Guidance Materials for Listed Issuers (Consolidated)

June 2025

Table of Contents

7 Public float

8 Transfer of listing from GEM to Main Board

9 Repurchase of securities and treasury shares

9.1 Repurchase of securities
9.2 Treasury shares

10 Continuing obligations

11 Notifiable transactions

11.1 Backdoor listings
11.2 Definition of transactions and calculation of percentage ratios
11.3 Aggregation of transactions
11.4 Shareholders' approval requirement
11.5 Disclosure and other requirements
11.6 Online display of documents
11.7 PRC filing requirements for overseas listings and securities offerings by Mainland companies

12 Connected transactions

12.1 Definition of connected persons and deeming provisions
12.2 Definition of connected transactions and calculation of percentage ratios
12.3 Continuing connected transactions
12.4 Aggregation of transactions
12.5 Shareholders' approval requirement
12.6 Exemptions from the connected transaction requirements
12.7 Disclosure and other requirements

13 Share schemes

14 Issuers listed under special listing regimes or other listing structures

14.1 Overseas issuers
14.2 Mineral companies
14.3 SPACs
14.4 Collective investment schemes

15 Spin-offs

16 Core shareholder protection standards

17 Corporate governance / environmental, social and governance / securities transactions by directors

17.1 Corporate governance code
17.2 Environmental, social and governance reporting code
17.3 Model code for securities transactions by directors of listed issuers

18 Other topics

18.1 Contractual arrangements
18.2 Special rights
18.3 Issuers associated with gambling activities
18.4 Stock Connect
18.5 Listing fees

1

Directors and senior management

1.1 Directors

1.2 Company secretaries

Whether an individual was qualified to act as a listed issuer's independent non-executive director having appropriate professional qualifications or accounting or related financial management expertise

Parties

- **Company A** – a Main Board issuer
- **Mr X** – Company A's proposed independent non-executive director

Facts

1. Company A proposed to appoint Mr X as an independent non-executive director.

2. It submitted that Mr X had the professional qualifications and accounting expertise required under Rule 3.10(2) because:

   a. He was a certified public accountant in the Mainland.

   b. He had worked as a principal accountant in a firm of certified public accountants in the Mainland (**Mainland CPA firm**) for 7 years and thereafter as a partner at another Mainland CPA firm for 8 years. He was the auditor-in-charge at a company listed on a stock exchange in the Mainland.

Relevant Listing Rules

3. Rule 3.10(2) states that:

   at least one of the independent non-executive directors must have appropriate professional qualifications or accounting or related financial management expertise.

   Note: With regard to "appropriate accounting or related financial management expertise", the Exchange would expect the person to have, through experience as a public accountant or auditor or as a chief financial officer, controller or principal accounting officer of a public company or through performance of similar functions, experience with internal controls and in preparing or auditing comparable financial statements or experience reviewing or analysing audited financial statements of public companies. It is the responsibility of the board to determine on a case-by-case basis whether the candidate is suitable for the position. In making its decision, the board must evaluate the totality of the individual's education and experience.

Analysis

4. The Exchange accepted that Mr X fulfilled Rule 3.10(2). Mr X's qualification as a certified public accountant in the Mainland and experience in accounting and auditing in the Mainland were relevant for considering his suitability to act as Company A's independent non-executive director under Rule 3.10(2).

Conclusion

5. Mr X was qualified to act as Company A's independent non-executive director under Rule 3.10(2).

Directors

Directors' training

1. Is there any prescribed form of training for directors? Would the training provided by the Exchange be considered as "continuous professional development" (CPD) for the purpose of MB Rule 3.09F / GEM Rule 5.02F?

The Exchange does not specify the format of director training. Different types of training may be counted as CPD, provided that the topics of such training fall within the scope of the topics specified in MB Rule 3.09G / GEM Rule 5.02G.

Directors' CPD may consist of external training, internal training or self-study e.g. attending in-house briefings, giving talks, attending training relevant to the listed issuer's business conducted by lawyers, and reading material relevant to the director's duties and responsibilities.

If a listed issuer's director has completed training by watching e-learning webcasts and videos provided by the Exchange on its website, such training would be considered as part of a director's CPD. Please refer to the Exchange's Corporate Governance Practices on the HKEX website for various training resources.

The training received by directors should be of sufficient quality to adequately support them in developing their knowledge and expertise. Directors should therefore consider the appropriate mode of training for each of the specified topics.

MB Rules 3.09F
GEM Rules 5.02F
First released: December 2011; last updated: May 2025

2. If a director sits on the board of several listed issuers, can the same training record be provided to each listed issuer for the purpose of compliance with the disclosure requirement in MDR paragraph B(i)?

Yes, provided that the training received is not issuer specific.

MB App C1 – MDR paragraph B(i) and Principle C.1
GEM App C1 – MDR paragraph B(i) and Principle C.1
First released: December 2011; last updated: May 2025

3. MB 3.09F / GEM Rule 5.02F states that all directors are required to receive CPD in each financial year of the listed issuer (General Director Training Requirement). Can the following count towards a director's compliance with the General Director Training Requirement:

(i) Training received to satisfy the training requirements of other organisations or professional associations that the director is subject to (e.g. CPD training requirements for solicitors or accountants);

(ii) Training received by the director in his / her capacity as a director of an issuer listed on an exchange other than the Main Board or GEM of the Exchange; and

(iii) Where a director is appointed during a listed issuer's financial year, training received by such director during the year before his / her appointment?

Yes, (i), (ii) and (iii) can all count towards a director's compliance with the General Director Training Requirement, provided that the topics of such training fall within the scope of the topics specified in MB Rule 3.09G / GEM Rule 5.02G.

MB Rules 3.09F and 3.09G
GEM Rules 5.02F and 5.02G
First released: May 2025

4. Please explain how the General Director Training Requirement and the requirement for first-time directors to complete minimum training hours within 18 months of their date of appointment (First-Time Director Training Requirement) apply to directors of listed issuers.

Regardless of their date of appointment, all directors of listed issuers as at 1 July 2025 will be subject to the General Director Training Requirement from the financial year commencing on or after 1 July 2025.

First-time directors who are appointed on or after 1 July 2025 will be required to complete 12 or 24 hours of training (as applicable) within 18 months of their date of appointment under the First-Time Director Training Requirement. During the relevant period, such directors may use the same training to satisfy the First-Time Director Training Requirement and the General Director Training Requirement. For the avoidance of doubt, first-time directors who are appointed before 1 July 2025 will not be subject to the First-Time Director Training Requirement.

MB Rules 3.09F and 3.09H
GEM Rules 5.02F and 5.02H
First released: May 2025

5. What information should a listed issuer disclose in its corporate governance report in respect of the training received by a director who is subject to the First-Time Director Training Requirement?

The listed issuer should disclose details of the training that the director completed within the relevant financial year in accordance with MDR paragraph B of the Corporate Governance Code, including the number of hours completed, mode of training and training topics covered.

Where the director has not yet completed the required training in that financial year, for transparency, the listed issuer should also disclose the remaining number of training hours to be completed by the director in the next financial year. On the other hand, where the director has completed the required training, the listed issuer should include a statement confirming the completion of such training.

MB Rule 3.09H and App C1 – MDR paragraph B(i)
GEM Rule 5.02H and App C1 – MDR paragraph B(j)
First released: May 2025

6. If a first-time director ceases to be a director of an issuer listed on the Main Board or GEM of the Exchange (HK Listed Issuer) prior to completing the required number of minimum training hours, would the training previously received count if he / she is subsequently appointed as a director of another HK Listed Issuer?

Yes, provided that the time gap between the conclusion of the first appointment and the subsequent appointment is within three years. The director would only be required to complete his / her remaining balance of training hours under the First-Time Director Training Requirement within 18 months from the date of the subsequent appointment.

However, if the time gap between the appointments exceeds three years, the director would be required to complete the full 12 or 24 hours of training (as applicable) within 18 months from the date of the subsequent appointment.

First-time directors are encouraged to complete their training as soon as possible to ensure that they can effectively discharge their duties and contribute to the board in a timely manner.

MB Rule 3.09H and Note 2 thereto
GEM Rule 5.02H and Note 2 thereto
First released: May 2025

Independent non-executive directors

7. What are "appropriate professional qualifications" referred to by MB Rule 3.10(2) / GEM Rule 5.05(2)?

In this Rule, "appropriate professional qualifications" normally means professional accounting qualifications.

(i) Is a professional qualification obtained from an overseas jurisdiction acceptable, such as a PRC or Singapore qualified accountant?

Yes, a professional qualification obtained from a recognised body in an overseas jurisdiction would be acceptable.

(ii) Can a solicitor be said to have appropriate professional qualifications, or does the individual need to have the appropriate experience?

A person with a legal qualification is acceptable if that person possesses "appropriate accounting or related financial management expertise" as required by MB Rule 3.10(2) / GEM Rule 5.05(2). The Exchange may question the factors the board has considered when making its decision to accept that person as being in compliance with the Rule.

MB Rule 3.10(2)
GEM Rule 5.05(2)
First released: December 2011; last updated: May 2025

8. Can a person who has served on the audit committee of a listed issuer for a number of years be considered to have the appropriate accounting or related financial management expertise required under MB Rule 3.10(2) / GEM Rule 5.05(2)?

Note to MB Rule 3.10(2) / GEM Rule 5.05(2) provides further clarification as to what the appropriate expertise means. Prima facie, we would not consider a person whose only experience has been serving as a member of an audit committee as able to fulfil the criteria set out in the note to the Rule.

MB Rule 3.10(2)
GEM Rule 5.05(2)
First released: December 2011; last updated: May 2025

9. Is experience with a non-public company acceptable as having the appropriate accounting or related financial management expertise required under MB Rule 3.10(2) / GEM Rule 5.05(2)?

Generally no, but the Exchange recognises that the experience and scope of duties of such a candidate may demonstrate that the individual is capable of discharging the role required of such person as set out in the Rule. We expect the board to evaluate the totality of the individual's experience and education when making its decision as to whether the individual is appropriate.

MB Rule 3.10(2)
GEM Rule 5.05(2)
First released: December 2011; last updated: May 2025

10. If an existing non-executive director (NED) meets the independence requirements, can the NED be re-designated as an independent non-executive director (INED)? Does an announcement need to be made for the re-designation?

Yes, an existing NED may be re-designated as an INED, but we will consider the individual's present or past relationship with the listed issuer or a connected person on a case-by-case basis. Where, in order to meet MB Rule 3.13 / GEM Rule 5.09 requirements, a director needs to comply with any relevant cooling off period under the Listing Rules, the relevant cooling off period needs to have ended by the date on which the individual confirmation of independence is given.

An announcement will need to be made for the re-designation from being a NED to an INED pursuant to MB Rule 13.51(2) / GEM Rule 17.50(2).

MB Rules 3.13 and 13.51(2)
GEM Rules 5.09 and 17.50(2)
First released: December 2011; last updated: May 2025

11. If a listed issuer designates an INED as the Lead INED, does an announcement need to be made for such a designation?

No, designation as a Lead INED does not fall within the types of director changes that require an announcement to be made pursuant to MB Rule 13.51(2) / GEM Rule 17.50(2).

CP B.1.2 of the Corporate Governance Code requires listed issuers to maintain an updated list of directors on their website and the Exchange's website. For transparency, listed issuers with a Lead INED should publicise any change in Lead INED designation as soon as possible by publishing an updated list of directors and their roles and functions.

MB Rule 13.51(2) and App C1 – CP B.1.2
GEM Rule 17.50(2) and App C1 – CP B.1.2
First released: May 2025

Tenure of independent non-executive directors

12. A listed issuer must not have INEDs who have served for a period of nine years or more (Long Serving INEDs) representing a majority of its INEDs as at the conclusion of a listed issuer's first annual general meeting (AGM) held on or after 1 July 2028. Please clarify whether the Exchange would regard a 50/50 split between Long Serving INEDs and non-Long Serving INEDs to be in compliance with this requirement.

The Exchange expects non-Long Serving INEDs to represent a majority (i.e. more than 50%) of the INEDs of a listed issuer by the end of phase one of the cap on INED tenure. This is consistent with the objective of the cap to promote regular board refreshment, with a view to phasing out all Long Serving INEDs by the end of the transition period.

Note 1 to MB Rule 3.13A
Note 1 to GEM Rule 5.09A
First released: May 2025

13. Where a NED is re-designated as an INED, would the individual's previous tenure as a NED be counted towards the calculation of his / her nine-year tenure for the purpose of the cap on INED tenure?

For the purpose of MB Rule 3.13A / GEM Rule 5.09A, "a period of nine years" will be counted from the date of appointment of an INED.

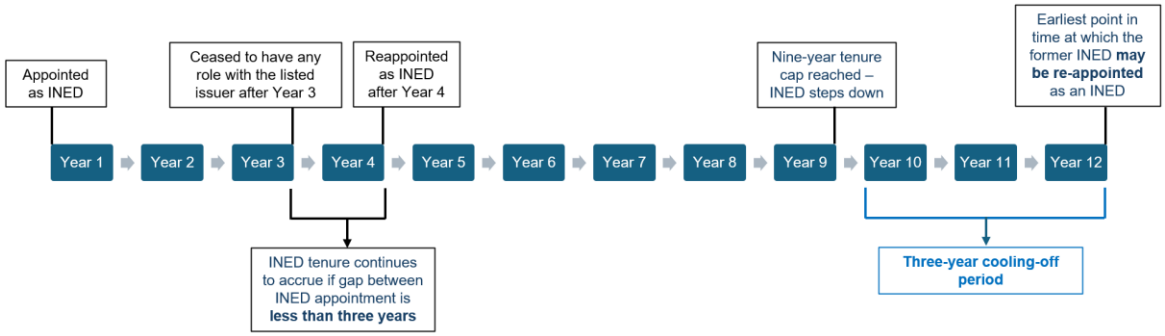
In the above scenario, the individual's nine-year tenure for the purpose of the cap on INED tenure will be counted from the date of his / her re-designation as an INED (i.e. the individual's previous tenure as a NED will not be counted).

Note 2 to MB Rule 3.13A
Note 2 to GEM Rule 5.09A
First released: May 2025

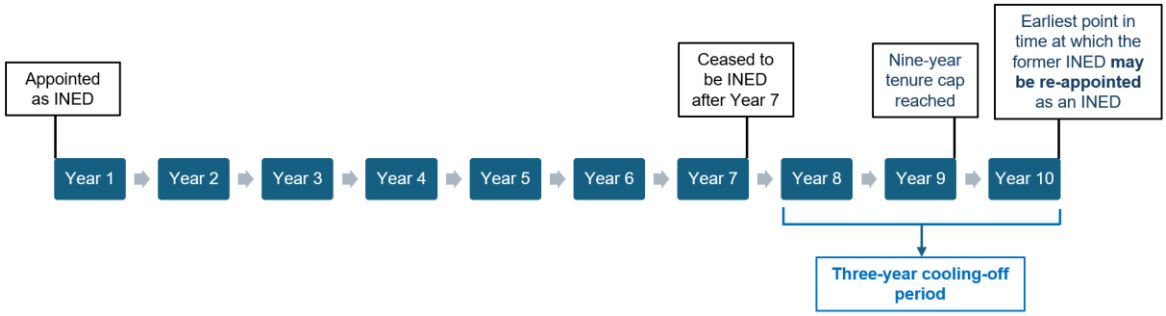
14. Note 2 to MB Rule 3.13A / GEM Rule 5.09A provides that where an individual ceases to be an INED of a listed issuer for a period(s) of less than three years (prior to serving as an INED for nine years), such period(s) will be counted towards the calculation of the nine-year tenure cap under MB Rule 3.13A / GEM Rule 5.09A. Further, a previous Long Serving INED may be re-appointed as an INED of the same listed issuer upon the expiry of a three-year cooling-off period in accordance with Note 3 to MB Rule 3.13A / GEM Rule 5.09A. Please provide some examples to illustrate the application of these requirements in practice.

Please refer to the illustrative examples below:

Illustrative example 1 – a former INED is re-appointed as an INED by the same listed issuer

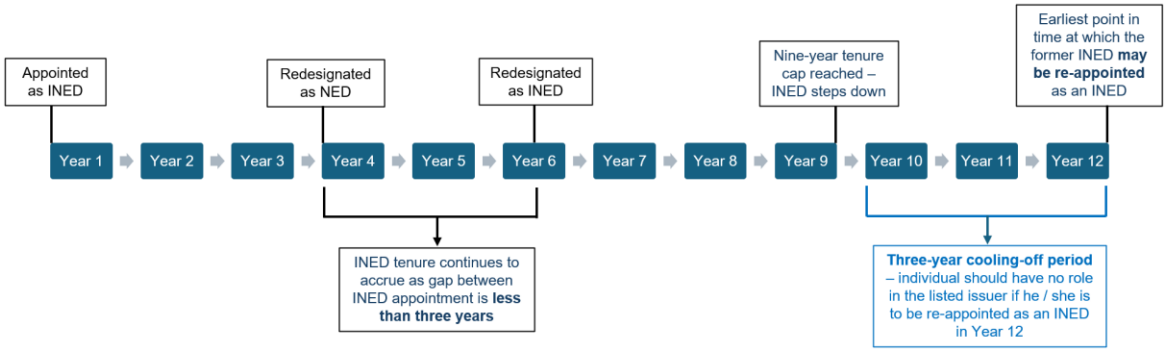


Illustrative example 2 – an INED steps down prior to reaching the nine-year tenure cap



If a Long Serving INED is re-designated as a NED (rather than stepping down from the listed issuer's board), the individual will need to observe a three-year cooling-off period (during which he / she does not have any role on the board of the listed issuer, its holding company or any of their respective subsidiaries or any core connected persons of the listed issuer) before he / she can be re-appointed as an INED of the same listed issuer.

