

HKE_x LISTING DECISION

Cite as HKE_x-LD36-1 (October 2003) (Withdrawn in October 2012; superseded by GL 43-12)

Summary	
Name of Parties	Company A - a Main Board new listing applicant Mr X – a shareholder of Company A Mr Y – a shareholder of Company A
Subject	Pre-IPO placing - whether shares subject to lock-up and counted as part of public float
Listing Rules	Rules 1.01, 8.24 and 10.07(1)
Decision	Lock-up is determined on case-by-case basis – placee subject to lock-up not counted as public

Summary of Facts

Mr X had acquired some shares in Company A by way of transfer from Mr Y shortly before Company A's listing application.

Mr Y held, prior to the transfer, more than 30 per cent of Company A's issued share capital, while Mr X would, upon listing, hold less than 10 per cent.

Mr X was an investor with no managerial position in Company A. The consideration paid by him represented a substantial discount to the IPO price.

Company A's sponsor asked the Exchange whether Mr X's shares would be subject to a lock-up and whether it could be counted as part of the public float for the purpose of the minimum public float requirement.

Analysis

Under Rule 1.01 of the Listing Rules, “any person who is or group of persons who are together entitled to exercise or control the exercise of [30 per cent] or more of the voting power at general meetings of the issuer or who is or are in a position to control the composition of a majority of the board of directors of the issuer ...” is a “controlling shareholder”.

Under Rule 1.01, a person who is entitled to exercise or control the exercise of 10 per cent or more of the voting power at any general meeting of a company is a “substantial shareholder” of that company. A substantial shareholder of an issuer is also a connected person.

Rule 10.07(1) subjects a controlling shareholder to the following lock-up:

“A person or group of persons shown by the listing document issued at the time of the issuer’s application for listing to be a controlling shareholder of the issuer shall not:—

- (a) in the period of 6 months from the date on which dealings in the securities of a new applicant commence on the Exchange, dispose of, and shall procure that the registered holder shall not dispose of, any of those securities of the issuer in respect of which he is or they are shown by that listing document to be the beneficial owner; or
- (b) in the period of 6 months commencing from the date on which the period referred to in the rule 10.07(1)(a) expires, dispose of or permit the registered holder to dispose of, any of the securities referred to in rule 10.07(1)(a) if, immediately following such disposal that person or group of persons would cease to be a controlling shareholder.”

Pursuant to Rule 8.24, a connected person cannot be counted as part of the public float for the purpose of the minimum public float requirement. The Rule further provides that the Exchange will not recognise as a member of the “public”: -

- any person whose acquisition of securities has been financed directly or indirectly by a connected person; or
- any person who is accustomed to take instructions from a connected person in relation to the acquisition, disposal, voting or other disposition of securities of the issuer registered in his name or otherwise held by him.

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

The placing of shares to persons shortly before the proposed listing of a company tends to call into question the genuineness of the transaction and may lead one to query whether the placee will be holding the shares for his own benefit or for the benefit of a controlling shareholder, with a view to circumventing the lock-up provisions of the Listing Rules. In the absence of satisfactory evidence to the contrary, where the transferor is a person who would otherwise be a controlling shareholder upon listing, the transferor and the placee will be regarded as a “group of persons who are together entitled to exercise or control the exercise of [30 per cent] or more of the voting power at general meetings of the issuer” for the purpose of the “controlling shareholder” definition in Rule 1.01. In such cases, therefore, the placee:

- must not, during the period of 6 months referred to in Rule 10.07(1)(a), dispose of, and must procure that the registered holder shall not dispose of, any of the placed shares; and
- must not, during the period of 6 months referred to in Rule 10.07(1)(b), dispose of or permit the registered holder to dispose of, any of the placed shares if, immediately following such disposal, the person or group of persons shown by the listing document to be a controlling shareholder (i.e. the transferor and the placee) would cease to be a controlling shareholder.

Furthermore, the Exchange would not regard any placee who is subject to a lock-up as a member of the public at the time of listing and for so long as the transferor and the placee together constitute a “group of persons who are together entitled to exercise or control the exercise of [30 per cent] or more of the voting power at general meetings of the issuer or who is or are in a position to control the composition of a majority of the board of directors of the issuer”.

It was also noted that:

- “shortly before a listing application” tends to be measured in terms of months rather than weeks and with the date of the listing application as reference point;
- the greater the amount of any discount to the IPO price and/or the greater the proximity in time of the placing to the date of the listing application, the greater would be the doubt as to the genuine nature of the transaction such that a lock-up of the shares would be warranted;
- whether the placing is of existing shares or new shares is of limited relevance since both methods achieve the same end, namely the final shareholding structure of the company upon listing;
- where a placee is not subject to any lock-up, the prospectus should include a prominent statement in the prospectus that there are no lock-up arrangements for the placee concerned together with an explanation as to why there are no lock-up arrangements in place; and
- in all cases, the prospectus should include a prominent statement giving the reasons for the placing, including any contribution which the placee has made to the company, any benefits which the placing is expected to bring to the company and a justification of the placing price.

Decision

Based on the facts of the present case, namely that Mr X had acquired his shares shortly before the proposed listing and at a substantial discount to the IPO price, Mr X’s shares would be subject to the Rule 10.07(1) lock-up in the manner described above.

Consequently, he would not be counted as a member of the “public” at the time of listing and for so long as Mr Y and Mr X together constitute a group of persons who are together entitled to exercise or control the exercise of 30 per cent or more of the voting power at general meetings of Company A or who is or are in a position to control the composition of a majority of the board of directors of Company A. As to whether Mr X would be counted as a member of the “public” thereafter, one would still need to have regard to Rule 8.24.