
Goldman Sachs (Asia) L.L.C.  
J. P. Morgan Securities (Asia Pacific) Ltd.  
Merrill Lynch Far East Limited  
Morgan Stanley Asia Limited  
Nomura International (Hong Kong) Limited  
UBS AG
10. Hermes Fund Managers Limited  
11. Linklaters  
12. Paul, Hastings, Janofsky & Walker  
13. Piper Jaffray Asia Limited  
14. PricewaterhouseCoopers  
15. SBI E2-Capital (HK) Ltd.  
16. Sinotec Investment Management  
17. Slaughter and May  
18. Stephenson Harwood & Lo  
19. Sun Hung Kai & Co. Limited  
20. Timothy Loh Solicitors  
21. Tricor Services Limited  
22. A market practitioner (name not disclosed at the respondent's request)

Statutory regulators

1. Companies Registry
2. The Financial Reporting Council

Individuals and retail investor representative

1. Chan Wai Lok, Leo
2. Gregg Li
3. John Maguire/Allen Tze
4. Paul Mok
5. Joseph So
6. JE Strickland
7. Tam Heung Man, Mandy
8. Webb-site.com

*Remarks:*

1. *One submission is counted as one response.*
2. *One respondent (Webb-site.com) indicated that the submissions in respect of two of the issues were made on behalf of 475 and 364 respondents respectively in answer to its own on-line surveys.*
3. *The total number of responses is calculated according to the number of submissions received and not the underlying members that they represent.*

