

HKEX LISTING DECISION

HKEX-LD99-2 (Published in July 2010) (Updated in April 2015 and withdrawn in July 2018)

[See Main Board Rules 7.19(1), 7.24A(1) and 13.36]

Parties	Company A – a Main Board issuer Company B – the subscriber of convertible bonds issued by Company A, and the sole underwriter of an open offer made by Company A
Issue	Whether a proposed Open Offer with a condition to issue a minimum amount of new shares to Company B, and issue of the convertible bonds required shareholder approval
Listing Rules	Main Board Rules 7.23, 13.36
Decision	The proposed Open Offer and issue of the convertible bonds required shareholder approval unless the condition was removed

FACTS

1. Company A proposed to raise funds without specific shareholder approval through:
 - a. An open offer of new shares to be issued pro rata at a discount of 40% to the latest closing price (the **Open Offer**). This would be fully underwritten by Company B on condition that it would acquire shares representing at least 6% of Company A's existing share capital (the **Condition**). The Open Offer would represent not more than 20% of Company A's existing share capital and would be below the 50% threshold that requires shareholder approval under Rule 7.24(5).
 - b. Issuing convertible bonds to Company B under a general mandate. The bonds would be convertible into shares representing 13% of Company A's existing share capital. Company B's agreement to subscribe was subject to the completion of the Open Offer, which was not conditional on the issue of the convertible bonds.
2. If Company B took up as underwriter all the new shares issued under the Open Offer and fully converted all the convertible bonds, it would obtain new shares representing approximately 30% of Company A's existing share capital. If it took up all the new shares issued under the Condition and fully converted all the

convertible bonds, it would obtain new shares representing approximately 19% of Company A's existing share capital.

APPLICABLE LISTING RULES

3. Rule 7.23 defines an open offer to mean:

An offer to existing holders of securities to subscribe securities, whether or not in proportion to their existing holdings which are not allotted to them on renounceable documents. ...

4. Rule 7.24(5) states that:

if the proposed open offer would increase either the number of issued shares or the market capitalisation of the issuer by more than 50% (on its own or when aggregated with any other open offers or rights issues announced by the issuer (i) within the 12 month period immediately preceding the announcement of the proposed open offer or (ii) prior to such 12 month period where dealing in respect of the shares issued pursuant thereto commenced within such 12 month period, together with any bonus securities, warrants or other convertible securities (assuming full conversion) granted or to be granted to shareholders as part of such rights issues or open offers):

- (a) the open offer must be made conditional on approval by shareholders in general meeting by a resolution on which any controlling shareholders and their associates or, where there are no controlling shareholders, directors (excluding independent non-executive directors) and the chief executive of the issuer and their respective associates shall abstain from voting in favour. The issuer must disclose the information required under rule 2.17 in the circular to shareholders;

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5. Rule 13.36 states that:

- (1) (a) Except in the circumstances mentioned in rule 13.36(2), the directors of the issuer ... shall obtain the consent of shareholders in general meeting prior to allotting, issuing or granting:—
- (i) shares;
- (ii) securities convertible into shares; or ...

Note: Importance is attached to the principle that a shareholder should be able to protect his proportion of the total equity by having the opportunity to subscribe for any new issue of equity securities. Accordingly, unless shareholders otherwise permit, all issues of equity securities by the issuer must be offered to the existing shareholders (and, where appropriate, to holders of other equity securities of the issuer entitled to be offered them) pro rata to their existing holdings, and only to the extent that the securities offered are not taken up by such persons may they be allotted or issued to other persons or otherwise than pro rata to their existing holdings. This principle may be waived by the shareholders themselves on a general basis, but only within the limits of rules 13.36(2) and (3).

(2) No such consent as is referred to in rule 13.36(1)(a) shall be required:—

(a) for the allotment, issue or grant of such securities pursuant to an offer made to the shareholders of the issuer ... pro rata ... to their existing holdings; or

...

(b) if, but only to the extent that, the existing shareholders of the issuer have by ordinary resolution in general meeting given a general mandate to the directors of the issuer, either unconditionally or subject to such terms and conditions as may be specified in the resolution, to allot or issue such securities or to grant any offers, agreements or options which would or might require securities to be issued, allotted or disposed of, whether during the continuance of such mandate or thereafter, subject to a restriction that the aggregate number of securities allotted or agreed to be allotted must not exceed the aggregate of (i) 20% of the number of issued shares of the issuer as at the date of the resolution granting the general mandate (or in the case of a scheme of arrangement involving an introduction in the circumstances set out in rule 7.14(3), 20% of the number of issued shares of an overseas issuer following the implementation of such scheme) and (ii) the number of such securities repurchased by the issuer itself since the granting of the general mandate (up to a maximum number equivalent to 10% of the number of issued shares of the issuer as at the date of the resolution granting the repurchase mandate), provided that the

existing shareholders of the issuer have by a separate ordinary resolution in general meeting given a general mandate to the directors of the issuer to add such repurchased securities to the 20% general mandate.

...

- (5) In the case of a placing of securities for cash consideration, the issuer may not issue any securities pursuant to a general mandate given under rule 13.36 (2)(b) if the relevant price represents a discount of 20% or more to the benchmarked price of the securities, such benchmarked price being the higher of:
- (a) the closing price on the date of the relevant placing agreement or other agreement involving the proposed issue of securities under the general mandate; and
 - (b) the average closing price in the 5 trading days immediately prior to the earlier of:
 - (i) the date of announcement of the placing or the proposed transaction or arrangement involving the proposed issue of securities under the general mandate;
 - (ii) the date of the placing agreement or other agreement involving the proposed issue of securities under the general mandate; and
 - (iii) the date on which the placing or subscription price is fixed, unless the issuer can satisfy the Exchange that it is in a serious financial position and that the only way it can be saved is by an urgent rescue operation which involves the issue of new securities at a price representing a discount of 20% or more to the benchmarked price of the securities or that there are other exceptional circumstances. The issuer shall provide the Exchange with detailed information on the allottees to be issued with securities under the general mandate.

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ANALYSIS

6. The general principle is that a shareholder should be able to protect his proportion of the total equity by having the opportunity to subscribe for any new issue of shares. Accordingly, unless the shareholders otherwise permit, all issues of shares must be first offered to them pro rata to their existing holdings, and only to the extent that the shares are not taken up by them may they be allotted or issued to other persons or otherwise than pro rata to their existing shareholdings. This principle may be waived by the shareholders on a general basis, but only within the limit of Rules 13.36(2) and (3).
7. In this case, since the Open Offer would be below the 50% threshold under Rule 7.24(5), it did not require shareholder approval. However, the Exchange considered that the Condition in the Open Offer was effectively a placing of new shares to Company B. It followed that since the shares were proposed to be issued at a discount greater than the 20% limit for share placement under Rule 13.36(5), Company A should obtain a specific mandate from the shareholders before proceeding with the Open Offer.
8. The proposed issue of the convertible bonds was subject to the completion of the Open Offer. The Exchange was concerned that in substance the Open Offer and the issue of the convertible bonds could be a package deal structured to circumvent the shareholder approval requirement.

CONCLUSION

9. To address the Exchange's concern, Company A and Company B removed the Condition from the Open Offer.