HKEx LISTING DECISION
HKEx-LD60-2013 (Published in April 2013) (Updated in July 2014, October 2019 (Rule amendments))

Summary	
Parties	Company A – a Main Board listed issuer The Target – a subsidiary of Company A Company B – a substantial shareholder of certain subsidiaries of the Target
Issue	Whether the Exchange would accept Company A's proposed alternative revenue ratio for classifying certain continuing connected transactions with Company B
Listing Rules	Main Board Rule 14A.80
Decision	The Exchange accepted the proposed alternative revenue ratio

FACTS

1. Company A recently completed the acquisition of the Target (the **Acquisition**) and accounted for it as a subsidiary. As Company B was the substantial shareholder of certain subsidiaries of the Target, it became a connected person of Company A.

2. After the Acquisition, the Target and its subsidiaries (the **Target Group**) would continue to purchase certain raw materials from Company B (the **Procurement Transactions**). Based on the annual cap for these continuing connected transactions, the revenue ratio was about 11% while the asset ratio and consideration ratio were less than 4%.

3. Company A submitted that its group had been substantially enlarged as a result of the Acquisition. However, the revenue ratio was calculated using the revenue shown in its latest published audited consolidated accounts and did not take into account the Target's results. This contrasted with the asset ratio where Company A could adjust its total assets to include the value of the Acquisition based on the information published according to the Rules.

4. Company A considered that the revenue ratio was anomalous. It proposed an alternative revenue ratio using the enlarged group's revenue shown in the pro forma consolidated income statement published in the circular for the Acquisition

(the **Circular**) under Chapter 14 of the Rules. The pro forma information was derived from Company A's latest published audited consolidated accounts and the accountants' report on the Target Group, with pro forma adjustments relating to the Acquisition.

5. Based on the alternative revenue ratio of about 2% and the other size test calculations, the Procurement Transactions were exempt from the independent shareholder approval requirement under the de minimis exemption.

APPLICABLE LISTING RULES

6. Rule 14.07(3) provides the calculation of a revenue ratio as follows:

> the revenue attributable to the assets which are the subject of the transaction divided by the revenue of the listed issuer (see in particular rule 14.14 and 14.17);

7. Rule 14.20 provides that:

> the Exchange may, where any of the calculations of the percentage ratios produces an anomalous result or is inappropriate to the sphere of activity of the listed issuer, disregard the calculation and substitute other relevant indicators of size, including industry specific tests. The listed issuer must provide alternative tests which it considers appropriate to the Exchange for consideration.

8. Rule 14A.80 provides that:

> if any percentage ratio produces an anomalous result or is inappropriate to the activity of the listed issuer, the Exchange may disregard the ratio and consider alternative test(s) provided by the listed issuer. The listed issuer must seek prior consent of the Exchange if it wishes to apply this rule.

ANALYSIS

9. Rule 14.07 sets out five percentage ratios for assessing the impact of a transaction on an issuer. They form the basis for classifying the transaction which determines whether the transaction is subject to any disclosure, reporting and/or shareholders' approval requirements under Chapter 14 or 14A.

10. The revenue ratio measures the materiality of a transaction by reference to the issuer's latest revenue figure as shown in its annual accounts.

11. In this case, the Exchange noted that:

- The Procurement Transactions were conducted by the Target Group in the ordinary and usual course of business. They constituted continuing connected transactions for Company A as a result of the Acquisition. It would be reasonable to take into account the Target Group's results when assessing the materiality of the Procurement Transactions.

- The pro forma financial information of the enlarged group was prepared in respect of the most recently completed financial year and published in the Circular according to the Rules. The alternative revenue ratio calculated using the revenue shown in the pro forma income statement would be acceptable.

CONCLUSION

12. The Exchange accepted Company A's proposal to disregard the revenue ratio and to use the alternative size test for classifying the Procurement Transactions.

Note: On 1 October 2019, Rules 14.20 and 14A.80 were amended to clarify that if any calculation of the percentage ratio produces an anomalous results or is inappropriate to the sphere of activities of the issuer, the Exchange (or the issuer) may apply an alternative size test that it considers appropriate to assess the materiality of a transaction under Chapters 14 and 14A.

The Rule amendments would not change the analysis and conclusion in this case.