

HKEx LISTING DECISION

Cite as HKEx-LD59-6 (August 2007) (Withdrawn in October 2012; Superseded by GL43-12)

Summary	
Name of Parties	Company A and its subsidiaries (the “Group”) - a Main Board listing applicant Pre-IPO Investor - a proposed pre-IPO investor of the Company A Director X - a non-executive director on Company A’s board nominated by the Pre-IPO Investor and approved by Company A’s board
Subject	Whether the special rights available to the Pre-IPO Investor complied with the principles under Listing Rules 2.03(2) and (4)
Listing Rules	Listing Rules 2.03(2), (4) and (5) Listing Rule 3.08 Listing Decision HKEx-LD36-1 (October 2003)
Decision	The Exchange determined that the special rights granted to the Pre-IPO Investor were contrary to the principles of Listing Rules 2.03(2) and (4) and they were subsequently removed.

SUMMARY OF FACTS

1. Prior to the submission of Company A’s listing application, Company A entered into a subscription agreement (the “Subscription Agreement”) with the Pre-IPO Investor under which the Company issued convertible bonds (the “CBs”) to the Pre-IPO Investor.
2. While the Pre-IPO Investor represented that it had no intention to convert the CBs prior to listing, the terms of the CBs entitled it to do so in whole or in part at any time before the expiration of six months from the listing date. The pre-set conversion price represented a discount of more than 50% to the mid-point of the offer price range. Unless converted earlier, the CBs would be deemed to be converted into Company A’s shares on the expiry of six months from the listing date. Upon conversion of the CBs, Company A’s shares held by the Pre-IPO Investor would be subject to a lock-up of six months from the date of listing. Company A would still meet the minimum public float requirement should the shares so converted not be counted as “public” for the purpose of Listing Rule 8.08.

3. The terms of the CBs also provided that for so long as the CBs were outstanding or the Pre-IPO Investor held Company A's shares, the consent of the Pre-IPO Investor was required before any of the following actions, among others, might proceed:
 - (i) a declaration of dividend by any member of the Group;
 - (ii) the creation of any mortgage, encumbrance or security arrangement of any kind over all or part of the Group's business, undertakings or assets;
 - (iii) the sale, lease or transfer of a substantial part of the Group's business or assets;
 - (iv) any amendments to the Group's constitutional documents; and
 - (v) any change in its executive directors.
4. As a right attached to the CBs, the Pre-IPO Investor could nominate a non-executive director to the board of Company A, pursuant to which Director X was appointed to the board with the approval of Company A's shareholders prior to listing.

THE ISSUE RAISED FOR CONSIDERATION

5. Whether the special rights available to the Pre-IPO Investor complied with the principles under Listing Rules 2.03(2) and (4).

APPLICABLE LISTING RULES OR PRINCIPLE

6. Listing Rules 2.03(2), (4) and (5) require that:
 - (2) the issue and marketing of securities is conducted in a fair and orderly manner ...
 - (4) all holders of listed securities are treated fairly and equally;
 - (5) directors of a listed issuer act in the interests of its shareholders as a whole – particularly where the public represents only a minority of the shareholders;
7. Listing Rule 3.08 requires that every director must in the performance of his duties as a director, among other things, act honestly and in good faith in the interests of the company as a whole and avoid actual and potential conflicts of interest and duty.
8. Listing Decision HKEx-LD36-1 states the following regarding pre-IPO placings:

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 ANALYSIS

9. When coming to its decision in the current case, the Exchange took into account the facts and circumstances of the case, Listing Rule 2.03 and the rationale for the decision in the previous case of Listing Decision HKEx-LD36-1.
10. In the scenario contemplated in Listing Decision HKEx-LD36-1, the placing of shares to the investors was completed before listing and the investors took genuine investment risks for such pre-IPO investment. In this case, it was more than likely that the CBs would be converted given the deep discount of the conversion price vis-a-vis the offer price, and as such the pre-IPO investment did not carry greater risks than those investors participating at IPO would assume. Accordingly the special rights granted to the Pre-IPO Investor which were not generally available to the public investors as set out in paragraph 3 above, including the right to nominate a non-executive director, were found to be inconsistent with the principles of Listing Rules 2.03(2) and (4).
11. The other arrangements of the Subscription Agreement including lock-up and public float met the technical requirements as memorialised in Listing Decision HKEx-LD36-1.
12. The Exchange did not require Director X to resign as his appointment to Company A's board had been agreed by the shareholders of Company A for his added value in improving corporate governance and ability to offer strategic business and financial input. Furthermore, Director X was appointed as a non-executive director and would not be participating in the daily management of Company A. Should there be a conflict between the decision of Company A's board and the rights of the Pre-IPO Investor, Director X would be obliged to abstain from voting at such meetings pursuant to Listing Rule 3.08 which requires every director, among others, in the performance of his duties as a director to avoid actual and potential conflicts of interest and duty and, including but without limitation, to act honestly and in good faith in the interests of Company A. This is also consistent with Listing Rule 2.03(5) whereby directors of Company A are to act in the interests of its shareholders as a whole. However in the event Director X resigned, the right of the Pre-IPO Investor to nominate a non-executive director to represent its interest in Company A would no longer exist.

THE DECISION

13. Based on the facts and circumstances that:
- (i) the special rights only available to the Pre-IPO Investor were removed;
 - (ii) the other arrangements of the Subscription Agreement met the technical requirements memorialised in Listing Decision HKEx-LD36-1;
 - (iii) Director X would abstain from voting should there be a conflict between the decisions of Company A's board and the rights of the Pre-IPO Investor; and
 - (iv) Director X would undertake to fulfil fiduciary duties and duties of skill, care and diligence as required under Listing Rule 3.08, including to act in the interests of the Company as a whole,

the Exchange determined that the issue could be addressed by way of disclosure in the prospectus.