

**HKEX GUIDANCE LETTER**

**HKEX-GL89-16 (November 2016) (Updated in October 2017 and February 2018)**

~~[The changes made to this Guidance Letter are to set out clearly the rationale of Rule 8.05(1)(c)]~~

[To amend the lock-up requirements for controlling shareholders of GEM applicants]

Subject	Guidance on issues related to “controlling shareholder” and related Listing Rules implications
Listing Rules and Regulations	<p>Main Board Rules 1.01, 6.12, 7.19, 7.24, 8.05(1)(c)/ 8.05(2)(c)/ 8.05(3)(c), 8.10, 9.03(3), 10.07(1), 13.17, 13.18, 13.36(4), 14.55, 14.89, 14.90, 14.91, 14A.11, 14A.28, 19A.04, 19A.14, 19B.03, paragraph 3(e) in Practice Note 15, paragraph 27A in Appendix 1A and 1E, paragraphs 6.3, 16 and 40.3 in Appendix 16/</p> <p>GEM Rules 1.01, 9.20, 10.29, 10.39, 11.03, 11.04, 11.12A(2), 12.09, 13.16A, 13.19, 17.19, 17.20, 17.42A, 18.04, 18.26, 18.27, 18.55(9), 18.68, 19.55, 19.88, 19.89, 19.90, 20.26, 25.10, 25.04(1), paragraph 3(e) in Practice Note 3 and paragraph 27A in Appendix 1A</p>
Related Publications	<p>Listing Decisions (HKEX-LD42-4, HKEX-LD44-4, HKEX-LD47-1, HKEX-LD48-3, HKEX-LD51-2, HKEX-LD51-4, HKEX-LD51-5, HKEX-LD85-2015 and HKEX-LD92-2015)</p> <p>Frequently Asked Questions (Series 1 No. 16 and Series 6 No. A4)</p>

**Important note:** *This letter does not override the Listing Rules and is not a substitute for advice from qualified professional advisers. If there is any conflict or inconsistency between this letter and the Listing Rules, the Listing Rules prevail. You may consult the Listing Department on a confidential basis for an interpretation of the Listing Rules or this letter.*

## 1 Purpose

- 1.1 This letter is intended to assist listing applicants, listed issuers and their advisers by (i) providing guidance on the Exchange’s interpretation of the purpose of ownership continuity and control requirement; (ii) providing guidance on the Exchange’s interpretation of the definition of “controlling shareholder” as set out in the Main Board Rules and the GEM Rules; and (iii) clarifying the Exchange’s practice regarding the key obligations to which a “controlling shareholder” is subject pursuant to the Main Board Rules and the GEM Rules, including the ownership continuity and control

requirement (Main Board Rules 8.05(1)(c)/ 8.05(2)(c)/ 8.05(3)(c)/ GEM Rule 11.12A(2)), the lock-up requirement (Main Board Rule 10.07(1)/ GEM Rule 13.16A) and various disclosure obligations at the pre-listing and post-listing stages. **(Updated in October 2017)**

- 1.2 The Exchange expects listing applicants to follow this guidance letter when preparing listing applications. A listing document that does not follow this guidance may be considered not substantially complete as required under Main Board Rule 9.03(3) and GEM Rule 12.09.
- 1.3 Issuers and sponsors are reminded that any change in shareholdings of an issuer referred to in this guidance letter may have implications under the Code on Takeovers and Mergers and they should separately seek appropriate professional advice.

## **2 Purpose of ownership continuity and control requirement**

- 2.1 The ownership continuity and control requirement is one condition under the profit or cash flow test (Main Board Rule 8.05(1)(c)/ GEM Rule 11.12A(2)) which a listing applicant must satisfy for its trading record to be counted towards the minimum required profit or cash flow.
- 2.2 The ownership continuity and control requirement is therefore intended to ensure that the listing applicant's financial performance resulted from the actual dynamics between the controlling shareholder(s) and the management for at least the last financial year of the track record. This means that the listing applicant must have been operated as an integrated unit under the same shareholder(s) who was able to exert substantial influence on the same directors and management.
- 2.3 Failure to satisfy the test raises concerns on packaging as there may be a material change in influence on management. However, a listing applicant can rebut these presumptions by demonstrating that there was no material change in influence on management despite the change in controlling shareholder(s) since a change in controlling shareholder(s) will not always render the listing applicant ineligible for listing. **(Updated in October 2017)**