Illustrative example 3 – an INED is re-designated as a NED prior to reaching the nine-year tenure cap



Notes 2 and 3 to MB Rule 3.13A
Notes 2 and 3 to GEM Rule 5.09A
First released: May 2025

15. Where a listed issuer changes its listing status from a secondary listing to a dual-primary / primary listing on the Exchange, how is the tenure of the listed issuer's INEDs calculated for the purpose of the cap on INED tenure?

The nine-year tenure cap requirement on INED tenure does not apply to secondary listed issuers. Accordingly, the nine-year tenure of the INEDs of a listed issuer who changes its listing status from secondary listing to dual-primary or primary listing on the Exchange will be counted from the date of its primary listing on the Exchange. As such, although the INEDs of such a listed issuer may be appointed at different dates, they will reach the nine-year tenure cap at the same time under the Rules. To avoid abrupt changes in board composition, in these circumstances the listed issuer should plan ahead and periodically refresh its board.

For the purpose of disclosure in the corporate governance report, the listed issuer should disclose the total tenure of each director (i.e. as calculated from the date of the director's appointment). In addition, for completeness, the listed issuer should include a note to indicate the total tenure of each director since its primary listing date for the purpose of computing compliance with the nine-year tenure cap requirement.

Note 2 to MB Rule 3.13A
MB App C1 – MDR paragraph B(a)
First released: May 2025

16. During the transition period for the cap on INED tenure:

(a) How will the current requirements in the Corporate Governance Code in respect of Long Serving INEDs apply?

During the transition period, the relevant code provisions will continue to apply for the two different situations as below:

- For listed issuers where all INEDs are Long Serving INEDs, the requirements on tenure disclosure in the shareholder circular and new INED appointment will continue to apply for any relevant AGM held on or before 30 June 2028 (i.e. the expiry of phase one); and

- For listed issuers where certain of their INEDs are Long Serving INEDs, the requirements on the re-election of Long Serving INEDs will continue to apply for any relevant AGM held on or before 30 June 2031 (i.e. the expiry of phase two).

(b) Is it necessary to re-elect a Long Serving INED every year at the AGM(using a separate AGM resolution)? Alternatively, can a listed issuer continue to re-elect Long Serving INEDs on a regular rotation basis in accordance with its constitutional documents?

The Corporate Governance Code does not require a listed issuer to consider the election of Long Serving INEDs every year. The listed issuer may continue to elect Long Serving INEDs on a regular rotation basis in accordance with its constitutional documents. However, under CP B.2.3, such further appointment should be subject to a separate resolution to be approved by shareholders.

Listed issuers with Long Serving INEDs should conduct comprehensive succession planning to phase out their Long Serving INEDs in an orderly and measured manner.

MB App C1 – CPs B.2.3 and B.2.4
GEM App C1 – CPs B.2.3 and B.2.4
First released: December 2011; last updated: May 2025

Overboarding

17. INEDs who hold seven (or more) Hong Kong listed issuer directorships (Overboarding INEDs) must comply with the cap of six concurrent Hong Kong listed issuer directorships by the first AGM held on or after 1 July 2028 by any listed issuer that an Overboarding INED serves. How will the current requirements in the Corporate Governance Code in respect of Overboarding INEDs apply during the transition period for the cap on overboarding?

During the transition period, the disclosure requirements in respect of the election of Overboarding INEDs will continue to apply for any relevant general meeting held on or before 30 June 2028.

MB Rule 3.12A, App C1 – CP B.3.4(b)
GEM Rule 5.07A, App C1 – CP B.3.4(b)
First released: May 2025

Procedures for election of directors

18. If the procedures for shareholders to propose a person for election as a director are set out in a listed issuer's constitutional documents (which are already required to be published on its website and the Exchange's website), does the listed issuer need to separately publish these procedures on its website?

Yes, we expect the listed issuer to publish the procedures separately on its website to facilitate shareholders to locate the procedures.

MB Rule 13.51D
GEM Rule 17.50C
First released: December 2011; last updated: May 2024

19. Are listed issuers required to publish on their websites the procedures for director election in both English and Chinese?

Yes.

MB Rule 13.51D
GEM Rule 17.50C
First released: December 2011; last updated: May 2024

General

20. Will directors still be subject to criminal liability for false or misleading information which they provide to the Exchange after the removal of the submission requirement of directors' undertakings?

Yes. Since the directors' undertakings under the repealed Form 5B of the MB Rules (or the repealed Form 6A of the GEM Rules) have been codified into the Listing Rules, a director or supervisor who provides information to the Exchange which is false or misleading in a material particular, may be in breach of section 384 of the Securities and Futures Ordinance, and therefore subject to the criminal sanctions imposed by that section.

MB Rules 3.09B, 3.09C and 3.09D
GEM Rules 5.02B, 5.02C and 5.02D
First released: December 2011; last updated: May 2025

HKEX Guidance Letter
HKEX-GL108-20

August 2020 (Updated in January 2024)

Experience and qualification of a company secretary

I. Purpose

1. This letter provides guidance on the requirements of company secretaries of new listing applicants and listed issuers, which is also set out in Chapter 3.10 of the Guide for New Listing Applicants. This letter also provides examples of company secretaries that meet the experience requirement.

II. Relevant Listing Rules

2. MB Rule 3.28 (GEM Rule 5.14) requires a company secretary of an issuer to possess certain academic or professional qualifications, or relevant experience to be considered capable of discharging the functions of company secretary:

Acceptable Qualification or **Relevant Experience**

The academic or professional qualifications to be considered acceptable by the Exchange (**Acceptable Qualification**) include:

(i) A Member of The Hong Kong Chartered Governance Institute;

(ii) A solicitor or barrister under the Legal Practitioners Ordinance (Cap. 159); and

(iii) A certified public accountant (as defined in the Professional Accountants Ordinance (Cap. 50)).

The Exchange's assessment criteria for relevant experience (**Relevant Experience**)[1] include:

(a) Length of employment with the issuer and other issuers and the roles the company secretary has played;

(b) Familiarity with the Listing Rules and other relevant laws and regulations;

(c) Relevant training taken and/or to be taken in addition to the minimum requirement under MB Rule 3.29 (GEM Rule 5.15) (i.e. 15 hours per financial year); and

(d) Professional qualifications in other jurisdictions.

[1] See examples in Appendix for company secretaries that meet the experience requirement.

III. Guidance

3. Issuers tend to appoint senior management members, or other employees that had served related roles for a period of time and are familiar with the issuer's business and affairs as company secretary. However, these individuals may not possess the Acceptable Qualification or Relevant Experience as required under MB Rule 3.28 (GEM Rule 5.14). In addition, issuers with principal business activities outside Hong Kong may have practical difficulties in finding a company secretary who possesses day-to-day knowledge of their affairs and the Acceptable Qualification or Relevant Experience.

4. In view of the above, the Exchange has granted waivers to issuers proposing to appoint a company secretary who does not have the qualification and experience required (the **Proposed Company Secretary**) for a specified period. The Exchange will consider the factors set out below in a waiver application and any waiver, if granted, will be for a fixed period of time (**Waiver Period**) subject to the following conditions

Factors to be considered	Conditions for waiver
(i) Whether the issuer has principal business activities primarily outside Hong Kong; (ii) Whether the issuer is able to demonstrate the need to appoint a person who does not have the Acceptable Qualification or Relevant Experience as a company secretary; and (iii) Why the directors consider the Proposed Company Secretary to be suitable to act as the issuer's company secretary.	(iv) The Proposed Company Secretary must be assisted by a person who possesses the qualifications or experience as required under MB Rule 3.28 (GEM Rule 5.14) ("**Qualified Person**") and is appointed as a joint company secretary throughout the Waiver Period; and (v) The waiver will be revoked if there are material breaches of the Listing Rules by the issuer.

5. These conditions are intended to ensure (i) that the Qualified Person will assist the issuer to comply with relevant Hong Kong law and regulations and to achieve a good corporate governance standard; and (ii) a reasonable time is given to enable the Proposed Company Secretary to acquire the Relevant Experience (in particular, the familiarity with the relevant regulatory requirements) over time.

6. The length of the Waiver Period will depend on the following factors, but in any case, will not exceed three years as the Proposed Company Secretary is expected to have acquired the Relevant Experience within such period:

   (i) the Proposed Company Secretary's experience in handling company secretarial matters and his/her relevant professional qualifications and/or academic background;

   (ii) the measures and systems in place to facilitate the Proposed Company Secretary in discharging his/her duties as a company secretary; and

   (iii) the issuer's regulatory compliance and/or material deficiencies/weaknesses in internal controls.

7. Upon the end of the Waiver Period, the Exchange will not automatically deem the Proposed Company Secretary to be qualified under MB Rule 3.28 (GEM Rule 5.14). The issuer must demonstrate and seek the Exchange's confirmation that the Proposed Company Secretary, having had the benefit of the Qualified Person's assistance during the Waiver Period, has attained the Relevant Experience and is capable of discharging the functions of company secretary. The Exchange will assess each case based on the specific facts and circumstances, taking into consideration the following factors:

   (i) compliance history of the issuer during the Waiver Period; and

   (ii) the relevant training undertaken by the Proposed Company Secretary during the Waiver Period.

Guidance on disclosure

8. The issuer should disclose in its announcement:

   (i) reasons for the waiver;

   (ii) details and conditions of the waiver; and

   (iii) qualification and experience of both the Proposed Company Secretary and the Qualified Person.

Appendix – Examples of cases where the Exchange accepted that the company secretaries had Relevant Experience

Company A

1. Mr. X was a member of a reputable overseas professional body of accountants.

2. Before joining Company A, Mr. X was the chief financial officer of another issuer listed on the Exchange. In addition to financial management and reporting matters, he also participated in the preparation of the company's regulatory announcements and circulars.

3. He had regularly attended training courses relating to corporate governance, accounting and financial reporting, the Listing Rules and company law.

Company B

4. Mr. Y had participated in Company B's initial public offering preparation and application. After the listing of Company B, he had more than seven years of experience working closely with the retiring secretary and professional advisers in the company's secretarial and administrative matters.

5. During the past three years, he had attended approximately 70 hours of training courses on Listing Rule compliance, corporate governance and other related laws/regulations.

Company C

6. Mr. Z had been a director of a subsidiary of Company C (the **Subsidiary**, which was also listed on the Exchange) for more than eight years. He was also appointed as the chairman of the Subsidiary two years ago and before that, he held various other senior positions at the Subsidiary (including managing director and chief executive officer). He had been actively involved in the corporate governance of the Subsidiary and ensuring its compliance with the Listing Rules.

7. He was familiar with Company C's operations and business. He had been a member of Company C's senior management for about two years, and had over 20 years of experience in the same kind of business carried on by Company C.

Company secretaries

1. Does an accountant or lawyer acting as a listed issuer's company secretary fulfil the requirement to attend relevant professional training each year by attending continuing professional development (CPD) courses on subjects such as litigation and accounting standards?

We intend that the training should be broad rather than restrictive. Where legal and accounting courses are relevant to a company secretary's role and duties, they should count towards the 15-hour training requirement.

MB Rule 3.29
GEM Rule 5.15
First released: December 2011; last updated: May 2024

2. If a person is the company secretary of a listed issuer that is dual-listed on the Hong Kong and a PRC stock exchange and attends training courses relating to PRC listing requirements and regulations, can those courses be counted towards the 15-hour training requirement?

As the company secretary of a Hong Kong listed issuer, this person should also undergo training on Hong Kong rules and regulations. However, the Exchange does not prescribe specific types of courses that a company secretary should attend, as long as they are relevant to their professional duties. If the training courses are of a general nature (e.g. a course on corporate governance), and not specifically on any PRC rules and regulations, then they may count towards the 15-hour training requirement.

MB Rule 3.29
GEM Rule 5.15
First released: December 2011; last updated: May 2024

2

Compliance advisers and other professional advisers

2.1 Compliance advisers

Guidance letter – Guidance on the compliance adviser requirement for newly listed issuers	GL67-13	2.1 – 1

2.2 Independent financial advisers

Guidance letter – Guidance on opinion letters prepared by independent financial advisers	GL76-14	2.2 – 1
Listing decision – Whether a firm was qualified to act as an independent financial adviser	LD102-2	2.2 – 8

2.3 Property valuers

Listing decision – Whether an individual was qualified to prepare valuation reports for Mainland properties	LD102-1	2.3 – 1

Guidance on the compliance adviser requirement for newly listed issuers

A. Background and purpose

1. The objective of the compliance adviser requirements is to ensure that directors of newly listed issuers receive the guidance and advice of an appropriately qualified firm in the period immediately following listing.

2. This letter reminds newly listed issuers of their obligations under the compliance adviser rules and gives guidance to issuers on its communication with their compliance advisers.

B. Relevant Listing Rules

3. Under Main Board Rule 3A.19 (GEM Rule 6A.19), an issuer must retain a compliance adviser to assist its compliance with the Listing Rules and all other applicable laws and regulations commencing on its listing and until the publication of its financial results for the first full financial year after listing.

4. Main Board Rule 3A.23 (GEM Rule 6A.23) sets out specific circumstances under which a newly listed issuer is obliged to consult with, and if necessary, seek advice from their compliance advisers on a timely basis:

   - before publication of any regulatory announcement, circular or financial report;

   - where a transaction, which might be a notifiable or connected transaction, is contemplated including share issues, sales or transfers of treasury shares and share repurchases;

   - where the issuer proposes to use the listing proceeds differently to the manner detailed in the listing document or where the issuer's business activities, developments or results deviate from any forecast, estimate or other information in the listing document; and

   - where the Exchange makes an inquiry of the issuer under Main Board Rule 13.10 (GEM Rule 17.11).

5. Main Board Rule 3A.24 (GEM Rule 6A.24) sets out the compliance adviser's role in the circumstances described above. For example, a compliance adviser should:

   - no less frequently than at the time when the compliance adviser reviews the issuer's financial reporting and when notified of a proposed change of use of IPO proceeds, discuss with the issuer:

     - its operating performance, financial condition by reference to its business plan and the use of proceeds set out in its listing document;

     - its achievement of any profit forecast or estimate set out in its listing document; and

- its compliance with any waivers granted by and any undertakings provided to the Exchange.

- advise the issuer on any connected transaction waiver application; and

- assess the understanding of all new appointees to the board of the issuer regarding the nature of their responsibilities and fiduciary duties as a director.

6. A compliance adviser may also act as an additional communication channel to maximize the effectiveness of communication between an issuer and the Exchange, including:

- accompanying an issuer to attend meetings with the Exchange; and

- dealing with the Exchange in respect of any or all matters listed in paragraph 4 above.

C. Guidance

7. A compliance adviser should guide the newly listed issuer on compliance with the Listing Rules and all other applicable laws, rules, codes and guidelines. It could only discharge this responsibility upon being approached by the issuer for advice and provided with adequate information.

8. The Exchange notes that some issuers breached the Listing Rules because their directors and/or responsible officers did not clearly understand the Listing Rules and failed to consult with their compliance advisers. Accordingly, issuers are encouraged to work closely with their compliance advisers. In particular, it should

- proactively discuss and seek advice from its compliance adviser on matters described under paragraph 4 above as required by the Listing Rules;

- maintain regular contact with its compliance adviser and keep it appraised of developments and proposed corporate actions. Given the wide scope of circumstances specified in paragraph 4, an issuer who is unsure about whether its proposed corporate action is subject to a Listing Rule should proactively discuss and seek confirmation from its compliance adviser as soon as possible; and

- allow adequate time for the compliance adviser to review the matter and provide advice, and for the issuer to consider and if necessary, act on the advice. For example, given that the publication of an announcement is time critical, the issuer should ensure that its compliance adviser is notified and provided with the draft announcement and information as it may reasonably require well in advance of the proposed publication date. An issuer should also be mindful to inform its compliance adviser when a transaction is contemplated, rather than after the relevant agreement has been signed or the transaction completed.

Guidance on opinion letters prepared by independent financial advisers

I. Purpose

1. This letter provides guidance on the content of the opinion letters prepared by independent financial advisers (**IFAs**) and certain recommended practices for IFAs, issuers and independent board committees (**IBCs**) in performing their duties under the Listing Rules.

II. Relevant Listing Rules

2. Under the Listing Rules, an issuer is required to appoint an IFA to advise its IBC and shareholders on:

   (i) connected transactions;

   (ii) equity fund raisings that would result in a material dilution of shareholders' interests, i.e. any rights issue or open offer that would increase the number of issued shares (excluding treasury shares) or market capitalisation of the issuer by more than 50%, and refreshment of general mandate;

   (iii) other corporate actions which would affect an issuer's listing status, i.e. withdrawal of listing, fundamental change in the issuer's business within 12 months after listing, and material spin-off that require shareholders' approval.

3. **IFA**

Eligibility to act as IFA

3. Main Board Rules 13.82 to 13.84 (GEM Rules 17.94 and 17.96) require that an IFA must be appropriately licensed by the Securities and Futures Commission (**SFC**)[1] and must discharge its responsibilities with due care and skill, and perform its duties with impartiality. Under the SFC's Corporate Finance Adviser Code of Conduct, an IFA should ensure that it has adequate competence, professional expertise and resources for the proper performance of its duties.

