HKEx LISTING DECISION
HKEx-LD99-3 (Published in July 2010) (Updated in July 2014)

Parties	Company X – a Main Board issuer The Investor – an institutional investor which proposed to subscribe for convertible bonds to be issued by Company X
Issue	Whether certain special rights available only to the Investor under the convertible bonds would comply with the general principles in Rule 2.03
Listing Rules	Main Board Rules 2.03(4), 14A.36~~14A.18~~, paragraph 4(3) of Appendix 3
Decision	The special rights available only to the Investor would contravene the general principle of fair and equal treatment of shareholders under Rule 2.03(4)

FACTS

1. Company X was in financial difficulties. It proposed to issue convertible bonds (the **Bonds**) to the Investor for general working capital and to redeem existing convertible bonds which were due for redemption within a year.

2. Under the terms of the Bonds, the following events (the Events) would trigger Company X's obligation to redeem the Bonds early from the Investor at a substantial premium:

   a. Company X's shareholders exercising their right to remove any directors nominated by Company A (**Event 1**).

   b. Company X failing to obtain shareholder approval for renewal of certain continuing connected transactions (**Event 2**).

3. Company X submitted that these terms were agreed on an arm's length basis taking into account its special circumstances at that time, and were necessary to attract new investors.

APPLICABLE LISTING RULES

4. Rule 2.03 states that the Rules are designed to ensure that investors have and can maintain confidence in the market and in particular that:

…

(4) all holders of listed securities are treated fairly and equally …

5. Rule 14A.36~~14A.18~~ states that:

> The connected transaction must be conditional on shareholders' approval at a general meeting held by the listed issuer. Any shareholder who has a material interest in the transaction must abstain from voting on the resolution.
> ~~the Exchange will require that connected transactions and continuing connected transactions are made conditional on prior approval by the shareholders of the listed issuer. The listed issuer must ensure that the following parties abstain from voting at the relevant meeting on resolution(s) approving the relevant transactions:~~
>
> ~~(1) any connected person with a material interest in the transaction; and~~
>
> ~~(2) any person falling within rules 14A.13(1)(b)(i) to (iv) that has a material interest in the transaction and its associates,~~

6. Appendix 3 to the Rules requires that the articles of association must conform with the following provisions:

> 4(3) That, where not otherwise provided by law, the issuer in general meeting shall have power by ordinary resolution to remove any director … before the expiration of his period of office.

ANALYSIS

7. Rule 2.03 describes the general principles and states that the Rules are designed to ensure that investors have and can maintain confidence in the market. It seeks to secure for shareholders certain assurances and equality of treatment which their legal position might not otherwise provide. One of the general principles is that all shareholders are treated fairly and equally (Rule 2.03(4)).

8. Here, Company X proposed to issue the Bonds under a general mandate and hence no specific shareholder approval would be required under the Rules.

9. The terms of the Bonds caused a concern that the rights and interests of Company X's shareholders might be prejudiced in that:

a. Appendix 3 to the Rules requires that an issuer's articles of association give shareholders the right to remove directors by ordinary resolution in a general meeting. The terms of the Bonds did not expressly prohibit shareholders from exercising this right. However, given Company X's financial difficulties and the substantial financial compensation payable by it if the shareholders exercised their right to remove directors nominated by Company A (Event 1), the right was unreasonably fettered.

b. The connected transaction rules seek to safeguard against connected persons taking advantage of their positions to the detriment of minority shareholders by requiring connected transactions to be disclosed and subject to independent shareholder approval. Similarly, the financial compensation payable by Company X if any of the continuing connected transactions were not renewed (Event 2) would effectively fetter shareholders' right to vote against those transactions.

10. Given the implications of the redemption obligations in respect of the Events, the Investor would effectively be given special rights not available to other shareholders of Company X. This would contravene Rule 2.03(4).

CONCLUSION

11. The Exchange requested Company X to address the issue. In response, Company X and the Investor agreed to remove the early redemption requirements concerning the Events.