

HKE_x LISTING DECISION

Cite as HKE_x-LD47-3 (July 2005) (Updated for accounting and auditing standards reference in September 2009)

[Withdrawn in April 2019; Superseded by HKEX-GL45-12]

Summary	
Name of Party	Company A – a Main Board listing applicant and its subsidiaries (the “Group”)
Subject	Whether the requirements of Listing Rules 8.05(1) and 4.04(1) could be satisfied where the Group’s three financial year trading record period comprised a prior-incorporation period under Company A’s predecessor and a post-incorporation period under Company A directly?
Listing Rules	Listing Rules 8.05(1)(a) and 4.04(1)
Decision	<p>The Exchange determined that:</p> <ul style="list-style-type: none">• the business that formed the subject matter of listing in the present case had been in existence for more than three financial years, and it had been separately demonstrated to the Exchange that the requirements of Listing Rules 4.04 and 8.05 had been satisfied;• the trading record period of Company A which comprised one period under Company A’s predecessor and a second period under Company A directly was not, in itself, objectionable to listing;• the presentation of the track record results of Company A in two accountants’ reports in its prospectus was an acceptable way to present financial information of the Group.

SUMMARY OF FACTS

1. Company A was incorporated in the first year of the three financial year track record period (comprising “Year 1, Year 2 and Year 3”). Therefore, Company A itself had a trading record of less than three years. Prior to its establishment, Company A’s business that formed the subject matter of listing (“Business”) was carried out by its parent company (“Parent”). Upon establishment, the Parent

- transferred the Business to Company A. The transfer involved a change in the minority shareholders' interests.
2. It was noted that the Business had been operated under substantially the same management and ownership since the beginning of the track record period. The Exchange also noted that the Group could meet the minimum profit requirement under Listing Rule 8.05(1) even without taking into account the results from the Predecessor Period.
 3. The Group's accounts had been prepared in accordance with accounting principles generally accepted in Hong Kong ("HK GAAP"). According to applicable accounting standards, the track record period of Company A was presented in two sets of accountants' reports covering the results of the Business for the prior-incorporation period (the "Predecessor Period"), and the results of Company A since the date of incorporation (the "Post Incorporation Period").
 4. According to the reporting accountants of Company A, the relevant accounting principles (that is SSAP27¹) precluded Company A from including the results of the Business for the Predecessor Period into its financial statement for the reason that there had been a change in the minority interests during the transfer of the Business from the Predecessor to Company A. Consequently, two accountants' reports were required to present the results of the Business for the track record period.
 5. With regard to the preparation of the financial information in relation to the Business during the Predecessor Period and the Post Incorporation Period, the reporting accountants confirmed that:-
 - a. the financial information in relation to the Predecessor Period had been extracted from the financial statements of the Predecessor. In particular, the assets, liabilities, results of operation and the cashflow could be easily identified from the underlying ledgers; the balance sheet items of the Business substantially did not require allocations; and most of the results from the operation of the Business could be directly captured; and
 - b. the basis of preparation of the two accountants' reports for the Predecessor Period and the Post Incorporation Period had no significant difference.

THE ISSUE RAISED FOR CONSIDERATION

6. Whether the requirements of Listing Rules 8.05(1) and 4.04(1) could be satisfied where the Group's three financial year trading record period comprised a prior-incorporation period under Company A's predecessor and a post-incorporation period under Company A?

APPLICABLE LISTING RULES OR PRINCIPLES

7. Listing Rule 4.04 (1) provides, in the case of a new applicant, the accountants' report must include:

‘the results of the issuer or, if the issuer is a holding company, the consolidated results of the issuer and its subsidiaries in respect of each of the three financial years immediately preceding the issue of the listing document.’

8. Listing Rule 8.05(1) provides that:

‘[T]o meet the profit test, a new applicant must have an adequate trading record under substantially the same management and ownership... This means that the issuer, or its group.... must satisfy each of the following:

- (a) a trading record of not less than three financial year (see rule 4.04) during which the profit attributable to shareholders must, in respect of the most recent period, be not less than HK\$20,000,000 and, in respect of the most recent year, be not less than HK\$30,000,000...;
- (b) management continuity for at least the three preceding financial years; and
- (c) ownership continuity and control for at least the most recent audited financial year.’