## **3 Definition and interpretation of “controlling shareholder”**

### ***Relevant Listing Rules***

- 3.1 Main Board Rule 1.01 (GEM Rule 1.01) defines “controlling shareholder” as any person who is or group of persons who are together:
  - (i) entitled to exercise or control the exercise of 30% (or such other amount as may from time to time be specified in the Code on Takeovers and Mergers as being

the level for triggering a mandatory general offer) or more of the voting power at general meetings of the issuer; or

- (ii) in a position to control the composition of a majority of the board of directors of the issuer<sup>1</sup>.

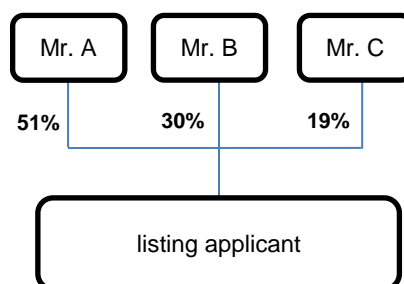
3.2 Main Board Rule 1.01 provides that for a listing of depositary receipts, a holder of depositary receipts can be treated as a “controlling shareholder” of the issuer, but Main Board Rules 14A.11 and 19B.03 state that a depositary will not be treated as such merely by reason that it is holding shares of an issuer as a depositary for the benefit of depositary receipt holders<sup>2</sup>.

### ***The Exchange’s Interpretation***

3.3 At the outset, it is important to note that the process of identifying the “controlling shareholder(s)” of a listing applicant is a case-specific exercise and depends on the facts and circumstances of each case. The sponsors need to perform the necessary and appropriate due diligence to ensure that information with regard to a “controlling shareholder” of a listing applicant set out in a listing document is true, accurate and complete in all material respects and not misleading or deceptive in any material respect. However, the Exchange has the power to deem any shareholder to be a “controlling shareholder” or a group of “controlling shareholders” of an issuer based on the facts and circumstances of that case.

3.4 We set out below some simplified examples of ownership structures of a listing applicant that are commonly seen and the way the Exchange would interpret the definition of “controlling shareholder” in these situations:<sup>3</sup>

#### **3.4.1 Example 1**



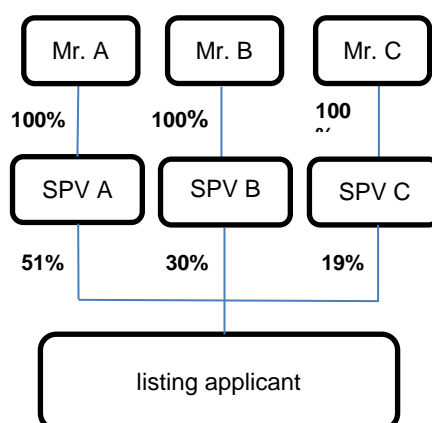
<sup>1</sup> In the case of a PRC issuer, see Main Board Rule 19A.14 (GEM Rule 25.10).

<sup>2</sup> Frequently Asked Questions (Series 6 No. A4) states that the depositary receipt framework applies to the Main Board only and depositary receipts are not allowed to be listed on GEM at this stage.

<sup>3</sup> These examples are not intended to be exhaustive. Furthermore, it is assumed that none of the holders of voting interests in the listing applicants in these examples have identified themselves as groups of controlling shareholders in their listing applications.

In Example 1, the Exchange considers each of Mr. A and Mr. B to be a controlling shareholder of the listing applicant as each of Mr. A and Mr. B is entitled to exercise 30% or more of the voting power at general meetings of the listing applicant. The Exchange does *not* consider Mr. C to be a controlling shareholder of the listing applicant as Mr. C is neither entitled to exercise, nor does Mr. C control the exercise of, 30% or more of the voting power at general meetings of the listing applicant.