4. Under Main Board Rules 13.83 and 13.84 (GEM Rules 17.95 and 17.96), an IFA must perform its duties with impartiality and must be independent from the issuer for whom it acts.

5. Main Board Rule 13.84 (GEM Rule 17.96) also provides a set of bright-line tests to assess the IFA's independence.

[1] Under the current regime, an IFA must be licensed by the SFC (i.e. Type 6 license and permitted to undertake work as a sponsor). A firm which holds a Type 6 license but does not have the capacity to act as a sponsor may be acceptable to act as an IFA if it has provided corporate finance advice on at least two significant corporate finance transactions. See also HKEX news release issued on 24 October 2006 and Listing Decision (LD102-2) issued in August 2010.

Content of IFA letters

6. Main Board Rules 13.39 and 14A.45 (GEM Rules 17.47 and 20.43) require an IFA to disclose in its letter:

   (i) whether the terms of the proposed transaction are fair and reasonable and in the interest of the issuer and its shareholders as a whole, and in the case of a connected transaction, whether it is on normal commercial terms and in the issuer's ordinary and usual course of business,

   (ii) its advice to the IBC on whether the independent shareholders should vote in favour of the transaction;

   (iii) the reasons for its opinion;

   (iv) key assumptions made; and

   (v) the factors taken into consideration in forming that opinion.

Standard of IFA works

7. Main Board Rule 13.80 (GEM Rule 17.92) requires an IFA to have a reasonable basis in formulating its opinion. Further, it should have no reason to believe that information it relied on is not true or omits a material fact.

8. The Listing Rule also sets out reasonable steps that an IFA are typically expected to perform. They include:

   (i) obtaining all information and documents of the issuer relevant to an assessment of the fairness and reasonableness of the transaction's terms;

   (ii) researching the relevant market and economic conditions and trends relevant to the pricing of the transaction;

   (iii) reviewing the fairness, reasonableness and completeness of any assumptions or projections relevant to the transactions;

   (iv) reviewing and assessing the alternative offers and the reasons given by management for rejecting these offers.; and

   (v) where third party expert opinion or valuation is involved,

   - interviewing the expert as to its expertise and independence;
   - reviewing the terms of engagement and assessing the appropriateness of the scope of work; and
   - assessing the reasonableness of any representations made by the issuer or the party to the transaction to the expert.

(B) IBC

9. Under Main Board Rules 13.39(6), 14A.40 and 14A.41 (GEM Rules 17.47(6), 20.38 and 20.39), an issuer is required to establish an IBC (which shall consist only of independent non-executive directors) to advise shareholders as to whether the terms of the relevant transaction or arrangement are fair and reasonable (and in the case of a connected transaction, whether it is made on normal commercial terms and in the ordinary and usual course of business of the issuer) whether such a transaction or arrangement is in the interests of the issuer and its shareholders as a whole and to advise shareholders on how to vote, taking into account the recommendations of the IFA.

(C) Issuer

10. Under Main Board Rule 13.81 (GEM Rule 17.93), an issuer must afford any IFA it appoints under the Listing Rules full access at all times to all persons, premises and documents relevant to the IFA's performance of duties. In particular, the terms of engagement with experts retained to perform services related to the transaction should contain clauses giving the IFA access to such expert, its report and information provided to or relied on by the expert.

11. Under Main Board Rules 2.13 and 14A.69 (GEM Rules 17.56 and 20.67), the information contained in an issuer's circular must be accurate and complete in all material respects and not be misleading or deceptive, and the circular must provide a clear and adequate explanation of the subject transaction and all information necessary to allow the shareholders to make an informed decision.

III. Guidance

12. An IFA advises the IBC and shareholders on material corporate actions of the issuer, and it is important that the IFA's advice is impartial and useful to assist shareholders to make informed voting decisions.

13. The Listing Rules have specific requirements governing the provision of an IFA opinion on issuer's corporate actions. Issuers, IBCs and IFAs are expected to observe the following when performing their duties under the Listing Rules:

(A) IFA's qualifications, experience and relationships

14. An IFA must ensure that it is independent from the issuer and other parties to the proposed transaction, and has sufficient expertise and resources to give an opinion on the transaction.

15. The opinion letter should include the following information that shareholders may consider relevant for assessing what weight to give to the opinion:

    (i) the qualifications and experience of the person signing off the IFA letter that are relevant to the proposed transaction; and

(ii) any relationship`s or interests with the issuer or any other parties that could reasonably be regarded as relevant to the independence of the IFA[2]. In particular, where the IFA has in the last two years acted as an IFA to the issuer's other transactions and has assessed that such relationship would not affect its independence, details of the services provided should be disclosed.

(B) Access to information

16. An IFA should determine what information it requires for giving its opinion on the proposed transaction.

17. The issuer is obliged to afford the IFA full access to all persons, premises and documents relevant to the IFA's performance of its duties. Examples include:

(i) any expert retained by the issuer to perform services for the transaction and the documents and information related to the expert's work; and

(ii) where an issuer has agreed on the consideration for an acquisition based on a valuation of the target, details of the valuation model, key assumptions and financial forecasts related to the target.

(C) Work done on information obtained

18. The IFA should take all reasonable steps to satisfy itself that there is no reason to believe that the information it relies on is untrue, or omits a material fact. While the IFA may not undertake due diligence work on the transaction, it should carefully consider the extent of work it requires to properly discharge its duties. It is expected to:

(i) critically review the information obtained. Where it involves valuation (including forecasts or projections) of the assets or businesses subject to the transaction, the IFA should assess whether the methodologies and assumptions used are reasonable, cross-check the valuation using other methodologies that it considers appropriate and comment on the results and any material differences; and

(ii) where it involves reports prepared or opinions given by an expert, take steps to assess the quality of the expert's work and its independence and qualification, including:

- interviewing the expert as to its expertise and independence, reviewing its terms of engagement and assessing the appropriateness of its scope of work, and

- making due inquiries to assess the accuracy and completeness of information relied on by the expert, and the reasonableness of any representations made by the issuer or the party to the expert.

(D) Analysis of the transaction

19. An IFA should form its opinion based on reasonable grounds and disclose them in its opinion letter. It is required to take all reasonable steps to satisfy itself that it has a reasonable basis for giving its advice and recommendation required by the Listing Rules.

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[2] An IFA is not independent if any of the circumstances set out in Main Board Rule 13.84 (GEM Rule 17.96) exist.

20. In practice, it is common for IFAs to refer to reports prepared or opinions given by experts retained by the issuers and/or use comparable analysis to assess the fairness and reasonableness of the transaction. To assist shareholders to better understand the transaction and the IFA's analysis and how it formed its opinion, the IFA should:

    (i) disclose its work done to assess the fairness and reasonableness of the valuation or opinion given by the expert (see also paragraph 18);

    (ii) to the extent possible, use more than one valuation methodology to assess the value of the assets or businesses subject to the proposed transaction, and where only one methodology is used, state the reason why this is so;

    (iii) describe the methodologies it used and the reasons for choosing them, and comment on the range of values derived from these methods;

    (iv) explain all key assumptions that are specific and on which its opinion is based. It should also consider including a sensitivity analysis if changes in any key assumptions are likely to affect the valuation significantly;

    (v) ensure that the comparables are a fair and representative sample. The bases for compiling such comparables should be clearly stated, including the parameters or criteria for selecting the comparables, the reasons for using these parameters or criteria, and any adjustments for the dissimilarities among the comparables or anomalous items; and

    (vi) set out other relevant factors for assessing the fairness and reasonableness of the transaction. Examples include: its research on market conditions and trends relevant to the transaction, material risks relating to the transaction and the target, any alternative options or offers available to the issuer and the reasons given by its management for rejecting them, the issuer's financial situation and solvency, its bargaining position and the opportunity costs.

21. The IFA should not attempt to deal with any limitations or deficiencies it faces by disclaiming or limiting its scope of assessment.

(E) Presentation of information in IFA letter

22. An IFA letter must be clear and concise, and contain only information that is relevant and necessary to enable shareholders to arrive at an informed decision. It should set out:

    (i) a clear view of the IFA on the fairness and reasonableness of the subject transaction and the reasons for its view;

    (ii) its analysis or comments on the key terms of the proposed transaction and other relevant factors (e.g. the reasons and benefits for entering into the transaction);

    (iii) the valuation methodologies and key assumptions adopted by the IFA;

    (iv) the source of information which is material to the IFA's opinion, including sufficient detail to enable the significant of the information to be assessed (or where appropriate, a cross-reference to information contained in other parts of the circular or public document); and

    (v) its work done and comments on any valuation or projection provided by the issuer or any expert's work that it relies on in forming its opinion; and

(vi) the IFA's and the expert's (if applicable) qualification and experience relevant to the transaction, and their relationship and interests in the issuer and other parties to the transaction (see paragraphs 15 and 18).

23. An IFA should prepare its opinion letter in plain language and ensure that the letter is easy to read and understand. It should also note that:

(i) the information included in its letter should relate to its analysis and opinion;

(ii) its letter should avoid repeating the information contained in other parts of the transaction circular. Where appropriate, the letter may include cross-reference to this information;

(iii) pictorial representations, charts, graphs and diagrams should be presented without distortion and, where relevant, should be to scale; and

(iv) quotations (for example, from newspapers or stockbroker circulars) should not be used unless the IFA has corroborated or substantiated them and details of the origin are stated.

(F) Role of the IBC

24. Under the Listing Rules, the IBC (comprising independent non-executive directors) is required to advise shareholders on the fairness and reasonableness of the subject transaction and how they should vote. It is in turn advised by the IFA.

25. To discharge its duties and ensure that it is properly advised, the IBC should take an active role in selecting an IFA that is independent and qualified to opine on the subject transaction:

(i) The IBC should be primarily responsible for selecting the IFA, and approving its terms of engagement and fees. They should consider all relevant factors in selecting the appropriate IFA, including:

(a) the nature, scale and complexity of the subject transaction;

(b) the qualifications and experience of the IFA. For example, the IFA's experience in advising similar transactions, its technical expertise relevant to the transaction or ability to assess other expert's work;

(c) whether the IFA can meet the independence guidelines set out in Listing Rules, and whether there are any other matters that may affect, or perceived to affect, the IFA's independence (including any previous engagement as an IFA to other transaction of the issuer) ; and

(d) whether the IFA has adequate resources to perform the work.

(ii) The IBC should oversee the procedures adopted by the management in identifying potential IFAs and avoid any practice that would undermine the IFA's independence and objectivity (e.g. opinion shopping).

26. The IBC should ensure that its members and the IFA have sufficient time to evaluate the transaction. The parties should ensure that any discussions or communications in the early stage would not undermine the IFA's independence and objectivity. For example, the IFA should not be involved in the formulation of the proposed transaction or structuring of its terms.

27. It is the IBC's responsibility to give its own views and recommendation on the subject transaction, taking into account the IFA's opinion. The IBC should exercise independent judgement on the transaction and critically review the IFA letter and use their knowledge and expertise to challenge the IFA's views and analysis.

(G) Issuer's responsibility

28. The issuer should support the IBC in performing its duties, including adopting procedures for selection of IFAs and providing all information and documents that are necessary for the IBC to assess the subject transaction.

29. The issuer should announce the appointment of the IFA in its announcement of the subject transaction, or where an IFA has not been appointed, as soon as possible after the appointment is made.

30. The issuer is required to provide the IFA with all information it reasonably requires for giving its opinion on the subject transaction. It should also response on a timely basis to the issues raised by the IFA to enable it to properly discharge its duties.

31. The issuer should keep the IFA informed of any material changes to any information previously given to or accessed by the IFA.

32. The issuer must ensure that the circular contains all information that is necessary for its shareholders to make an informed assessment of the subject transaction. They include:

    (i) details of the bases for determining the consideration, and where it is supported by a valuation of assets or businesses subject to the transaction, the valuation methods and assumptions adopted by the management;

    (ii) detailed explanations as to the reasons and benefits for entering into the transactions; and

    (iii) the management's discussion and analysis on any alternative options or offers available to the issuer and the reasons given for not accepting them.

Whether a firm was qualified to act as an independent financial adviser

Parties

- **Company A** – a Main Board issuer
- **Company B** – a newly formed company holding a Type 6 licence under the Securities and Futures Ordinance (**SFO**)
- **Mr X** and **Mr Y** – Company B's responsible officers

Facts

1. Company A proposed to appoint Company B as independent financial adviser regarding its connected transactions.

2. Company B had a SFO Type 6 licence (advising on corporate finance) with the condition that it could not act as sponsor in listing applications.

3. Its two responsible officers, Mr X and Mr Y, each held a Type 6 licence without the condition and had more than 10 years of experience in corporate finance. In particular, each had provided financial advice in many transactions under the Rules.

4. Company B asked whether it could accept Company A's appointment.

Relevant Listing Rules

5. Rule 13.39(6)(b) states that in relation to connected transactions,

   the issuer shall appoint an independent financial adviser acceptable to the Exchange to make recommendations to the independent board committee and the shareholders as to whether the terms of the relevant transaction or arrangement are fair and reasonable and whether such a transaction or arrangement is in the interests if the issuer and its shareholders as a whole and to advise shareholders on how to vote.

6. Rule 13.82 states that:

   an independent financial adviser must be appropriately licensed by the Commission and must discharge its responsibilities with due care and skill.

7. The Exchange's press release of 24 October 2006 states that a firm is acceptable as independent financial adviser if it:

   - is appropriately licensed or registered to undertake sponsor work (i.e. it is licensed or registered under the SFO for Type 6 regulated activity and permitted under its licence or certificate of registration to undertake work as a sponsor); or

   - meets the current Exchange practice as to what is acceptable i.e. it has completed two significant corporate finance transactions.

Analysis

8. The role of an independent financial adviser is to advise independent shareholders on corporate finance transactions. The Exchange's press release cited above sets out non-exhaustive factors it would consider when assessing a company's suitability to act as independent financial adviser.

9. Company B was not permitted to take up sponsor work under its Type 6 licence. However, its responsible officers, Mr X and Mr Y, were holders of a Type 6 licence and had significant relevant experience. The Exchange was prepared to consider the qualifications of the responsible officers in assessing if Company B was suitable to act as independent financial adviser. For this case, the Exchange was satisfied that they had the technical competence and experience necessary to advise shareholders on corporate finance transactions.

Conclusion

10. The Exchange accepted that with Mr X and Mr Y as its responsible officers, Company B was qualified to act as independent financial advisor.

Whether an individual was qualified to prepare valuation reports for Mainland properties

Parties

- **Company A** – a Main Board issuer, also listed on a Mainland stock exchange
- **Appraiser** – a Mainland real estate appraising company
- **Mr X** and **Mr Y** – two real estate appraisers employed by the Appraiser

Facts

1. Company A announced a disposal of its property, a commercial building, in Beijing (**Property**) to its parent company. This was a connected transaction which required independent shareholder approval. The circular would include a valuation report on the Property issued by the Appraiser and prepared by Mr X and Mr Y.

2. Mr X and Mr Y were the Appraiser's employees but were not members of the Hong Kong Institute of Surveyors (**HKIS**) or the Royal Institution of Chartered Surveyors.

3. Company A submitted that Mr X and Mr Y were qualified to prepare the report under Rule 5.08(2)(b) and paragraph 4.1 of Practice Note 12 because:

   (1) The Appraiser was a member of China Institute of Real Estate Appraisers and Agents (**CIREA**) and subject to its professional discipline.

   (2) CIREA was a national self-disciplined professional body of real estate appraisers and real estate brokers in the Mainland. Its responsibilities include promoting academic research and education, preparing and reviewing professional standards and ethics, holding national examinations for professional qualification of appraisers and brokers, and organizing continuing professional development activities for its members. CIREA may take disciplinary actions against members who breach its rules or practicing standards including a warning, public censure, or suspension or cancellation of membership. CIREA's practicing members are real estate appraisers registered under the Mainland regulations which require the appraisers to have relevant qualifications and experience and comply with certain continuing professional development standards.

   (3) CIREA and HKIS had signed a reciprocity agreement in relation to the recognition of qualifications of Mainland real estate appraisers and Hong Kong surveyors. Under the agreement, each institute's individual members who meet certain eligibility criteria and are nominated by the institute can apply for the other institute's membership through an examination organized by the other institute. Company A considered that CIREA was a professional body of similar standing to HKIS.

(4) Mr X and Mr Y were not members of CIREA. The Appraiser, as a CIREA member, required its employees to comply with the professional discipline of CIREA when preparing a property valuation report.

(5) Mr X and Mr Y were registered with the Ministry of Construction (**MOC**) as certified real estate appraisers and hence qualified to provide property valuation reports in the Mainland. They were required under the MOC rules and regulations to comply with the professional discipline and ethics regulations of the real estate appraisal industry in the Mainland (including those issued by CIREA), although membership of CIREA was not required for a certified real estate appraiser to provide property valuation reports.

(6) Under the rules and regulations mentioned in (4) and (5) above, Mr X and Mr Y had to comply with the Code for Real Estate Appraisal issued by MOC. The Code was the main professional discipline of CIREA. It was also the highest national standard and comparable with the HKIS property valuation standards referred to in Rule 5.05.

(7) Both Mr X and Mr Y had been working in Beijing as certified real estate appraisers and valuing commercial buildings for more than 10 years. They also attended continuous training on the CIREA standards as required under the relevant regulations.

Relevant Listing Rules

4. Rule 5.05 states that:

All valuation reports must contain all material details of the basis of valuation which must follow the "Hong Kong Guidance Notes on the Valuation of Property Assets" published by The Royal Institution of Chartered Surveyors (Hong Kong Branch) and The Hong Kong Institute of Surveyors.