9. Listing Rule 4.08(3) requires accountants' report to prepared in accordance with the Auditing Guideline – Prospectuses and the reporting accountant (AG 3.340) issued by the Hong Kong Institute of Certified Public Accountants.

10. Listing Rule 4.11 requires the financial history of results and the balance sheet included in the accountants' report must normally be drawn up in conformity with Hong Kong Financial Reporting Standards or International Financial Reporting Standards.

11. Paragraph 1(f) of Appendix to AG 3.340 specifically states that:

‘where, for example, companies under common control but legally unconnected are formed into a legal group prior to issue or floatation, the accountant's report should be prepared on a combined basis and should explain the basis of preparation in the introductory paragraphs of the report.’

12. Statements of Standard Accounting Practice 27 ('SSAP27')¹ of Hong Kong Financial Reporting Standards ('HKFRS') sets out the principles for the accounting treatment of group reconstructions. In that paragraph 5 thereof requires:

'[A] group reconstruction should be accounted for by using merger accounting if:

- a. merger relief is taken advantage of ;
- b. the ultimate shareholders remain the same, and the rights of each such shareholder, relative to the others, are unchanged; and
- c. any minority interest in the net assets of the group is unaltered by the transfer.

Acquisition accounting should be used for all group reconstructions that are not accounted for by using merger accounting.'

THE ANALYSIS

13. The Exchange ordinarily interprets Listing Rule 8.05 as an eligibility standard, while requirements of Chapter 4 of the Listing Rules related to the contents of accountants' report (See, for example, Listing Decision HKEx-LD41-2). As such, Listing Rule 4.04(1) and Listing Rule 8.05(1) are separate requirements.
14. When assessing whether a listing applicant can meet the eligibility requirements under Listing Rule 8.05, the starting point of the Exchange's analysis is the historical ownership interest in the listing applicant and its subsidiaries during the last three financial years as presented in accordance with the requirements under Rule 4.04(1).
15. Further more, in assessing whether there is a sufficient trading record under Listing Rule 8.05, the Exchange interprets the rule to refer to the business that forms the subject matter of listing and not the legal entity that forms the listing applicant as such.
16. Based on the above analysis, considerations were given to the followings:

In respect of compliance with Rule 4.04(1)

- a. the two accountants' reports together presented the historical results of the Business that formed the substance of listing for three full financial years in compliance with the requirements of Listing Rule 4.04;

In respect of compliance with Rule 8.05(1)

- b. the Business that formed the substance of listing had been conducted for over three financial years originally as a division of the Parent and subsequently as a division of Company A since its incorporation in Year 1;
 - c. the Business was carried on by the Group and the Predecessor under substantially the same management;
 - d. there was no change in management and ownership control upon the incorporation of Company A and the transfer of the Business from the Predecessor to Company A in Year 1; and
 - e. the minimum profit requirements could be met.
17. Given that it was demonstrated to the Exchange that the requirements under Listing Rule 8.05(1) could be met on the basis of the historical accounts that were presented, the Exchange determined that the presentation of the track record results of Company A in two accountants' reports in its prospectus was an acceptable way to present financial information of the Group.

THE DECISION

18. Based on the above analysis and having regard to the material facts, it was determined that:
- a. the Business that formed the subject matter of listing had been in existence for more than three financial years;
 - b. Listing Rules 4.04 and 8.05 had been separately demonstrated to the satisfaction of the Exchange;
 - c. the trading record period of Company A which comprised a Predecessor Period and a Post Incorporation Period was not, in itself, objectionable to the listing of Company A; and
 - d. the presentation of the track record results of Company A in two accountants' reports in its prospectus was an acceptable way to present financial information of the Group.

Note:

1. *SSAP 27 was superseded in 2005. Please also refer to Accounting Guideline 5 – Merger Accounting for Common Control Combinations (issued in November 2005). (Added in September 2007)*