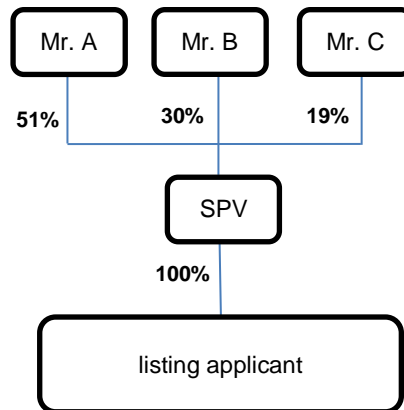
### 3.4.2 Example 2<sup>4</sup>



In Example 2, the Exchange considers each of Mr. A, SPV A, Mr. B and SPV B to be a controlling shareholder of the listing applicant as (i) each of SPV A and SPV B is entitled to exercise 30% or more of the voting power at general meetings of the listing applicant and (ii) each of Mr. A and Mr. B is entitled to, through SPV A and SPV B respectively, control the exercise of 30% or more of the voting power at general meetings of the listing applicant. The Exchange does *not* consider Mr. C or SPV C to be a controlling shareholder of the listing applicant as each of Mr. C and SPV C is neither entitled to exercise, nor does Mr. C or SPV C control the exercise of, 30% or more of the voting power at general meetings of the listing applicant.

<sup>4</sup> This example assumes that each of SPV A, SPV B and SPV C is an investment vehicle of Mr. A, Mr. B and Mr. C respectively, and exclusively hold the individuals' interests in the listing applicant and have no operations. If such investment vehicles do not exclusively hold the interests in the listing applicant and/or have other businesses, we will assess such cases on a case-by-case basis.

3.4.3 Example 3<sup>5</sup>



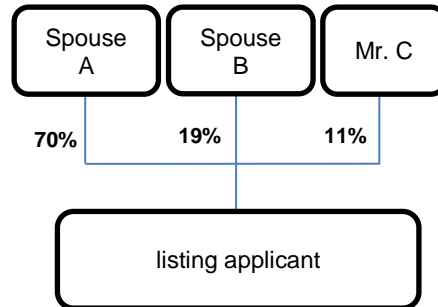
In Example 3, the Exchange considers SPV, which has 100% of the voting power at general meetings of the listing applicant, to be a controlling shareholder of the listing applicant as SPV is entitled to exercise 30% or more of the voting power at general meetings of the listing applicant. Mr. A also falls within the definition of “controlling shareholder” of the listing applicant as Mr. A controls SPV (and hence SPV’s voting interests in the listing applicant) by virtue of holding more than 50% of the voting interests of SPV. On the other hand, since neither Mr. B nor Mr. C holds more than 50% of the voting interests of SPV, neither Mr. B nor Mr. C is in a position to control SPV’s voting interests in the listing applicant.

However, on the basis that Mr. A, Mr. B and Mr. C have decided to restrict their ability to exercise direct control over the listing applicant by holding their interests through a common investment holding company (namely SPV), the Exchange will *presume* Mr. A, Mr. B and Mr. C to be a group of controlling shareholders of the listing applicant. If Mr. B and/ or Mr. C do not consider themselves as part of the group of controlling shareholders, the listing applicant should provide a detailed submission rebutting this presumption.<sup>6</sup> Unless the Exchange accepts such rebuttal, Mr. B and Mr. C shall be disclosed as controlling shareholders in the listing document.

<sup>5</sup> This example assumes that the SPV is an investment vehicle of Mr. A, Mr. B and Mr. C and exclusively holds their interests in the listing applicant and has no operations. A listed issuer, for example, would not be an SPV. If such investment vehicle does not exclusively hold the interests in the listing applicant and/ or has other businesses, we will assess such cases on a case-by-case basis.

<sup>6</sup> For the factors that the Exchange considers in determining whether any individual shareholder had been acting as part of a group of controlling shareholders, see listing decisions: HKEX-LD44-4 and LD51-5.

### 3.4.4 Example 4



In Example 4, although Spouse B is not individually entitled to exercise 30% or more of the voting power at general meetings of the listing applicant and hence does not fall within the definition of “controlling shareholder” of the listing applicant, the Exchange will *presume* Spouse A and Spouse B to be a group of controlling shareholders by virtue of their relationship of being spouses. If Spouse B does not believe he/ she is part of the controlling group of shareholders, the listing applicant should provide a detailed submission rebutting this presumption<sup>7</sup>. Unless the Exchange accepts such rebuttal, Spouse B shall be disclosed as a controlling shareholder in the listing document. The Exchange applies the same presumption to all shareholders who are “close associates” of each other as defined in Main Board Rule 1.01 (GEM Rule 1.01).<sup>8</sup>

3.5 The Exchange notes that in past situations similar to Examples 3 and 4 above, applicants would state in their listing applications the identity of the controlling shareholder(s) without clearly explaining the basis. Listing applicants are required to disclose the basis for the identification of their controlling shareholder(s) in the listing documents submitted as part of their listing applications. To rebut the Exchange’s presumption in situations similar to Examples 3 and 4 above, listing applicants must provide a detailed submission providing the reasons as part of their listing applications for the Exchange’s consideration.