5. Rule 5.08 states that

Unless dispensation is obtained from the Exchange, all valuations of properties must be prepared by an independent qualified valuer and for this purpose:-

(1) …

(2) a valuer is a qualified valuer only if:-

(a) …

(b) for the purposes of valuation of properties situated outside Hong Kong, the valuer has the appropriate professional qualifications and experience of valuing properties in the same location and category to carry out the valuation.

6. Para 4.1 of PN12 states that:

for the purpose of valuing properties in developing property markets, a valuer would normally be regarded as having the appropriate professional qualifications and experience for valuing properties in developing property markets if he is subject to the discipline of the RICS or the HKIS (i.e. Hong Kong Institute of Surveyor) or professional body of similar standing to the RICS or HKIS and has a minimum of 2 years experience in valuing properties in the relevant location or has relevant experience to the satisfaction of the Exchange.

Analysis

7. Under paragraph 4.1 of PN12, the Exchange would regard a valuer as having appropriate qualifications if he is subject to the discipline of the RICS or the HKIS or a professional body of similar standing to either of them. The Exchange was satisfied that Mr X and Mr Y had the required qualifications because:

    a. It considered that CIREA was a professional body of similar standing to the HKIS.

    b. The Appraiser was a CIREA member.

    c. Mr X and Mr Y were certified real estate appraisers in the Mainland. Although they were not CIREA members, they were required under the Appraiser's internal regulations and MOC rules and regulations to comply with the professional discipline of CIREA.

8. Given their property valuation experience, the Exchange also considered that they had the experience required under paragraph 4.1 of PN12.

Conclusion

9. Mr X and Mr Y were qualified to prepare the valuation report for Company A's circular.

3

Accounting and auditing matters

3.1 Accountants' report

Listing decision – Whether the Exchange would waive the accountants' report requirement for an acquisition of a business from an overseas listed company	LD74-1	3.1 – 1
Listing decision – Whether the Exchange would waive the accountants' report requirement for a proposed acquisition of equity interest in an overseas listed target company that would become a subsidiary of the listed issuer	LD28-2012	3.1 – 6
Listing decision – Whether the Exchange would waive the accountants' report requirement for a proposed acquisition of equity interest in an overseas listed target company that would be accounted for as an associate in the listed issuer's financial statements	LD74-2	3.1 – 9
Listing decision – (1) Whether the Exchange would waive the requirement for the transaction circular to include an accountants' report on the target company's businesses to be acquired by the listed issuer under a merger proposal; and (2) whether the disclosure requirements relating to acquisitions of infrastructure projects would apply	LD74-3	3.1 – 12

3.2 Financial disclosure

Guidance letter – Guidance on the presentation of non-GAAP measures	GL103-19	3.2 – 1
Listing decision – Whether the Exchange would waive the requirement for the transaction circular to include a profit and loss statement on the property to be acquired by the listed issuer	LD66-2013	3.2 – 4
Frequently asked questions - Financial disclosure	FAQ3.2 – No.1-7	3.2 – 6

3.3 Recognition of overseas audit firms

Frequently asked questions - Recognition of overseas audit firms under Accounting and Financial Reporting Council Ordinance	FAQ3.3 – No.1-6	3.3 – 1

Whether the Exchange would waive the accountants' report requirement for an acquisition of a business from an overseas listed company

Parties

- **Company A** – a Main Board listed company
- **Vendor** – a company listed on the New York Stock Exchange

Facts

1. Company A agreed to acquire from the Vendor certain assets and assume certain liabilities in connection with the Vendor's business in manufacturing and selling certain electronic products (**Target Business**) (**Acquisition**). This constituted a very substantial acquisition for Company A.

2. Chapter 4 of the Listing Rules required the financial information of the Target Business included in the accountants' report to be drawn up in conformity with Hong Kong Financial Reporting Standards (**HKFRS**), the standards adopted by Company A, and the accountants' report to be prepared in accordance with the Auditing Guidelines – Prospectus and the reporting accountant (Statement 3.340) issued by the Hong Kong Institute of Certified Public Accountants (**HKAG 3.340**)[1].

3. Company A proposed that instead of an accountants' report on the Target Business that strictly complied with Chapter 4, its circular for the Acquisition (**Circular**) would include:

    - the audited combined financial statements of the Target Business (**US Financials**) prepared by the Vendor in accordance with US GAAP and audited by the Vendor's auditors in accordance with the standards of Public Company Accounting Oversight Board (United States) (**PCAOB Standards**); and

    - an explanation of the differences and a line-by-line reconciliation (**Reconciliation**) between the accounting policies of the Target Business under US GAAP and Company A's accounting policies under HKFRS. Company A's auditors would review and report on the adjustments in the Reconciliation in arriving at the financial information of the Target Business under HKFRS under HKAG 3.340[1];

[1] HKAG 3.340 was superseded by Hong Kong Standard on Investment Circular Reporting Engagements 200 "Accountants' Reports on Historical Financial Information in Investment Circulars" (HKSIR 200), which became effective for engagements where the investment circular is dated on or after 1 July 2017.

Further, as the Vendor would submit to the US Securities and Exchange Commission a Form 8K with the US Financials, they would not be presented in the format of an accountants' report in Hong Kong. Nevertheless, the US Financials in the Circular would include additional disclosure so that the Circular would contain the same level of information as an accountants' report under the Listing Rules.

4. Company A applied for a waiver from the Chapter 4 requirements for the accountants' report on the Target Business for the following reasons:

   - The Vendor was active in over 160 countries. The Target Business had been centrally operated by the Vendor together with other divisions and had never been operated individually under a separate entity or otherwise on a standalone basis. The Target Business was only part of the Vendor's business operations and was not required to be reported on as a distinct business under any regulation or legislation. No audited financial statements for the Target Business had been previously prepared or reported on a standalone basis.

   - The Vendor's accounting systems, control procedures and data maintenance functions were managed on a centralised basis. The accounting records of the Vendor and therefore the Target Business were maintained under US GAAP, and the financial reporting processes were designed to facilitate independent audit under the PCAOB Standards.

   - In view of the complexity and extensive coverage of the Vendor's accounting systems worldwide, there would be practical difficulties in changing the Vendor's accounting standards to conform with HKFRS in order to prepare the financial statements of the Target Business under HKFRS.

   - Company A also submitted that for a professional accounting firm to opine on the financial statements of the Target Business, it would need to extend its audit scope to cover all the accounting systems and control procedures of the Vendor which supported the operations of not just the Target Business but other different divisions within the Vendor group. Company A had been informed that the Vendor would not allow any accounting firms other than its own auditors to access its systems and accounting records which covered the other parts of its group. Although Company A's auditors were an affiliated firm of the Vendor's auditors, they were two separate legal entities and were managed independently. As the Vendor did not consent to Company A's auditors reviewing the Vendor's books and records other than those of the Target Business, it was impossible for them to report on the financial information of the Target Business by themselves or jointly with the Vendor's auditors under HKAG 3.3401 as required by Rule 4.08(3). Further, the Vendor advised that its auditors had limitations in preparing an accountants' report as prescribed by HKAG 3.3401 as the US Financials were prepared under US GAAP.

   - While the Vendor's auditors were not registered under the Professional Accountants Ordinance as required by Rule 4.03, it was a firm with international name and reputation and registered with the PCAOB. In addition, Company A was of the opinion that PCAOB Standards and the Hong Kong Statements of Auditing Standards were substantially consistent with each other.

- The audit opinion on the US Financials would be a "fairly presented" opinion under US GAAP and this would not strictly comply with Rule 4.08(2) which required a "true and fair" opinion. Company A considered that both opinions provided the same degree of assurance on audited financial statements.

Relevant Listing Rules

5. Rule 14.69(6)(a)(i) provides that a circular issued in relation to a very substantial acquisition or a listing document issued in relation to reverse takeover must contain:-

...

(6)(a) on an acquisition of any business, company or companies:

(i) an accountants' report on the business, company or companies being acquired in accordance with Chapter 4 of the Exchange Listing Rules... The financial information on the business, company or companies being acquired as contained in the accountants' report must be prepared using accounting policies which should be materially consistent with those of the listed issuer.

6. Rule 4.03[2] provides that:-

all accountants' reports must be prepared by certified public accountants who are qualified under the Professional Accountants Ordinance for appointment as auditors of a company and who are independent both of the issuer and of any other company concerned to the same extent as that required of an auditor under the Companies Ordinance and in accordance with the requirements on independence issued by the Hong Kong Institute of Certified Public Accountants, provided that, in the case of a circular issued by a listed issuer in connection with the acquisition of an overseas company, the Exchange may be prepared to permit the accountants' report to be prepared by a firm of accountants which is not so qualified but which is acceptable to the Exchange. Such a firm must normally have an international name and reputation and be a member of a recognised body of accountants.

7. Rule 4.08(2) provides that in all cases:-

the reporting accountants must express an opinion as to whether or not the relevant information gives, for the purposes of the accountants' report, a true and fair view of the results and cash flows for the period reported on and of the statement of financial position as at the end of each of the period reported on.

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2 Rule 4.03(1) was amended to reflect the amendment to the Accounting and Financial Reporting Council Ordinance (Cap. 588) (**AFRCO**) that established the PIE Engagement (as defined in Rule 1.01) regime which came into effect on 1 October 2019. The preparation of an accountants' report in a very substantial acquisition circular is the PIE Engagement. In the case of a very substantial acquisition circular issued by a listed issuer incorporated outside Hong Kong relating to the acquisition of an overseas company, the Exchange may be prepared to accept the appointment of an overseas audit firm that is not qualified under the Professional Accountants Ordinance but is a Recognised PIE Auditor (as defined in Rule 1.01) of that issuer under the AFRCO.

In relation to an application for the recognition of an overseas audit firm under the AFRCO, an issuer must obtain a statement of no objection from the Exchange. Generally, other than having an international name and reputation and being a member of a recognized body of accountants, an overseas audit firm must also be subject to independent oversight by a regulatory body of a jurisdiction that is a full signatory to the IOSCO MMOU (as defined in Rule 1.01). It would be acceptable if the relevant audit oversight body is not a signatory to the IOSCO MMOU but the securities regulator in the same jurisdiction must be a full signatory to the IOSCO MMOU. See notes to Rule 4.03(1). The Rule amendment would not change the analysis and conclusion in this case.

8. Rule 4.08(3) provides that in all cases:-

   the accountants' report must state that it has been prepared in accordance with the Auditing Guideline – Prospectuses and the reporting accountant (Statement 3.3.40) [1] issued by the Hong Kong Institute of Certified Public Accountants.

9. Rule 4.11 provides that:-

   the financial history of results and the statement of financial position included in the accountants' report must normally be drawn up in conformity with:-

   (a) Hong Kong Financial Reporting Standards; or

   (b) International Financial Reporting Standards.

Analysis

10. Under the Listing Rules, an issuer must ensure that the information in its circular for a notifiable transaction is accurate and complete in all material respects and not misleading or deceptive. The circular must contain all information necessary to allow the issuer's shareholders to make a properly informed decision on how to vote on the transaction.

11. In this case, the facts submitted by Company A demonstrated that it was extremely difficult for Company A to prepare an accountants' report on the Target Business that strictly complied with Chapter 4. The Exchange was satisfied that the circumstances of this case were exceptional and compliance with the Listing Rules by Company A in unmodified form would be unduly burdensome and impractical.

12. The Exchange also took into account:

    a. The US Financials would contain the same level of information as required in an accountants' report under the Listing Rules. The waiver application mainly involved modifications to the Rule requirements concerning the accounting and auditing standards for preparing financial information of the Target Business for incorporation in the Circular.

    b. While the US Financials were prepared under US GAAP, the Reconciliation would provide financial information under HKFRS to facilitate shareholders' assessment of the performance and financial position of the Target Business. Company A's auditors took additional procedures according to HKAG 3.340[1] in respect of the Reconciliation which gave assurance on the unaudited financial information of the Target Business under HKFRS.

    c. The US Financials were audited by the Vendor's auditors in accordance with PCAOB Standards.

    d. While Rule 4.03 requires the reporting accountants to be qualified under the Professional Accountants Ordinance, it also provides that for an acquisition of an overseas company, the Exchange may permit an accountants' report to be prepared by a firm of accountants which is not so qualified but which must normally have an international name and reputation and must be a member of a recognised body of accountants. The circumstances here were similar to an acquisition of an overseas company and the Vendor's auditors met the criteria in Rule 4.03.

13. The Exchange was satisfied that there would be sufficient and appropriate alternative disclosure in the Circular to enable Company A's shareholders to make a properly informed assessment of the Target Business. The granting of the waiver requested by Company A would be unlikely to result in undue risks to its shareholders.

Conclusion

14. The Exchange granted the waiver[3] on the basis that the Circular would contain the alternative disclosure proposed by Company A[4] in the waiver application.

[3] From 1 October 2019 onwards, this waiver is also subject to the overseas audit firm to be recognised by the Accounting and Financial Reporting Council (**AFRC**).

[4] Under the AFRCO, only an issuer incorporated outside Hong Kong is permitted to appoint an overseas audit firm and submit a recognition application to the AFRC for a PIE Engagement.

Whether the Exchange would waive the accountants' report requirement for a proposed acquisition of equity interest in an overseas listed target company that would become a subsidiary of the listed issuer

Parties

- **Company A** – a Main Board issuer
- **Target** – a company listed on the Toronto Stock Exchange

Facts

1. Company A proposed to make a cash offer to acquire all the Target's shares (**Acquisition**). Upon completion, the Target would become a subsidiary of Company A.

2. The Acquisition would be a major transaction. The Listing Rules required an accountants' report on the Target be included in Company A's circular for the Acquisition. Company A requested a waiver from the requirement for the following reasons:

    - The Target was listed on the Toronto Stock Exchange. It had published its financial information, including audited accounts, on a regular basis under the overseas regulatory requirements.
    - It would be unduly burdensome for Company A to engage professional accountants to prepare an accountants' report on the Target as required by the Rules in light of the substantial time and costs required.
    - The circular would contain alternative disclosure for the shareholders to assess the Target's financial performance:
        - The Target's published audited financial statements for the last three financial years and its latest published unaudited 9-months financial information prepared under the Canadian generally accepted accounting principles (**Canadian GAAP**). The Target's auditors had issued a clean opinion on the audited financial statements. They had also reviewed the unaudited 9-month financial information under the Canadian standards. They were a firm of accountants with international name and reputation and registered with a recognized body of accountants.

- A line-by-line reconciliation of the Target's financial information for the differences between its accounting policies under the Canadian GAAP and Company A's accounting policies under HKFRS, with an explanation of the differences. Company A's auditors would review the reconciliation under Hong Kong Standard of Assurance Engagements 3000.

- Additional information which was required for an accountants' report under the Rules but not disclosed in the Target's published accounts.

Relevant Listing Rules

3. Rule 14.67 requires that:-

...a circular issued in relation to an acquisition constituting a major transaction must contain:-

...

(6)(a)(i) an accountants' report on the business, company or companies being acquired in accordance with Chapter 4 of the Exchange Listing Rules provided that, where any company in question has not or will not become a subsidiary of the listed issuer, the Exchange may be prepared to relax this requirement. The accounts on which the report is based must relate to a financial period ended 6 months or less before the circular is issued. The financial information on the business, company or companies being acquired as contained in the accountants' report must be prepared using accounting policies which should be materially consistent with those of the listed issuer; ...

4. Rule 4.03[1] provides that:-

all accountants' reports must normally be prepared by certified public accountants who are qualified under the Professional Accountants Ordinance for appointment as auditors of a company and who are independent both of the issuer and of any other company concerned to the same extent as that required of an auditor under the Companies Ordinance and in accordance with the requirements on independence issued by the Hong Kong Institute of Certified Public Accountants, provided that, in the case of a circular issued by a listed issuer in connection with the acquisition of an overseas company, the Exchange may be prepared to permit the accountants' report to be prepared by a firm of practising accountants which is not so qualified but which is acceptable to the Exchange. Such a firm must normally have an international name and reputation and be a member of a recognised body of accountants.

[1] On 1 January 2022, Rule 4.03(2) was amended to state that, in the case of a major transaction circular issued by a listed issuer in connection with the acquisition of an overseas company, the overseas audit firm must also be subject to independent oversight by a regulatory body of a jurisdiction that is a full signatory to the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (**IOSCO MMOU**). It would be acceptable if the relevant audit oversight body is not a signatory to the IOSCO MMOU but the securities regulator in the same jurisdiction must be a full signatory to the IOSCO MMOU. The Rule amendment would not change the analysis and conclusion in this case.

5. Rule 4.11 requires that:-

the financial history of results and the balance sheet included in the accountants' report must normally be drawn up in conformity with:-

(a) Hong Kong Financial Reporting Standards (HKFRS); or

(b) International Financial Reporting Standards (IFRS); or

...

Analysis

6. Under the Listing Rules, an issuer must ensure that the information in its circular for a notifiable transaction is accurate and complete in all material respects and not misleading or deceptive. The circular must contain all information necessary to allow the issuer's shareholders to make a properly informed decision on how to vote on the transaction.

7. In this case, the Exchange noted that:

- The Target had been publishing financial information to the market on a regular basis to enable investors to assess its activities and financial position. It was listed on an overseas stock exchange and its financial disclosures were subject to supervision by regulatory authorities.

