

**HKEx LISTING DECISION**  
Cite as HKEx-LD48-2 (December 2005)

*[Withdrawn in April 2019; Superseded by HKEX-GL45-12]*

<b>Summary</b>	
<b>Name of Party</b>	Company A - a Main Board listing applicant and its subsidiaries (the 'Group')
<b>Subject</b>	Whether compensation income arising from the one-time early termination of a contract could be counted towards satisfaction of the profit requirements under Listing Rule 8.05(1)(a)?
<b>Listing Rule</b>	Listing Rule 8.05(1)(a)
<b>Decision</b>	The Exchange determined that the relevant income was related to activities within the ordinary and usual course of Company A's business, and therefore could be counted towards satisfaction of the profit requirements of Listing Rule 8.05(1)(a).

**SUMMARY OF FACTS**

1. Company A was principally engaged in the provision of logistic services including warehousing ('Logistic Services') for its customers.
2. The track record profit results of Company A included income arising from the one-time early termination of a contract entered into between the Group and an independent customer of the Group in the first financial year of the track record period. If the early termination fee had not been included, Company A could not have recorded a profit of not less than HK\$30 million for the first two financial years of the track record period for the purpose of Listing Rule 8.05(1)(a).
3. The contract with the independent customer was for the provision of purpose-built warehousing services for the customer under a fixed term lease arrangement with a guaranteed minimum lease. The purpose-built warehouse was not for the exclusive use of the customer. Due to a change in business plan, the customer terminated the contract in the first financial year of the track record period and paid compensation to the Group. After the early termination, the customer continued to use the facility on a shorter term basis until the middle of the second financial year of the track record period.
4. The Exchange reviewed whether the compensation income should be permitted to be counted as profits for the purpose of Listing Rule 8.05(1)(a).

5. The sponsor considered that the compensation income fell within the ordinary and usual course of business of the Group for the following reasons:
  - a. the compensation fee was calculated on the basis of the minimum guarantee fees over the remaining term of the contract. The minimum guarantee fees were intended to protect the Group's investment in the contract;
  - b. because of the dynamic business environment of the Group's business, early termination of contracts was not uncommon. It was demonstrated to the Exchange that during the track record period the Group had also received compensation for early termination of contracts by customers although no purpose-built facilities were involved in such cases; and
  - c. the reporting accountants of Company A confirmed that the compensation income was not considered to be an extraordinary item, and was regarded as part the ordinary course of business of the Group. Accordingly, the reporting accountants treated the compensation income as operating profit in the relevant audited financial statements in accordance with the Statements of Standard Accounting Practice issued by Hong Kong Institute of Certified Public Accountants.

#### **THE ISSUE RAISED FOR CONSIDERATION**

4. Whether compensation income arising from the one-time early termination of a contract could be counted towards satisfaction of the profit requirements under Listing Rule 8.05(1)(a)?

#### **APPLICABLE LISTING RULES OR PRINCIPLE**

5. Listing Rule 8.05(1)(a) states that:

to meet the profit test, a new applicant must have an adequate trading record of not less than three financial years during which the profit attributable to shareholders must, in respect of the most recent year, be not less than HK\$20,000,000 and, in respect of the two preceding years, be in aggregate not less than HK\$30,000,000. The profit mentioned above should exclude any income or loss of the issuer, or its group, generated by activities outside the ordinary and usual course of its business.
6. Listing Rule 4.11 states that '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’.

### **THE ANALYSIS**

7. In determining whether an item of income can be counted towards satisfaction of the profit requirement of Listing Rule 8.05(1)(a), the Exchange must be satisfied that, based on the facts and circumstances of a particular case, the income arises from the ordinary and usual course of business.
8. On the basis of the facts and circumstances of Company A’s case, including the fact that both the sponsor and the reporting accountants considered that the compensation income was generated from activities within the ordinary and usual course of Company A’s business, the Exchange allowed the income associated with the one-time early termination of a contract to be counted as profit for the purpose of Listing Rule 8.05(1)(a).

### **THE DECISION**

9. Based on the material facts and circumstances of Company A’s case, the Exchange determined that the relevant income was related to activities within the ordinary and usual course of Company A’s business, and therefore could be counted towards satisfaction of the profit requirements of Listing Rule 8.05(1)(a)