## 4 Key requirements on “controlling shareholder” at the pre-listing stage

Pre-listing, a controlling shareholder of a listing applicant is subject to the following key obligations pursuant to the Main Board Rules and the GEM Rules:

- (i) *listing eligibility requirement*: the ownership continuity and control requirement (Main Board Rules 8.05(1)(c)/ 8.05(2)(c)/ 8.05(3)(c)/ GEM Rule 11.12A(2)); and

<sup>7</sup> See Footnote 6 above.

<sup>8</sup> In the case of a PRC issuer, see Main Board Rule 19A.04 (GEM Rule 25.04(1)).

- (ii) *disclosure requirement in listing document*: details of any controlling shareholders and their interests in any competing business (Main Board Rule 8.10/ GEM Rule 11.04; paragraph 27A in Appendix 1A and 1E to the Main Board Rules/ paragraph 27A in Appendix 1A to the GEM Rules).

***Ownership continuity and control requirement***

4.1 In practice:

- (i) the Exchange requires both Main Board and GEM listing applicants to demonstrate “*ownership continuity and control*” in the way required by Frequently Asked Questions (Series 1 No. 16) for at least the most recent financial year up until the time immediately before the offering and/ or placing becomes unconditional (the “**Relevant Period**”);
- (ii) the Exchange applies the definition and interpretation of “*controlling shareholder*” as set out in Section 2 above when applying the interpretation of “*ownership continuity and control*” as set out in Frequently Asked Questions (Series 1 No. 16);
- (iii) for a listing applicant to demonstrate “*ownership continuity and control*”, for at least the Relevant Period, there has been no change to any controlling shareholder(s) identified at the beginning of the most recent financial year;
- (iv) for a listing applicant with a group of controlling shareholders holding their interests directly in the listing applicant to meet the ownership continuity and control requirement, for at least the Relevant Period: (1) the shareholders constituting the group of controlling shareholders must not change (i.e. no addition or departure of shareholders); (2) there must be no material changes in the voting interests in the listing applicant held by each shareholder constituting the group of controlling shareholders; and (3) such group of controlling shareholders together remains a group of controlling shareholders of the listing applicant and there are no new controlling shareholders;
- (v) for a listing applicant with a group of controlling shareholders holding their interests indirectly in the listing applicant (such as through SPV in Example 3) to meet the ownership continuity and control requirement, for at least the Relevant Period: (1) the shareholders constituting the group of controlling shareholders must not change (i.e. no addition or departure of shareholders); (2) there must be no material changes in the voting interests in the SPV held by each shareholder of SPV; and (3) SPV remains a controlling shareholder of the listing applicant and there are no new controlling shareholders; and
- (vi) the Exchange will assess whether any change in the voting interests held by each shareholder constituting the group of controlling shareholders amounts to a

material change on a case-by-case basis. The Exchange encourages potential listing applicants to consult with the Exchange in advance on any plans to transfer any voting interest in the listing applicant (or SPV as the case may be)<sup>9</sup>.

***Disclosure requirement in listing document: details of any controlling shareholders and their interests in any competing business***

- 4.2 A listing applicant shall apply the definition and interpretation of “controlling shareholder” as set out in Section 2 above and determine the identity of the controlling shareholders of the listing applicant immediately upon completion of the offering and/or placing, and disclose in the listing document as required by paragraph 27A in Appendix 1A to the Main Board Rules and the GEM Rules, Main Board Rule 8.10(1)(a) and GEM Rules 11.03 and 11.04 in respect of such controlling shareholder(s).

**5 Key requirements on “controlling shareholder” at the post-listing stage**

Post-listing, a controlling shareholder of a listed issuer is subject to the following key obligations under the Main Board Rules and the GEM Rules:

- (i) *lock-up requirements* (Main Board Rule 10.07(1)/ GEM Rule 13.16A(1)); and
- (ii) *restrictions from voting and disclosures in specific circumstances*.