- The Target's accounts to be disclosed in the circular were audited/reviewed by its auditors. While the auditors were not registered under the Hong Kong Professional Accountants Ordinance, they were a firm of accountants with international name and reputation and registered with a recognized body of accountants[2].

- The reconciliation would provide financial information under HKFRS to facilitate shareholders' assessment of the Target's performance and financial position. Company A would engage its auditors to review the reconciliation.

- Company A would make additional disclosures in the circular to bridge the gap between the Target's accounts and an accountants' report required by the Rules.

8. The Exchange considered that Company A had taken reasonable steps to provide sufficient information to its shareholders to assess the Target's business. It would be unduly burdensome for Company A to produce an accountants' report on the Target. Granting the waiver would be unlikely to result in undue risks to its shareholders.

Conclusion

9. The Exchange agreed to waive the accountants' report requirement.

[2] The securities regulator in Canada was a full signatory to the IOSCO MMOU.

Whether the Exchange would waive the accountants' report requirement for a proposed acquisition of equity interest in an overseas listed target company that would be accounted for as an associate in the listed issuer's financial statements

Parties

- **Company A** – a Main Board listed company
- **Target** – a company listed on the Australian Stock Exchange
- **Vendor** – a shareholder of the Target

Facts

1. Company A agreed to purchase certain interests in the Target (**Acquisition**) from the Vendor. The Target was listed on the Australian Stock Exchange (**ASX**). The Target's business was in line with Company A's principal activities.

2. Upon completion of the Acquisition, Company A's interest in the Target would increase from approximately 12% to 20%. The Acquisition constituted a major transaction for Company A.

3. Before the Acquisition, Company A accounted for its interest in the Target as "available for sale equity investment". Upon completion of the Acquisition, Company A's 20% interest in the Target would be treated as an investment in an associate and accounted for using the equity method of accounting.

4. Company A proposed to include the following information in its circular for the Acquisition instead of an accountants' report on the Target:

    - the Target's published audited financial statements for the preceding three years together with the latest published unaudited quarterly and interim financial information of the Target prepared under Australian accounting standards;
    - a letter from Company A's reporting accountants explaining that there were no differences between Australian accounting standards and HKFRS that had material effect on the Target's financial information in the circular; and
    - the reason for not preparing an accountants' report on the Target.

5. Company A applied for a waiver from the requirement to produce an accountants' report on the Target for the following reasons:

(a) The Acquisition was a transaction between Company A and the Vendor. The Target was not obliged to assist Company A to prepare an accountants' report on it for the Acquisition. Neither Company A nor the Vendor had access to the Target's books and records to prepare an accountants' report on it in accordance with the Listing Rules.

(b) The Target would not become a subsidiary of Company A as a result of the Acquisition.

(c) Company A had requested the Target to assist in the preparation of the accountants' report but it had declined.

(d) The Target had published its financial information on a regular basis under the listing rules in Australia. It was not prepared to disclose any additional financial information.

(e) While the Target's financial information was prepared under Australian accounting standards but not HKFRS, the standards adopted by Company A, there should be no material differences in the reported amounts under the two accounting standards. The Target's accounting policies were materially consistent with Company A's.

Relevant Listing Rules

6. Rule 14.67 requires that:

… a circular issued in relation to an acquisition constituting a major transaction must contain:-

…

(6)(a)(i) an accountants' report on the business, company or companies being acquired in accordance with Chapter 4 of the Exchange Listing Rules provided that, where any company in question has not or will not become a subsidiary of the listed issuer, the Exchange may be prepared to relax this requirement. The accounts on which the report is based must relate to a financial period ended 6 months or less before the circular is issued. The financial information on the business, company or companies being acquired as contained in the accountants' report must be prepared using accounting policies which should be materially consistent with those of the listed issuer; ...

7. Rule 4.11 requires that:

The financial history of results and the balance sheet included in the accountants' report must normally be drawn up in conformity with:-

(a) Hong Kong Financial Reporting Standards; or

(b) International Financial Reporting Standards…

Analysis

8. Under the Listing Rules, an issuer must ensure that the information in its circular for a notifiable transaction is accurate and complete in all material respects and not misleading or deceptive. The circular must contain all information necessary to allow the issuer's shareholders to make a properly informed decision on how to vote on the transaction.

9. While Rule 14.67(6)(a)(i) provides that the Exchange may relax the requirement for an accountants' report where the company to be acquired has not or will not become a subsidiary of the issuer, a request for relaxation will need to be assessed case by case having regard to the facts and circumstances.

10. Here, the Target had not been and would not, as a result of the Acquisition, become Company A's subsidiary. Therefore, Rule 14.67(6)(a)(i) applied. In determining whether to relax the accountants' report requirement, the Exchange took into account:

    - Company A did not have access to non-public information of the Target required to prepare an accountants' report on it. Strict compliance with the accountants' report requirement by Company A would be impractical;

    - the Target had been publishing financial information to the market on a regular basis to enable investors to assess its activities and financial position. It was listed on an overseas stock exchange and its financial disclosures were subject to supervision by regulatory authorities; and

    - Company A submitted that there were no differences between Australian accounting standards and HKFRS, the standards adopted by Company A, that had material effect on the Target's financial information in the circular. This was supported by Company A's reporting accountants. Company A's shareholders should be able to assess the performance and financial position of the Target based on the alternative disclosure included in the circular.

11. The Exchange considered that Company A had taken reasonable steps to ensure sufficient information was provided to its shareholders to make a properly informed assessment of the Target. The granting of the waiver as requested by Company A would be unlikely to result in undue risks to its shareholders.

Conclusion

12. The Exchange granted the waiver to Company A on condition that the circular would contain the alternative disclosure proposed by Company A in its waiver application.

(1) Whether the Exchange would waive the requirement for the transaction circular to include an accountants' report on the target company's businesses to be acquired by the listed issuer under a merger proposal; and (2) whether the disclosure requirements relating to acquisitions of infrastructure projects would apply

Parties

- **Company A** – a Main Board listed company
- **Target Company** – a statutory corporation whose operations were to be merged with Company A under the Merger

Facts

1. The principal activities of both Company A and the Target Company included operating railway systems.

2. Company A and the Target Company entered into agreements regarding the proposed merger of their operations and other related transactions (**Merger**). Under the Merger, Company A would acquire substantially all business operations of the Target Company whose residual operations would predominantly be administrative only.

3. The Merger would constitute a very substantial acquisition for Company A under Chapter 14. As the Target Company was a connected person of Company A, the Merger would also constitute a connected transaction under Chapter 14A. The Merger would be subject to approval by Company A's independent shareholders.

Issue 1

4. Under Rule 14.69(4)(a)(i), Company A had to include an accountants' report in accordance with Chapter 4 on the business being acquired under the Merger in its circular for the Merger (**Circular**).

5. Company A applied for a waiver from compliance with Rule 14.69(4)(a)(i) for the following reasons:

- The Merger effectively involved an acquisition (whether by way of transfer of legal or beneficial title, service concession or licence) of those assets, or rights, and liabilities which were then required by the Target Company to operate and maintain its business.

- The tangible assets that formed part of the Target Company's then railway network were not acquired by Company A but were subject to a service concession arrangement under which Company A would have the right to access, use and operate them for a specified term. Legal title to the assets would remain with the Target Company and they would continue to be recognised in the Target Company's balance sheet as fixed assets. However, the operating results generated from the assets over the concession period would effectively be acquired by Company A. Company A would recognise a service concession asset in respect of payments to acquire the rights to operate the Target Company's assets under the service concession arrangement.

- To prepare an accountants' report on the business being acquired under the proposed Merger, it would be necessary to "carve-out" the assets, liabilities, income and expenses that were not subject to the Merger from the accounts of the Target Company and its subsidiaries (**Target Group**). This would require significant judgements and assumptions and was not practical given the nature, complexity and detail of the arrangements under the Merger. Further, this financial information might not provide a meaningful picture on the assets employed by the Target Group for its business operations during the reporting period as the railway assets subject to the service concession arrangement would not be recognised in the balance sheets.

- Company A was of the view that the audited financial statements of the Target Group would present meaningful and comprehensive information to shareholders of Company A in understanding the business operations subject to the Merger by presenting the revenue generated and expenses incurred, together with the assets employed and liabilities incurred during the period reported on.

6. Company A proposed that the Circular would contain an accountants' report on the Target Group which would include the following information:

   (i) the Target Group's financial statements for the latest three financial years and the stub period (**Relevant Period**);

   (ii) additional information including a reconciliation table and narrative descriptions by way of an explanatory note to explain the impact of the Merger on the Target Group's financial results and cashflows for the Relevant Period and its financial position as at the end of the period, the adjustments for items which would not be acquired by Company A, and how the figures would be translated to the pro-forma financial information of the enlarged group in the Circular (**Additional Information**); and

   (iii) the opinion of Company A's reporting accountants that the Target Group's financial information (including the Additional Information) gave a true and fair view of the results and cashflows for each of the financial years and period reported on and the state of affairs of the Target Group as at the end of each year and the period.

Issue 2

7. Company A noted that there were specific disclosure requirements in Rule 14.71 and 14A.70(9) for a very substantial acquisition and connected transaction which involved acquiring an interest in an infrastructure project or an infrastructure or project company. While "infrastructure project" was not defined in Chapters 14 and 14A, reference was made to Rule 8.05B(2) which provided that "infrastructure projects" are projects which create the basic physical structures or foundations for the delivery of essential public goods and services necessary for the economic development of a territory or country. According to Rule 8.05B(2), examples of infrastructure projects included the construction of railways and mass transit systems.

8. The Merger would involve Company A acquiring the rights to access, use and operate the assets which formed part of the then railway network of the Target Company under a service concession arrangement. Company A enquired whether Rules 14.71 and 14A.70(9) would apply to the Merger.

Relevant Listing Rules

9. Rule 14.69(4)(a)(i) provides that a circular issued in relation to a very substantial acquisition or a listing document issued in relation to a reverse takeover must contain:-

...

(4)(a) on an acquisition of any business, company or companies:

(i) an accountants' report on the business, company or companies being acquired in accordance with Chapter 4 of the Exchange Listing Rules... The financial information on the business, company or companies being acquired as contained in the accountants' report must be prepared using accounting policies which should be materially consistent with those of the listed issuer.

10. Rule 14.71 provides that:

Where a major transaction, very substantial acquisition, … involves acquiring or disposing of an interest in an infrastructure project or an infrastructure or project company, the listed issuer shall incorporate in the circular or listing document a business valuation report on the business or company being acquired or disposed of and/or traffic study report in respect of the infrastructure project or infrastructure or project company. Such report(s) must clearly set out:

(1) all fundamental underlying assumptions including discount rate or growth rate or growth rate used; and

(2) a sensitivity analysis based on the various discount rates and growth rates.

Where any business variation is based on a profit forecast, the accounting policies and calculations for the underlying forecasts must be examined and reported on by the auditors or reporting accountants. Any financial adviser mentioned in the circular or listing document must also report on the underlying forecasts.

11. Rule 14A.70(9) provides that a circular in relation to a connected transaction that involves an acquisition or disposal of a company or business engaging in an infrastructure project must contain, among others, a business valuation report on that company or business and/or traffic study report on the project. The report(s) must set clearly out:

    (a) all significant underlying assumptions including discount rate or growth rate used; and

    (b) a sensitivity analysis based on different discount rates and growth rates;

    If the business valuation is based on a profit forecast, the accounting policies and calculations for the underlying forecasts must be examined and reported on by the auditors or reporting accountants. Any financial adviser mentioned in the circular must also report on the underlying forecasts; …

12. Rule 8.05B provides that:

    The Exchange may accept a shorter trading record period and/or may wary or waive the above profit or other financial standards requirement in rule 8.05 in the following cases:-

    …

    (2) newly formed 'project' companies, for example a company formed to construct a major infrastructure project. The Exchange considers that "infrastructure projects" are projects which create the basic physical structures or foundations for the delivery of essential public goods and services that are necessary for the economic development of a territory or country. Examples of infrastructure projects include the construction of roads, bridges, tunnels, railways, mass transit systems, water and sewage systems, power plants, telecommunication systems, seaports and airports. A new applicant of such 'project' companies must be able to demonstrate that:

    …

    (d) where it is involved in more than one project, the majority of its project(s) are in the pre-construction or construction stage.

    …

Analysis

13. Under the Listing Rules, an issuer must ensure that the information contained in its circular for a notifiable and/or connected transaction is accurate and complete in all material respects and not misleading or deceptive. The circular must contain all information necessary to allow the issuer's shareholders to make a properly informed decision on how to vote on the transaction.

Issue 1

14. Rule 14.69(4)(a)(i) requires the circular for a very substantial acquisition to contain an accountants' report on the business or company to be acquired to enable shareholders to assess the performance and financial position of the business or company. Chapter 4 sets out the standards of preparation and assurance for the disclosure of information in the accountants' report.

15. Issuers are expected to exercise all reasonable care to ensure full compliance with the Listing Rules. The Exchange will not grant waivers, except where the Rules already contemplate the granting of waivers under certain circumstances or where it is satisfied that there are exceptional and justifiable circumstances to grant a waiver. The "Guide on Applications for Waivers and Modifications of the Listing Rules" available on the HKEX website sets out a non-exhaustive list of factors that the Exchange will generally consider when assessing a waiver application.

16. In deciding on a waiver, the Exchange will take into account the circumstances and reasons outlined in the application and all other information supplied by the issuer.

17. In this case, the Merger involved complex and detailed arrangements, and it would be impractical for Company A to prepare an accountants' report on the business being acquired under the proposed Merger. An accountants' report, even if prepared, would be "pro-forma" financial information and would not comply with Rule 4.29.

18. The Exchange also took into account that:

    a. The Merger would effectively involve an acquisition of substantially all the business operations of the Target Company. It would be acceptable for Company A to provide the Target Group's historical financial statements to facilitate shareholders' understanding of the Target Group's business operations during the Relevant Period. The Additional Information would explain the impact of the Merger on the results and financial position of the Target Group in the Relevant Period and the items that would be accounted for differently in Company A's accounts after the Merger.

    b. The accountants' report, including the Target Group's financial statements during the Relevant Period and the Additional Information, would be reported on by Company A's reporting accountants.

    c. This alternative disclosure was submitted by Company A after considering alternative approaches for preparing an accountants' report for the Circular. The Exchange accepted that Company A had taken reasonable steps to ensure sufficient information was provided to its shareholders to make a properly informed assessment of the business being acquired.

19. The Exchange was satisfied that the circumstances of this case were exceptional and the granting of the waiver would be unlikely to result in undue risks to the shareholders whose interests the Listing Rules were intended to protect.

Issue 2

20. Rule 14.71 or 14A.70(9) applies to the circular for a notifiable transaction (being major or above) or a non-exempt connected transaction which involves acquiring or disposing of an interest in an infrastructure project or an infrastructure or project company. The Rules require the circular to contain a business valuation report on the business or company being acquired or disposed of and/or traffic study report in respect of the infrastructure project or infrastructure or project company.

21. When applying Rules 14.71 and 14A.70(9), the Exchange will take a purposive approach to ensure that the intent of the Rules is adhered to. The purpose of the additional disclosure requirements under the Rules is to ensure shareholders have the necessary information to make an informed judgement of the acquisition or disposal of an infrastructure project. This is particularly the case where the infrastructure project is under construction or in the pre-construction stage or is recently completed. The lack of a reasonable trading record for the project calls for the need for a business valuation report and/or traffic study report in respect of the project to facilitate shareholders' assessment of the transaction. The approach is consistent with the requirements of Rule 8.05B(2).

22. The Rules are not intended to apply to an acquisition of a completed infrastructure project, or a company holding the completed project, with a reasonable trading record (which is ordinarily expected to cover at least three years). This is because an accountants' report on the business or company will be available for shareholders to properly assess its operations and financial position.

23. In this case, the Exchange accepted that Rules 14.71 and 14A.70(9) would not apply to the Merger having regard to the following factors:

    - The Merger would involve Company A acquiring the rights to access, use and operate the assets which formed part of the then railway network of the Target Company under a service concession arrangement. The information and analysis provided by Company A indicated that a majority of the assets being acquired were related to completed infrastructure projects with a reasonable trading record.

    - The Circular would contain the accountants' report which would provide Company A's shareholders with the necessary information to make a properly informed assessment of the business being acquired under the Merger.

Conclusion

24. The Exchange decided to grant a waiver to Company A from strict compliance with Rule 14.69(4)(a)(i) on condition that the Circular would contain the alternative disclosure proposed by Company A in its waiver application.

25. The Exchange determined that Rules 14.71 and 14A.70(9) would not apply to the Merger.

HKEX 香港交易所

HKEX Guidance Letter
HKEX-GL103-19

April 2019 (Updated in January 2024)

Guidance on the presentation of non-GAAP measures

I. Purpose

1. This letter provides guidance on the presentation of non-GAAP measures in a listing document. The guidance is also set out in Chapter 3.11 of the Guide for New Listing Applicants.

II. Guidance

2. Non-GAAP measures are numerical measures of historical performance, financial position or cash flow that are not GAAP measures based on HKFRS or IFRS or CASBE (e.g. EBITDA, adjusted EBITDA and adjusted net profit).

3. An applicant and its sponsor should ensure that the presentation of non-GAAP measures is not misleading (see the IOSCO's "Statement on Non-GAAP Financial Measures"[1]). The following principles enhance the reliability and comparability of non-GAAP measures and minimise misleading disclosure:

Defining the non-GAAP measure

(i) Define each non-GAAP measure, reflect its composition, and explain the basis of calculation. The information that applicants provide regarding non-GAAP measures should be readily accessible (e.g. accompanying the non-GAAP measures) so that readers can easily find it when reading the measures.