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<sup>9</sup> The Exchange ordinarily would not consider there to be a breach in the ownership continuity and control requirement in the situations set out below (these are not intended to be exhaustive):

- (i) when a controlling shareholder has transferred his/ her/ its voting interests in the listing applicant held through his/ her/ its controlled SPV to another SPV controlled by him/ her/ it; and
- (ii) when a controlling shareholder has transferred his/ her/ its voting interests to a trust for estate planning purposes and the controlling shareholder has retained control over such trust and the listing applicant consistent with the principles set out in HKEX-LD48-3.



### ***Lock-up requirements***

- 5.1 Main Board Rule 10.07(1) (GEM Rule 13.16A(1)) states that a person or group of persons shown by the listing document issued at the time of the issuer's application for listing to be controlling shareholders of the issuer shall not, apart from any offer of shares for sale contained in a listing document: (a) dispose of shares in the period commencing on the date by reference to which disclosure of the shareholding of the controlling shareholder is made in the listing document and ending on the date which is 6 months (GEM: 12 months) from the date of listing (the "**First Six-month Lock-up Period**"); and (b) dispose of shares in the period of 6 months (GEM: 12 months) commencing on the date on which the First Six-month Lock-up Period expires if immediately following such disposal that person or group of persons would cease to be a controlling shareholder (the "**Second Six-month Lock-up Period**").<sup>10</sup> (Updated in February 2018)
- 5.2 The rationale of Main Board Rule 10.07(1) (GEM Rule 13.16A(1)) is that, when listing a new company, the controlling shareholder is giving potential investors a "snap shot" view of the issuer and a general indication of that controlling shareholder's intentions for the issuer in the coming months, normally for a period of at least 12 months (GEM: 24 months). Investors act on the contents of those listing documents and rely on the information given in the listing documents and on inferences which can reasonably be drawn from that information (unless the contrary is clearly and specifically stated). For example, if the controlling shareholder of the issuer remains the controlling shareholder post-listing, then it implies it has no intention to further sell down its interests in the near future. Main Board Rule 10.07(1) (GEM Rule 13.16A(1)) are therefore designed to enforce such implied intention for at least the first 12 months (GEM: 24 months) following a new issue. (Updated in February 2018)
- 5.3 In practice:
- (i) the Exchange expects listing applicants to apply the definition and interpretation of "*controlling shareholder*" as set out in Section 2 above and determine the identity of the controlling shareholders of the listing applicant as at the date of the published listing document, and such controlling shareholder(s) should be subject to the lock-up requirements pursuant to Main Board Rule 10.07(1) (GEM Rule 13.16A(1));
  - (ii) where the interest of a controlling shareholder identified as at the date of the published listing document will decrease to below 30% as a result of an occurrence of event(s) which is *certain* to happen based on the disclosure in the

<sup>10</sup> Note that Notes (2) and (3) to Main Board Rule 10.07 and GEM Rule 13.19 require any controlling shareholder of a Main Board and GEM listed issuer to inform the issuer of the pledge(s)/ charge(s) of any securities beneficially owned by them in the issuer in favor of an authorized institution for a bona fide commercial loan and any disposal of such pledged/ charged securities by the pledgee/ chargee, and the issuer must disclose such information by way of an announcement as soon as possible.

listing document, e.g. the issuance of shares by the issuer and/ or sale of shares by any existing shareholder as part of the offering and/ or placing, such shareholder shall be subject to lock-up during the First Six-month Lock-up Period, but not during the Second Six-month Lock-up Period. This is because the relevant shareholder would have ceased to be a controlling shareholder of the issuer during the Second Six-Month Lock-up Period and the restriction on disposal such that it “*cease[s] to be a controlling shareholder*” under Main Board Rule 10.07(1)(b)/ GEM Rule 13.16A(1)(b) is not applicable; but (Updated in February 2018)

- (iii) where the interest of a controlling shareholder identified as at the date of the published listing document will decrease to below 30% as a result of the exercise of an over-allotment option by the underwriter(s) of an offering and/ or placing, such shareholder shall be subject to a 12-month (GEM: 24-month) lock-up of its shares after the listing of the issuer, i.e. such shareholder must maintain at least the same number of shares immediately after listing as stated in the issuer’s listing document for at least 12 months (GEM: 24 months) after the listing of the issuer. This approach is consistent with the policy rationale of Main Board Rule 10.07(1) because exercise of the over-allotment option is *uncertain* at the time of listing and the controlling shareholder was prepared to remain as a controlling shareholder of the issuer unless the over-allotment option is exercised based on its disclosure in the listing document. Investors should be able to reasonably expect the relevant shareholder’s involvement in the issuer during the Second Six-month Lock-up Period: see relevant listing decision HKEX-LD85-2015. (Updated in February 2018)