(ii) Distinguish non-GAAP measures from GAAP measures by appropriate labelling (e.g. adjusted net profit (non-GAAP measure) and adjusted net profit margin (non-GAAP measure)).

(iii) Do not characterise or label a measure as EBIT/EBITDA if it is not, in which case such measure should be distinguished (e.g. adjusted EBIT/EBITDA (non-GAAP measure)).

(iv) Reasons for presenting the non-GAAP measure including usefulness of the information and the additional value provided to investors.

(v) Highlight that the non-GAAP measure does not have a standardised meaning prescribed by GAAP and therefore may not be comparable to similar measures presented by other issuers.

[1] The "Statement on Non-GAAP Financial Measures" was published by the IOSCO in June 2016.

Unbiased purpose

(i) Non-GAAP measures should not be used to avoid presenting adverse information to the market. For example, if non-recurring expenses are excluded, the non-recurring gains must also be excluded (i.e. do not "cherry pick" non-GAAP adjustments to achieve the most positive measure).

(ii) Do not use individually tailored accounting principles, including certain adjusted revenue measures (e.g. a non-GAAP measure that reflects revenue recognised over the service period under GAAP on an accelerated basis as if the applicant earned revenue when it billed its customers).

Ensure prominence of presentation of GAAP measures over non-GAAP measures

(i) Presentation of non-GAAP measures, including information provided for reference, should not confuse or obscure the presentation of GAAP measures.

(ii) GAAP measures should always be presented before the non-GAAP measures if they appear in the same section of a document. For example, the extract of the relevant GAAP results in the discussion of the results of operations should be presented immediately before the non-GAAP measures.

(iii) Do not present non-GAAP measures with more prominence, in more details or with greater emphasis than the GAAP measures. In any event, presenting a full non-GAAP income statement is prohibited.

(iv) Disclosures related to non-GAAP purpose and use should not state or imply that the non-GAAP measures are superior to, provide better information about, or more accurately represent the results of operations than GAAP measures.

Reconciliation to comparable GAAP measures

(i) The reconciliation should:

(a) Be quantitative.

(b) Be clear, concise and appropriately labelled.

(c) Begin with GAAP measures and reconciled to non-GAAP measures with reconciling items derived from the financial statements reported in GAAP (when a reconciling item cannot be extracted directly from the financial statements, show how this figure is calculated).

(d) Explain the nature of each adjustment.

Consistent presentation of non-GAAP measures

(i) Consistently present non-GAAP measures for comparative periods.

(ii) Explain the change in composition of the non-GAAP measures (if any), and provide comparative figures for the prior period with such figures adjusted to reflect the change in composition.

(iii) Explain the reason why a particular non-GAAP measure is no longer presented (if any).

(iv) An applicant should consider whether its non-GAAP measures are consistent with standard measures used in its industry or by its peers, and if not, state such fact, and explain the differences and how they may affect comparability with other companies.

Normal, recurring, cash operating expenses

(i) Avoid adjusting items that are (a) reasonably likely to recur in the foreseeable future, or are activities that affected the entity in the recent past and describing them as non-recurring, infrequent or unusual; or (b) normal and cash operating expenses necessary to generate revenue or normal and recurring charges.

(ii) Adjustments that are non-cash, non-recurring, and/or non-operating in nature (e.g. listing expenses, fair value change of convertible preferred shares which will be converted into equity upon listing, and share-based payments) are common adjusting items when presenting adjusted net profit (non-GAAP measure). The Exchange will request an applicant to remove any adjusting item which is considered as normal, recurring, cash operating expenses necessary to business operations (e.g. impairment of trade receivables relating to an applicant's normal business). In evaluating what is normal and/or recurring in nature, the applicant should consider the nature and effect of the non-GAAP adjustment and its relevance on business operations.

Treatment of tax adjustments

(i) Present reconciling adjustments on a gross basis before tax and avoid double counting.

(ii) Present and explain income taxes as a separate adjustment.

4. Sponsor should perform due diligence, and reporting accountants and other experts should perform appropriate procedures, to ensure accurate presentation of non-GAAP measures, including (i) the accuracy of the reconciling items; and (ii) the reasonableness of the adjustments (e.g. whether the adjustments would result in double counting).

5. The above guidance should also apply to listed issuers which present non-GAAP measures in any documents pursuant to the Listing Rules (e.g. financial reports, announcements and circulars).

Whether the Exchange would waive the requirement for the transaction circular to include a profit and loss statement on the property to be acquired by the listed issuer

Parties

- **Company A** – a Main Board listed issuer
- **Vendor** – an independent third party

Facts

1. Company A proposed to acquire from the Vendor a commercial building in Hong Kong (**Property**) for investment purposes. The acquisition would be a major transaction for Company A.

2. Before the proposed transaction, the Vendor had leased the units in the Property to third parties for rental income. Under Rule 14.67(6)(b)(i), as the Property was a revenue-generating asset with an identifiable income stream, Company A's circular for the acquisition would need to include a profit and loss statement for the Property's identifiable net income stream for the 3 preceding financial years, and the statement would need to be reviewed by the auditors or reporting accountants.

3. Company A applied for a waiver from Rule 14.67(6)(b)(i) because:

   (a) Despite Company A's request, the Vendor refused to provide the underlying books and records of the Property to Company A, except the subsisting tenancy agreements for various units in the Property (**Tenancy Agreements**) and some information on the expenses related to the Property. Company A was unable to properly compile the profit and loss statement for the Property's net income stream in the last 3 years given the limited information available from the Vendor.

   (b) Company A arrived at the consideration for the acquisition after arm's length negotiation with the Vendor taking into account the market value of the Property and other nearby properties. The circular would include a valuation report on the Property prepared according to the Rule requirements.

   (c) It would make alternative disclosures in the circular to enable shareholders to assess the transaction:

      (i) a summary of the Tenancy Agreements including the monthly rental income;

(ii) the gross rental income for the Property for the period from the commencement of the earliest Tenancy Agreement to the latest financial year end date; and

(iii) an estimate of the monthly expenses for the Property payable by the landlord based on the terms of the Tenancy Agreement and the experience of Company A's management in the property industry.

(d) Its directors were of the view that omission of a profit and loss statement for the Property's net income stream in the past would not render the circular materially incomplete or misleading or deceptive.

Relevant Listing Rules

4. Rule 14.67 requires that:

"… a circular issued in relation to an acquisition constituting a major transaction must contain:

…

(6)(b) on an acquisition of any revenue-generating assets (other than a business or company) with an identifiable income stream or assets valuation:

(i) a profit and loss statement and valuation (where available) for the 3 preceding financial years (or less, where the asset has been held by the vendor for a shorter period) on the identifiable net income stream and valuation in relation to such assets which must be reviewed by the auditors or reporting accountants to ensure that such information has been properly compiled and derived from the underlying books and records. The financial information on which the profit and loss statement is based must relate to a financial period ended 6 months or less before the circular is issued. The financial information on the assets being acquired as contained in the circular must be prepared using accounting policies which should be materially consistent with those of the listed issuer; …"

Analysis

5. Under the Listing Rules an issuer must ensure that the information in its circular for a notifiable transaction is accurate and complete in all material respects and not be misleading or deceptive. The circular must contain all information necessary to allow shareholders to make a properly informed decision on how to vote on a transaction.

6. In this case, Company A had no access to the accounting records and supporting documents to properly compile a profit and loss statement for the Property's net income stream as required. The Exchange considered that Company A had taken reasonable steps to provide alternative information to its shareholders for assessing the impact of the transaction on Company A, and the waiver would not result in an omission of material information in the circular.

Conclusion

7. The Exchange granted the waiver to Company A.

Financial disclosure

1. Given the Exchange has updated the audit terminology in the Listing Rules with reference to the Hong Kong Standards on Auditing (HKSAs) on auditor reporting, the terms "modified opinion" and "modified report" are defined in MB Rule 1.01 / GEM Rule 1.01. However, there is no definition of "modification" in the Listing Rules. Please clarify the use of the term "modification".

"Modification" is a generic term which should be read in the context of the Listing Rules.

Audit engagements

Where the financial information has been audited and an opinion has been expressed by the auditors / reporting accountants, then the term "modification" in the Listing Rules should refer to:

(a) a modified opinion (i.e. a qualified opinion, an adverse opinion or a disclaimer of opinion); and/or

(b) an emphasis of matter paragraph or a paragraph to highlight a material uncertainty related to going concern without modifying the opinion.

Review engagements

Where the financial information has been reviewed and a review conclusion has been expressed by the auditors / reporting accountants, then the term "modification" in the Listing Rules should refer to:

(a) a modified review conclusion (i.e. qualified conclusion, an adverse conclusion or a disclaimer of conclusion); and/or

(b) an emphasis of matter paragraph or a paragraph to highlight a material uncertainty related to going concern without modifying the review conclusion.

(Note: A review is substantially less in scope than an audit conducted in accordance with relevant HKICPA standards (or equivalent standards issued by IAASB and China Ministry of Finance). Currently, the applicable HKICPA standards for a review engagement are Hong Kong Standards on Review Engagements 2400 (Revised) and 2410.)

MB Rules 1.01, 4.18, 14.68(2)(a)(i), App D1A - 35, App D1C - 42(2), App D1E - 35, App D2 - 45(7) and 46(8)
GEM Rules 1.01, 7.22, 18.50(8), 18.64, 19.68(2)(a)(i), App D1A - 35, App D1C - 42(2)
First released: March 2019; last updated: May 2024

2. The Hong Kong Standards on Auditing require a listed issuer's auditor to report "Key Audit Matters" (KAM) in its audit report. Will the listed issuer need to disclose details of KAM in the preliminary results announcement?

There is no specific requirement under the Listing Rules for a listed issuer to provide details of KAM in its results announcement. For investors to better understand the financial statements and the audit that was performed, it is considered more appropriate that KAM should be read and considered together with the full audit report and the complete set of financial statements. Therefore, the listed issuer is recommended to publish its full annual report as soon as practicable after the preliminary results announcement has been issued.

MB Rules 1.01, App D2 - 45(7) and 46(8)
GEM Rules 1.01, 18.50(8), 18.64, 18.76 and 18.78(5)
First released: January 2017; last updated: May 2024

3. When the auditors express an unmodified opinion but include an "Emphasis of Matter" paragraph or a separate section under the heading "Material Uncertainty Related to Going Concern", will the listed issuer need to provide details in the preliminary results announcement?

Yes.

MB Rules 1.01, App D2 - 45(7) and 46(8)
GEM Rules 1.01, 18.50(8), 18.64, 18.76 and 18.78(5)
First released: January 2017; last updated: May 2024

4. When the interim results have been reviewed by the listed issuer's auditors and where the review report is modified, will the listed issuer need to provide details in the review report in the interim results announcement and select the headline category "Modified Report by Auditors" when submitting the announcement for publication?

Yes.

MB App D2 - 46(5), 46(6) & 46(7)
GEM Rules 18.61, 18.78(5), 18.78(6) and 18.78(7)
First released: January 2017; last updated: May 2024

5. Paragraph 24 of Appendix D2 to the MB Rules / GEM Rule 18.28 requires a listed issuer to disclose details of directors' emoluments on a named basis in its financial statements. Is it necessary to disclose the comparative figures for the corresponding previous period?

Yes.

MB App D2 - 24
GEM Rule 18.28
First released: March 2004; last updated: May 2024

6. What are the disclosure requirements under section 436 of the Companies Ordinance for a Hong Kong incorporated listed issuer in relation to the publication of non-statutory accounts under the Listing Rules, such as annual/interim results announcement, interim report, circulars or listing documents?

The listed issuer must include a statement indicating that the statement of comprehensive income for a full financial year and/or the statement of financial position at a financial year end (**Statements**) presented in the account are not statutory financial statements under the Companies Ordinance. The listed issuer must also disclose whether (a) an auditor's report had been prepared; and (b) the auditors gave a qualified or modified audit opinion on the Statements.

For details, please refer to Accounting Bulletin 6 "Guidance on the Requirements of Section 436 of the Hong Kong Companies Ordinance Cap. 622" issued by HKICPA.

MB Rules 4.25 to 4.29, 11.03, 11.04, 11.16 to 11.19, 13.48(1), 13.49(1), 13.49(6), 14.66 to 14.69, 14.60A, 14.61, App D2 - 45(1)
GEM Rules 7.27 to 7.31, 14.03, 14.06, 14.28 to 14.31, 18.49, 18.50(1), 18.53, 18.78, 19.60A, 19.61, 19.66 to 19.69
First released: February 2015; last updated: May 2024

7. For listed issuers incorporated outside Hong Kong, the Listing Rules require their directors' report to include disclosures as required under section 390 of the Companies Ordinance, except for the names of their subsidiaries' directors under section 390(3)(b). Are they required to comply with the requirements under section 390(4) to (7) (New Sections) which were added to the Companies Ordinance in 2018 to allow a holding company incorporated in Hong Kong to make available a list of the names of its subsidiaries' directors on its website or at its registered office for inspection by the members, instead of disclosing those names in the directors' report?

No. As the Listing Rules do not require listed issuers incorporated outside Hong Kong to disclose the names of their subsidiaries' directors in the directors' report, the New Sections do not apply.

MB App D2 - 28(2)(a) and 28.2
GEM Rule 18.07A(2)(a) and Note 2 to 18.07A
First released: February 2015; last updated: May 2024

Recognition of overseas audit firms under the Accounting and Financial Reporting Council Ordinance

1. AFRC is Hong Kong's independent regulator of listed entity auditors. All audit firms intending to carry out a PIE Engagement are subject to a system of registration (for Hong Kong audit firms) and recognition (for non-Hong Kong audit firms[1]) as PIE Auditors.

Any overseas audit firm is required to be recognised by the AFRC before the overseas audit firm can (i) undertake (i.e. accept an appointment to carry out) any PIE Engagement; and (ii) carry out any PIE Engagement for an overseas issuer. Under the AFRCO, the Exchange needs to issue a statement of no objection (SNO) before the AFRC considers an application of the overseas audit firm to be recognised as a Recognised PIE Auditor. The overseas audit firm must not accept an appointment for carrying out any PIE Engagement for an overseas issuer unless the application for recognition has been granted by the AFRC.

(i) Which types of engagements fall within the PIE Engagements?

The audit engagements falling within the PIE Engagements are summarised below:

Preparation of auditors' or accountants' report	Is it a PIE Engagement?
Annual financial statements	√
Listing document	√
Very substantial acquisition	√
Reverse takeover	√
Major transaction	×
Very substantial disposal	×
Extreme transaction	×
De-SPAC transaction	×

For those engagements not falling within the PIE Engagements, such as accountants' reports included in major transaction and very substantial disposal circulars, the Listing Rules continue to apply. Therefore, it is at the Exchange's discretion to accept an overseas audit firm as the reporting accountants under the Listing Rules and recognition with the AFRC is not required.

[1] Recognition of overseas audit firms does not apply to audit firms located in Mainland China. Under the AFRCO, the endorsed Mainland China audit firms (for the PRC issuers only) will be recognised as a PIE Auditors without a recognition application being made to the AFRC.

(ii) Who should submit the formal application to the AFRC for appointing an overseas audit firm for the PIE Engagement?

It is the responsibility of the overseas issuer to submit the application, together with a SNO issued by the Exchange. The AFRC considers the application of an overseas audit firm on a case-by-case basis.

The overseas issuers are reminded that they should plan their applications ahead and allow sufficient time to seek the SNO and obtain the AFRC's approval for recognition of a Recognised PIE Auditor. For further details on the recognition of overseas audit firms, please refer to the AFRC's website.

MB Rules 4.03, 19.20 and 19C.16
GEM Rules 7.02 and 24.13
First released: September 2019; last updated: May 2024

2. What information should be submitted to the Exchange when making an application for a SNO?

The SNO application must be made in writing. Based on all relevant facts and circumstances, the overseas issuer should provide an explanation, that supports the SNO application, and all other relevant information that it reasonably believes should be brought to the Exchange's attention, including but not limited to:

(i) Details of the PIE Engagement and role of the overseas audit firm acting as:

a. auditors; and/or
b. reporting accountants.

(ii) Information of the overseas issuer or the business, company or companies being acquired (collectively **target** in the case of an acquisition), including its name, address, place of incorporation and nature of the business of the group/target.

(iii) Information of the overseas audit firm, including:

a. having an international name and reputation;

b. being a member of, or registered with, an accountancy body (please specify the name of accountancy body in the home country) that is a member of the International Federation of Accountants (**IFAC**)[2]; and

c. being subject to independent oversight by a regulatory body of a jurisdiction (please specify the name of regulatory body in the home country) that is a signatory to the IOSCO MMOU[3].

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2 A SNO issued by the Exchange is one of the eligibility criteria to be a Recognised PIE Auditor. There is no indication that the overseas audit firm mentioned in the SNO will be approved by the AFRC, as the AFRC has the following additional criteria:
(a) the overseas audit firm is subject to the regulation of an overseas regulatory organisation recognised by the AFRC; and
(b) the overseas audit firm has adequate resources and possesses the capability to carry out a PIE Engagement for the overseas issuer.
Generally, an overseas regulatory organisation is recognised by the AFRC, if it is a member of the International Forum of Independent Audit Regulators (IFIAR); or from a jurisdiction which has attained equivalence status granted by the European Commission under Article 46 of the Statutory Audit Directive 2006/43/EC. For details, please refer to the AFRC's website.

3 It would be acceptable if the relevant audit oversight body is not a signatory to the IOSCO MMOU but the securities regulator in the same jurisdiction is a full signatory to the IOSCO MMOU.

(iv) Auditing and financial reporting standards adopted in relation to the PIE Engagement.

(v) Reasons for engaging an overseas audit firm to undertake the PIE Engagement[4], such as:

a. the overseas audit firm has a geographical proximity and familiarity with the businesses of that overseas issuer or the target; and/or

b. that overseas issuer or the target is listed on a Recognised Stock Exchange (as defined in MB Rule 1.01 / GEM Rule 1.01), and the overseas audit firm is the auditor of that overseas issuer or the target; and/or

c. the overseas audit firm is the statutory auditor of that overseas issuer or the target.

MB Rules 4.03, 19.20 and 19C.16
GEM Rules 7.02 and 24.13
First released: September 2019; last updated: May 2024

3. Is an overseas issuer required to apply for a "new" SNO in the following circumstances:

(i) Annual renewal of the recognition (i.e. "same" overseas audit firm) to the AFRC?

No. The SNO is not required when applying for renewal of the recognition to the AFRC.

(ii) To appoint an overseas audit firm (who is the auditors of the issuer) as its reporting accountants for a transaction circular, which falls within the PIE Engagements?

No. The SNO is not required. In addition, the issuer does not have to re-apply for recognition to the AFRC when the recognition of that audit firm remains valid.

Note: Although the SNO is not required, the issuer is required to apply MB Rule 4.03 / GEM Rule 7.02 waiver for a new engagement as required under the Listing Rules.

(iii) To appoint "another" overseas audit firm as its auditors or reporting accountants for a transaction circular (which falls within the PIE Engagements)?

Yes. The issuer should make a fresh recognition application, together with the SNO, to the AFRC.

MB Rules 4.03, 19.20 and 19C.16
GEM Rules 7.02 and 24.13
First released: September 2019; last updated: May 2024

[4] The Exchange will consider exercising its discretion not to issue a SNO if the overseas issuer fails to satisfy the Exchange of its reasons for its engagement of an overseas audit firm to undertake the PIE Engagement.

4. Does an overseas issuer need to apply for a waiver of MB Rule 4.03 / GEM Rule 7.02, in addition to seeking the SNO, when it plans to appoint an overseas audit firm as reporting accountants for its PIE Engagement?

Yes. The waiver and SNO are granted on a case-by-case basis.

The overseas issuer is required to submit a waiver application together with its SNO application. The Exchange will grant this waiver, provided that the overseas audit firm is recognised by the AFRC. The overseas issuer should also disclose this waiver, including its details and reasons, in the circular or listing document.

MB Rule 4.03
GEM Rule 7.02
First released: September 2019; last updated: May 2024

5. Does an overseas issuer have to disclose in its annual report, circular or listing document that its auditors or reporting accountants for a PIE Engagement are the Registered or Recognised PIE Auditors?

Yes.

MB Rules 4.03, 19.20 and 19C.16
GEM Rules 7.02 and 24.13
First released: September 2019; last updated: May 2024

6. Is a PRC issuer permitted to appoint an overseas audit firm as its reporting accountants for the preparation of the accountants' report in a notifiable transaction circular relating to the acquisition of an overseas company (regardless of whether it constitutes a PIE Engagement)?

Yes, provided that the PRC issuer seeks a waiver from strict compliance with MB Rule 4.03 / GEM Rule 7.02, and obtains a SNO (in the case of PIE Engagements) from the Exchange.

MB Rules 4.03 and 19A.08
GEM Rule 7.02
First released: September 2019; last updated: May 2024

4

Trading halt, suspension, cancellation and withdrawal of listing

4.1 Trading halt, suspension and resumption

4.2 Long suspension and delisting

Guidance letter – Guidance on long suspension and delisting	GL95-18	4.2 – 1
Guidance letter – Guidance on investigations conducted by long suspended issuers	GL120-24	4.2 – 15
Listing decision – Whether the Exchange would cancel the listing of a listed issuer whose shares had been suspended from trading for a prolonged period due to insufficient public float	LD110-2017	4.2 – 26

Guidance on trading halts

I. Purpose

1. This letter sets out the criteria and principles of trading halts. It provides guidance on good practices about trading halts pending disclosures of material information by listed issuers. For the Exchange's practice and guidance on trading resumption of companies suspended due to insufficient operations or other material regulatory issues, please see our Guidance on long suspension and delisting (HKEX-GL95-18). Issuers should also refer to the "Guidelines on Disclosure of Inside Information" published by the Securities and Futures Commission (**SFC**) for guidance on their Inside Information (as defined in the Securities and Futures Ordinance (**SFO**)) disclosure obligations under the SFO.

II. Criteria and principles of trading halts

2. The Exchange is the front line regulator of listed issuers. It has a statutory obligation under the SFO to ensure, so far as reasonably practicable, an orderly, informed and fair market in the trading of securities.

3. For this purpose or the protection of investors the Exchange may suspend trading in any securities. Trading halts are tools to address both potential and actual false, unfair or disorderly market. Trading halts serve to protect investors by allowing trading on a fully informed basis. By creating a break in trading they aim to avert the risk of a false, unfair or disorderly market or where such conditions are already emerging.

4. At the same time, to ensure the proper functioning of the market, any trading halt should be kept to a period that is absolutely necessary to ensure investors are not denied reasonable access to the market.

5. Although other jurisdictions have trading halt procedures in place based on broadly similar objectives, the detail of the arrangements is usually tailored to local circumstances and often varies considerably.

III. Guidance on good practices about trading halts pending disclosures of material information by listed issuers

Where a trading halt is necessary

6. Under Main Board Rule 13.10A and GEM Rule 17.11A, an issuer must, as soon as reasonably practicable, apply for a trading halt (where an announcement cannot be made promptly) in the following circumstances:

   (a) it has information which must be disclosed to avoid, in the opinion of the Exchange, a false market[1]; or

[1] For the meaning of "false market" and an issuer's obligation to avoid it, see FAQ10 - No.1.

(b) it reasonably believes that there is Inside Information which must be disclosed under the Inside Information Provisions[2]; or

(c) circumstances exist where it reasonably believes or it is reasonably likely that confidentiality may have been lost in respect of certain Inside Information.

Avoiding and minimising halt

7. While a trading halt may be necessary to protect investors or to maintain an orderly market, in the interests of promoting a continuous market the Exchange would expect listed issuers to plan their affairs so that a trading halt can be avoided and/or any halt can be kept as short as is reasonably possible. The duration of any trading halt should be for the shortest possible period. Listed issuers are obliged to ensure that trading of their securities resume as soon as practicable following the publication of an announcement or when the reasons for the trading halt no longer apply[3].

8. Under the Listing Rules issuer announcements containing Inside Information can only be published outside trading hours. Accordingly, significant agreements should only be signed outside, and not during, trading hours. Listed issuers should prepare their announcements ahead of signing of agreements such that they can be released immediately after agreements are signed.

9. Listed issuers undertaking transactions which involve complex or controversial issues or for which announcements require pre-vetting by the Exchange[4] should seek early consultations with, or regulatory clearance from, the Exchange. This process should take place before, and not after, the signing of a significant agreement so as to avoid and/or minimise the duration of any trading halt.

10. In preparing transaction announcements, listed issuers should ensure that the information is clearly presented in plain language and the announcements include information which is required under the Listing Rules, the Inside Information Provisions and any other information which is relevant and material to investors. Unnecessarily lengthy disclosures may result in delaying the release of the announcement thereby prolonging the trading halt. It may also hinder investors' understanding and appraisal of the transaction.

11. Where trading is halted pending an announcement of a transaction, the issuer should publish the transaction announcement and resume trading as soon as possible. If there is a development during the trading halt (e.g. further negotiation that may materially change the terms of the agreement), it would be inappropriate for the issuer to continue the trading halt pending the outcome of its negotiation. In such situation, the issuer is still required to publish the transaction announcement in compliance with the Listing Rules and Inside Information Provisions and resume trading as soon as possible.

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2 Part XIVA of the Securities and Futures Ordinance

3 Main Board Rule 6.05. See also GEM Rule 9.09 which requires an issuer to use its reasonable endeavours to obtain all relevant consents necessary to ensure the lifting of such trading halt or suspension.

4 Main Board Rule 13.52(2) and GEM Rule 17.53(2) require certain types of announcements to be pre-vetted and cleared by the Exchange prior to publication.

Incomplete proposals and business negotiations

12. Listed issuers are subject to, among others, Part XIVA of the SFO to disclose its Inside Information and the Exchange would refer listed issuers to their legal advisers and the guidelines published by the SFC. One commonly used safe harbour from the obligation to disclose Inside Information under the SFO is the preservation of confidentiality of information concerning an incomplete proposal or business negotiation. To maintain a fair, orderly and continuously trading market the Exchange would also expect listed issuers to take effective and appropriate measures to preserve confidentiality of such information including, for example, execution of enforceable confidentiality undertakings and use of code names in circulating draft documents amongst professional parties. The Exchange would only agree to a trading halt if there appears to be a reasonable concern on the leakage of Inside Information and/or practical difficulty in maintaining confidentiality.

Response to Exchange's enquiries

13. The Exchange routinely monitors share price and volume movements and reviews print and online media news to detect possible leakages of Inside Information and to prevent the possible development of any false or unfair market in the trading of securities. It is critically important that authorised representatives of listed issuers are contactable at all times and are in a position to answer enquiries from the Exchange on any unusual share price and volume movements and media news. They are expected to confirm (i) whether the directors are aware of any matter of development that is or may be relevant to the unusual trading movement of its listed securities, or information necessary to avoid a false market, or any inside information which needs to be disclosed under the Inside Information Provisions[5], and (ii) if so, provide details.

14. Where listed issuers are engaged in confidential business negotiation they should also monitor their share price and volume movements and media coverage to ensure that their measures to preserve confidentiality are effective. In response to any Exchange's enquiries on a listed issuer's unusual share price and volume movements and/or media coverage, the issuer must promptly and carefully assess whether it has a disclosure obligation under the SFO to disclose its Inside Information, if any.

15. In all cases listed issuers should have in place an appropriate delegation of authority to allow for timely release of information to the Exchange and, where appropriate, to the public by publication of an announcement. Such delegation should enable the authorised representatives to timely request a trading halt pending publication of an announcement.

Handling of specific market speculations and negative publicity

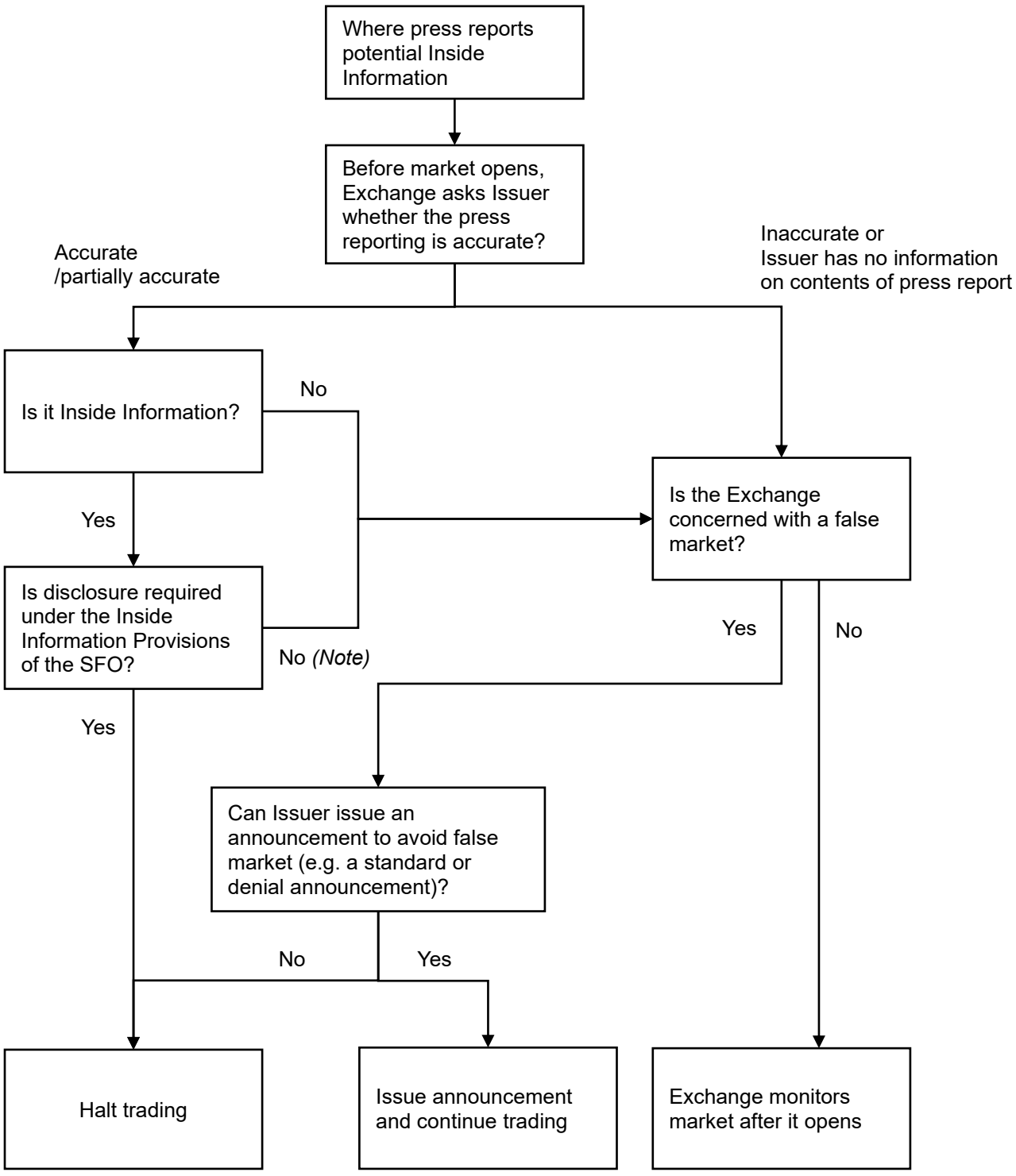
16. From time to time there appear in the market specific rumors, speculations or negative publicity made by commentators. In these circumstances such issuers' directors must promptly and carefully assess whether a disclosure obligation arises under the SFO and the Listing Rules.

[5] Main Board Rule 13.10(2) and GEM Rule 17.11(2)

17. Whilst an issuer is not generally expected to respond to market comments, if any market comment has, or is likely to have, an effect on the issuer's share price/volume such that there may potentially be a false market, the Exchange may require the issuer to make a clarification announcement. Where the issuer is unable to make such announcement promptly, the Exchange may require it to request a trading halt pending the clarification to address potential or actual false market. It is therefore important for issuers to establish procedures to actively monitor their share price and any news, comments or reports relating to them circulated in the market. Issuer directors should ensure that they have a proper understanding of the issuer's business, financial position and prospects and there is an effective system for them to continuously monitor developments so that they can promptly and accurately respond to the Exchange's enquiries concerning the issuer's affairs and where necessary publish announcements to correct or prevent a false market.

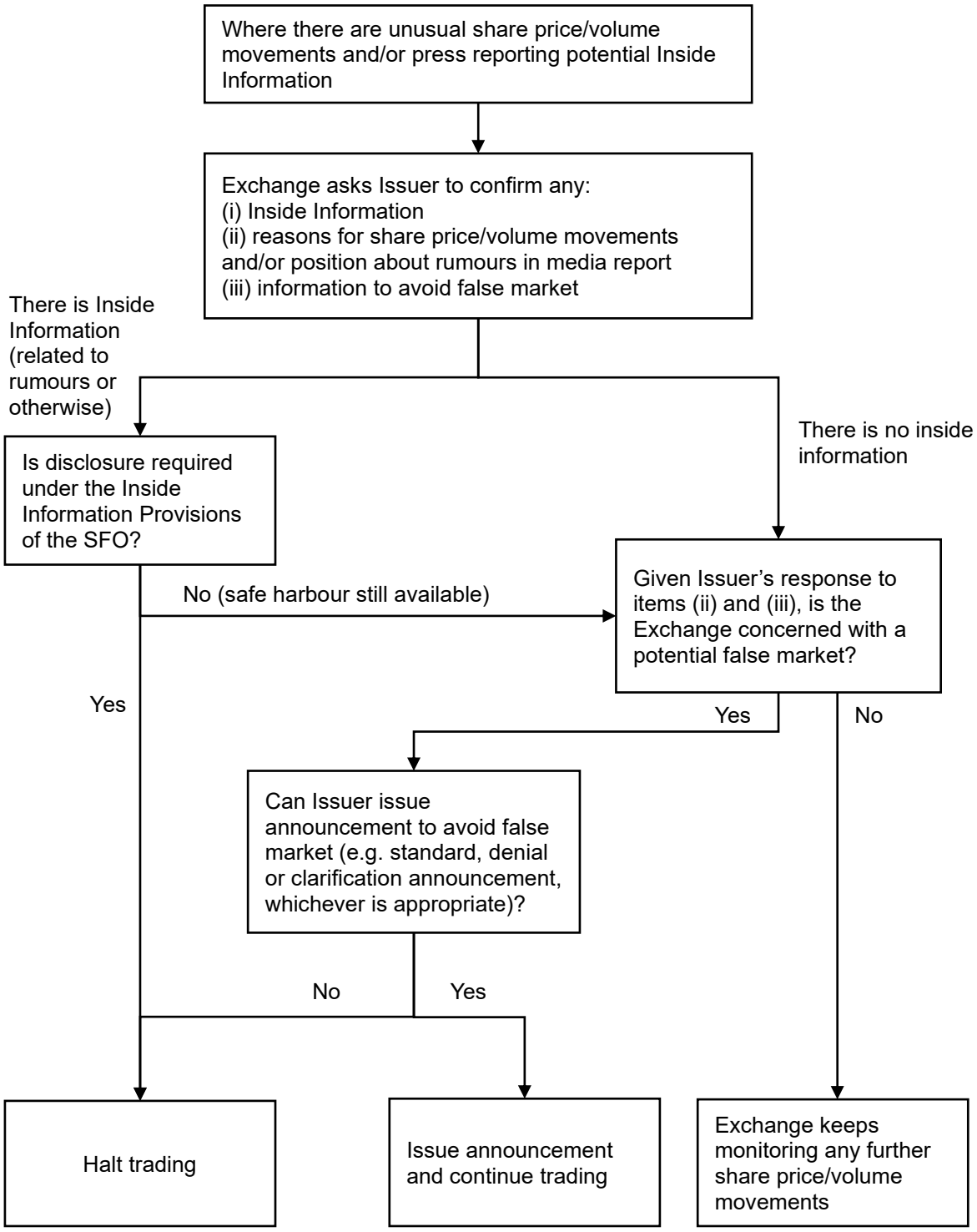
18. Please see below two decision-tree-diagrams illustrating the scenarios where the Exchange enquires about an issuer's unusual share price and/or volume movements and/or market comments:

Decision tree about whether a trading halt is appropriate where the Exchange detects a possible leakage of Inside Information before market opens



Note: for example, with safe harbour under section 307D(l) of the SFO

Decision tree about whether a trading halt is appropriate where the Exchange detects a possible leakage of Inside Information during trading hours



Special considerations about dual or multiple listings and A and H share issuers

19. Dual or multiple-listed issuers must ensure, as far as practicable, simultaneous dissemination of information in the different markets and, if that is impracticable (e.g. for time zone differences), that the information is disseminated before the market opens in Hong Kong.