5.4 Where there is a group of controlling shareholders holding their interests directly or indirectly (such as through SPV in Example 3) in the listed issuer, to comply with the lock-up requirement pursuant to Main Board Rule 10.07(1)/ GEM Rule 13.16A(1):

- (i) in the First Six-month Lock-up Period, (1) the shareholders constituting the group of controlling shareholders must not change (i.e. no addition or departure of shareholders); (2) there must be no material changes in the voting interests held by each shareholder constituting the group of controlling shareholders in the listed issuer (or among the shareholders of SPV as the case may be); and (3) such group of controlling shareholders (or SPV as the case may be) must maintain the same aggregate voting interests in the listed issuer; and (Updated in February 2018)
- (ii) in the Second Six-month Lock-up Period, (1) the shareholders constituting the group of controlling shareholders must not change (i.e. no addition or departure of shareholders); (2) there must be no material changes in the voting interests held by each shareholder constituting the group of controlling shareholders in the listed issuer (or by each shareholder of SPV as the case may be); and (3) such group of controlling shareholders (or SPV as the case may be) must maintain an

aggregate voting interests of at least 30% in the listed issuer. **(Updated in February 2018)**

- 5.5 The Exchange will assess whether any change in the voting interests held by each shareholder constituting the group of controlling shareholders amounts to a material change on a case-by-case basis. The Exchange encourages listed issuers to consult with the Exchange in advance on any plan to transfer any voting interest in the listed issuer (or SPV as the case may be).

***Restrictions from voting and disclosures in specific circumstances***

- 5.6 A controlling shareholder of a listed issuer is also subject to the following key continuing obligations pursuant to the Main Board Rules and the GEM Rules:
- (i) *restrictions from voting in favor of certain material corporate actions, including withdrawal of listing (Main Board Rule 6.12/ GEM Rule 9.20); rights issue/ open offer enlarging share capital by over 50% (Main Board Rules 7.19 and 7.24/ GEM Rules 10.29 and 10.39); refreshment of general mandate (Main Board Rule 13.36(4)/ GEM Rule 17.42A), reverse takeovers (Main Board Rule 14.55/ GEM Rule 19.55) and spin-offs (Paragraph 3(e) in Practice Note 15 of the Main Board Rules/ Paragraph 3(e) in Practice Note 3 of the GEM Rules);*
  - (ii) *for issuers listed for one year or less, abstain in voting on acquisitions or disposals or other transactions which would result in a fundamental change in the principal business of the issuer (Main Board Rules 14.89 to 14.91/ GEM Rules 19.88 to 19.90);*
  - (iii) *announcements and disclosure in quarterly/ interim/ annual reports on (i) details of loans requiring controlling shareholders to pledge shares (Main Board Rule 13.17/ paragraphs 6.3 and 40.3 of Appendix 16 to the Main Board Rules/ GEM Rules 17.19, 18.04, 18.55(9) and 18.68) or to fulfill specific performance obligations (Main Board Rule 13.18/ paragraphs 6.3 and 40.3 of Appendix 16 to the Main Board Rules/ GEM Rule 17.20, 18.55(9) and 18.68) and (ii) contracts of significance (paragraph 16 of Appendix 16 to the Main Board Rules/ GEM Rules 18.26 and 18.27); and*
  - (iv) *connected transaction implications: acquisition of interest in a target company from third party is a connected transaction if target company's substantial shareholder is or is proposed to be a controlling shareholder of the listed issuer (Main Board Rule 14A.28/ GEM Rule 20.26).*
- 5.7 Listed issuers are required to apply the definition and interpretation of “controlling shareholder” as set out in Section 2 above in identifying the controlling shareholder(s) of the listed issuer, and such controlling shareholder(s) would be subject to the key obligations set out in paragraph 4.6 and other miscellaneous obligations of controlling shareholders under the Main Board Rules and the GEM Rules.

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