20. For A and H share issuers, the Exchange and the PRC Exchanges closely co-ordinate and communicate as simultaneous trading halts in both markets are generally necessary to maintain a fair and orderly market in the trading of the respective A and H shares. If an A and H share issuer has unpublished material information warranting a trading halt in both markets, such trading halt requests should be made by the issuer with both exchanges simultaneously. The issuer should also release its announcement containing the material information in both markets simultaneously such that, as far as practicable, trading resumption can be achieved at both markets at the same time. In other specific circumstances where trading halt or suspension is required in one market, and not the other, under the respective home market rules, the A and H share issuer should announce the reason for the trading halt or suspension as soon as practicable to ensure that shares in the other market can continue to trade in an orderly manner.

IV. Keeping the market well informed during a trading halt

21. Under the Listing Rules, listed issuers must release an announcement promptly after a trading halt is effected to inform the market of a reason for its trading halt, e.g. “trading in the shares of Issuer A … has been halted … pending the release of an announcement containing inside information…”. To make such announcements meaningful, listed issuers should disclose details (such as the subject of the transaction and the applicable Listing Rule classifications) on the reason for the trading halt, e.g. “ trading in the shares of Issuer A … has been halted … pending the release of an announcement about a further issuance of equity securities amounting to 5% of Issuer A’s existing issued shares which would constitute a connected transaction for the purpose of the Listing Rules and Inside Information for the purpose of the SFO…”

22. If a trading suspension cannot be avoided and significant time is expected to be needed to prepare and release the relevant material information, listed issuers should nevertheless publish periodic updates (**holding announcements**) on their progress towards such preparation of information disclosure and trading resumption.

23. Listed issuers are reminded that, under Section 307B(1) of the SFO, they must disclose their Inside Information as soon as reasonably practicable. This legal obligation exists irrespective of whether trading in its listed securities is suspended or otherwise.

V. Administrative matters

24. Under Main Board Rule 13.10A and GEM Rule 17.11A, a listed issuer must apply for a trading halt in certain circumstances where an announcement cannot be promptly made. If a trading halt is necessary, such request should be made in writing before 9:00 am for trading halt in the morning trading session and 1:00 pm for trading halt in the afternoon trading session.

25. Any request for a trading halt must be supported with reasons and the Exchange would consider if a trading halt is appropriate in the circumstances. Resumption of trading, in the majority of cases, takes place from the next immediate trading window following publication of material information by listed issuers and, in a few cases, fulfillment of specific conditions imposed by the Exchange.

Whether the Exchange would agree to a listed issuer's request for a trading halt pending the outcome of its creditors' meeting

Facts

1. The Exchange was informed by a listed issuer (**Company A**) shortly after close of trading that it was due to have a meeting with its bank creditors the following day to advise them of the need to restructure the group's borrowings.

2. Company A submitted that there was uncertainty as to the outcome of the meeting. Company A also informed the Exchange that it had, in preparation for such meeting, provided updated financial information to its bank creditors.

3. Company A therefore requested a suspension of trading in its securities pending announcement of the outcome of the meeting and release of such updated financial information.

Relevant Listing Rules

4. Note (1) to Rule 6.02 of the Listing Rules provides that, "unless the Exchange considers that the reasons given in support of a suspension request warrant a suspension, it will expect a clarifying announcement to be issued instead".

Analysis

5. Company A had sufficient time to release an announcement to inform the public of the upcoming bank creditors' meeting and to update the public on its financial position. Company A should then follow up with a further announcement in due course.

Conclusion

6. The reasons given for the suspension request did not warrant a suspension and, the issue of an announcement was preferable to an unwarranted suspension. Company A therefore issued a press announcement in relation to its financial position and upcoming bank creditors' meeting and its securities continued to trade the next day.

Whether the Exchange would direct the resumption of trading in a listed issuer's shares

Parties

- **Company A** – a Main Board issuer
- **Group** – Company A and its subsidiaries

Facts

1. At its request, trading in Company A's shares was suspended pending release of inside information about regulatory investigations in the PRC involving its director and controlling shareholder (**Mr. A**). It subsequently disclosed that:

    - Mr. A was not contactable. Based on the information available to Company A, Mr. A was assisting regulatory authorities in the PRC in their investigations. The subject matter of the investigations and Mr. A's involvement in this matter were unknown to Company A. The regulatory authorities asked Company A about certain projects of the Group, took away certain books and records of the Group, and froze certain bank accounts of the Group.

    - Company A failed to repay certain bank loans when due, which triggered cross-defaults of other bank loans.

2. During the trading suspension, Company A continued to announce information available to it regarding the investigations, its assessment of the impact of the investigations on the Group, its negotiations on repayment schedules of outstanding bank loans and other actions taken to manage the Group's cash flow. Company A also published its audited financial results required by the Rules, which did not reveal any accounting irregularities or possible fraudulent activities on the part of the Group. The Group continued to operate its businesses and was able to secure new contracts with customers.

3. Based on Company A's disclosures, the Exchange considered that the reasons for the initial trading suspension no longer applied and Company A had satisfied the conditions for trading resumption imposed on it (see also guidance on long suspension and delisting set out in the Exchange's Guidance Letter HKEX-GL95-18).

4. In response, Company A sought to continue the trading suspension for these reasons:

- *Exceptional circumstances of the case:* Company A referred to Note 1 to Rule 6.05 which states that ñ*The Exchange is under an obligation to maintain an orderly and fair market for the trading of all Exchange listed securities and listed securities should be continuously traded save in exceptional circumstances.*ò It viewed ñ*exceptional circumstances*òas those not ordinarily encountered or anticipated and were beyond the control of the listed issuer concerned. It believed that its situation was exceptional and merited the Exchange allowing the continuing suspension.

- *Trading resumption not in the best interests of shareholders:* Company A submitted that with the benefit of the trading suspension, it had made significant progress in negotiating with banks for new repayment schedules of its outstanding loans. It was concerned that there would likely be panic selling of its shares by some shareholders after trading resumption, which would undermine the prospects of its negotiations with banks of the Group's credit facilities.

- *Undisclosed information:* Company A did not have the details of the investigations and was unable to make an informed view on the impact of the investigations on the Group's operations. It would be appropriate for the trading suspension to continue pending better understanding of these matters.

Relevant Listing Rules

5. Main Board Rules 6.05 to 6.07 and Paragraph 4 of Practice Note 11 states that:

ñ*6.05 The duration of any trading halt or suspension should be for the shortest possible period. It is the issuerôs responsibility to ensure that trading in its securities resumes as soon as practicable following the publication of an appropriate announcement or when the specific reasons given by the issuer supporting its request for a trading halt or suspension of trading in its securities, under rule 6.02, no longer apply*

Note : (1) The Exchange is under an obligation to maintain an orderly and fair market for the trading of all Exchange listed securities and listed securities should be continuously traded save in exceptional circumstances.

(2) The Exchange considers that the continuation of any trading halt or suspension beyond such period as is absolutely necessary denies reasonable access to the market and prevents its proper functioning.

6.06 Where trading has been halted or suspended the issuer shall notify the Exchange of:

(1) any change in circumstances affecting the reasons provided to the Exchange supporting the trading halt or suspension under rule 6.02; and

(2) any additional reasons which the issuer wishes the Exchange to take into account in the Exchange's determination whether or not the trading halt or suspension should be continued.

Note : (1) It is the issuerôs responsibility to provide the Exchange with all relevant information, which is within the issuerôs knowledge, to enable the Exchange to make an informed decision whether or not the trading halt or suspension of trading in the issuer's securities continues to be appropriate.

6.07 The Exchange shall have the power to direct the resumption of trading of halted or suspended securities. In particular the Exchange may:

(1) require an issuer to publish an announcement, in such terms and within such period as the Exchange shall in its discretion direct, notifying the resumption of trading in the issuer's halted or suspended securities, following the publication of which the Exchange may direct resumption of trading; and/or

(2) direct a resumption of trading following the Exchangeôs publication of an announcement notifying the resumption of trading in the halted or suspended securities.ò

Paragraph 4 of Practice Note 11

ñIn the interest of a fair and continuous market, the Exchange requires a trading halt or suspension period to be kept as short as is reasonably possible. This means that an issuer must publish an appropriate announcement as soon as possible after the trading halt or suspension arises. Under normal circumstances, the Exchange will restore dealings as soon as possible following publication of an appropriate announcement, or after specific requirements have been met. Failure by an issuer to make an announcement when required, may, if the Exchange feels it to be appropriate, result in the Exchange issuing its own announcement and a restoration of dealings without an announcement by the issueré ò

Analysis

6. The Exchange has a statutory duty to maintain a fair, orderly and informed market for the trading of securities and act in the interest of the investing public. The structure of the Listing Rules and the continuing obligations regime place the onus on listed issuers to avoid or minimise the duration of any suspension of trading. In the interest of promoting a continuous market for trading of listed securities, the duration of any suspension should be for the shortest possible period.

7. The Exchange disagreed with the reasons provided by Company A for the continued suspension of trading:

- The Exchange did not consider Company A's circumstances to be "exceptional" to justify the trading suspension. Suspension is a tool to facilitate the Exchange's role to maintain a fair, orderly and efficient market for the trading of securities or for the protection of investors. "Exceptional circumstances" to justify continuing suspension must serve these purposes. Where Company A might consider its circumstances to be "exceptional" and continued trading suspension to be in its best interests, the Exchange must also consider the interest of the investing public.

  This case did not fall into any "exceptional circumstances" in the Rules that require trading suspension. Company A submitted that it did not have any unpublished information constituting inside information under the Securities and Futures Ordinance (**SFO**).

- A trading suspension should not be used as a means to facilitate negotiations of the Group's credit facilities. Issuers are not allowed to suspend trading in listed shares to artificially "maintain" a price which may not be reflective of the market price. Provided that investors are provided with all material information about the listed securities, the securities will be traded on an informed basis.

- While Company A did not have the details of the investigations and was unable to ascertain any future impact of the investigations on the Group, it had disclosed all available information regarding the investigations to the extent possible. The impact of the investigations on the Group had been revealed through its announcements and financial reports published after the trading suspension. Company A had admitted that it had no inside information disclosure obligation under the SFO. It was not appropriate to continue with the trading suspension pending future development in the investigation.

- Whether trading in Company A's shares was suspended or not, it was obliged to disclose inside information as soon as reasonably practicable to comply with the SFO.

8. The Exchange considered that Company A had failed to provide sufficient reasons to justify the continued trading suspension. Having considered the circumstances of this case and the fact that Company A did not have any inside information yet to be disclosed, the Exchange decided to direct the resumption of trading in Company A's shares under Rule 6.07.

Conclusion

9. The Exchange directed the resumption of trading in Company A's shares under Rule 6.07.

Whether the Exchange would direct the resumption of trading in a listed issuer's shares

Parties

- **Company X** – a PRC issuer whose H shares were listed on the Main Board
- **Subsidiary** – a subsidiary of Company X whose shares were listed on a PRC stock exchange

Facts

1. At the request of Company X, trading of its H shares on the Exchange was suspended on Day 1 pending the publication of an announcement about a share reform proposal of the Subsidiary (**Proposal**) which Company X considered to be price sensitive information.

2. Based on the information available from Company X:

   - Company X was then interested in approximately 70% of the Subsidiary's issued share capital. Trading in the Subsidiary's shares on the PRC stock exchange had also been suspended.

   - Company X's board of directors had resolved to approve, in principle, the Proposal subject to Company X and the Subsidiary entering into a merger agreement (which would then determine the final terms and conditions of the Proposal).

   - The Proposal would involve the issue of A shares by Company X, at specific exchange ratios (**Exchange Ratios**), to other shareholders of the Subsidiary as consideration for the cancellation of the Subsidiary's shares held by them, with a cash alternative for those who did not wish to receive in whole or in part the A Shares. The A Shares would be listed on a PRC stock exchange subject to the approval of relevant regulatory authorities. The Proposal's implementation would result in the merger of the Subsidiary with Company X.

3. Following the suspension of trading in its H shares, Company X published an announcement (**Announcement**) about the Proposal. The Announcement contained the Proposal's salient features including the preliminary Exchange Ratios and cash alternative amounts and their effects.

4. The Announcement stated that trading in Company X's H shares would continue to be suspended pending the release of an announcement of the signing of the relevant merger agreement and the determination of the Exchange Ratios. Company X also made a submission to the Exchange requesting continued suspension of trading in its H shares because:

   - The Subsidiary had to comply with PRC law and regulations, including consulting its shareholders during a period of 10 days following the release of the announcement concerning the Proposal and trading in the Subsidiary's shares on the PRC stock exchange would remain suspended during this period. The Exchange Ratios and cash alternative amounts would be determined and fixed upon completion of the consultation. The Exchange Ratios and cash alternative amounts disclosed in the Announcement were preliminary proposals only and were subject to change.

   - Continued suspension of trading in the shares of the Subsidiary prior to completion of the consultation period complied with the relevant PRC laws and regulations in relation to share reforms. Company X was of the view that as the Proposal would involve the issue of A Shares by Company X, any fluctuation in the market price of its H shares prior to the resumption of trading of the Subsidiary's shares on the PRC stock exchange would affect the Exchange Ratios and cash alternative amounts, and in turn the chance of success of the Proposal.

Relevant Listing Rules

5. Rule 6.01 provides that the Exchange may suspend dealings in any securities and impose such conditions as it thinks fit if it considers it necessary for the protection of investors or the maintenance of an orderly market.

6. Rule 6.05 provides that:

   The duration of any suspension should be for the shortest possible period. It is the responsibility of the issuer of securities suspended from trading to ensure that trading in its securities resumes as soon as practicable following the publication of an appropriate announcement in accordance with Rule 2.07C or when the specific reasons given by the issuer in support of its request for a suspension of trading in its securities, pursuant to Rule 6.02, no longer apply.

   Note:(1) The Exchange is under an obligation to maintain a orderly and fair market for the trading of all Exchange listed securities and listed securities should be continuously traded save in exceptional circumstances

   (2) The Exchange considers that the continuation of any suspension beyond such period as is absolutely necessary denies reasonable access to the market and prevents its proper functioning.

7. Rule 6.06 provides that:

   Where trading has been suspended the issuer of the relevant securities shall notify the Exchange of:

   (1) any change in circumstances affecting the reasons provided to the Exchange in support of the suspension pursuant to Rule 6.02; and

(2) any additional reasons which the issuer wishes the Exchange to take into account in the Exchange's determination whether or not the suspension of dealing in the issuer's securities should be continued.

Note: (1) It is the responsibility of the issuer of the suspended securities to provide the Exchange with all relevant information, which is within the knowledge of issuer, to enable the Exchange to take an informed decision whether or not the suspension of trading in that issuer's securities continues to be appropriate.

8. Rule 6.07 provides that:

The Exchange shall have the power to direct the resumption of trading of suspended securities. In particular the Exchange may:

(1) require a listed issuer to publish an announcement, in such terms and within such period as the Exchange shall in its discretion direct, notifying the resumption of trading in the issuer's suspended securities, following the publication of which the Exchange may direct resumption of trading; and/or

(2) direct a resumption of trading following the publication of an announcement by the Exchange notifying the resumption of trading in the suspended securities.

9. Rule 6.08 provides that:

The Exchange's power under rule 6.07 shall be subject to the review process set out in rule 2B.06. An issuer opposing the resumption of trading in its securities has the burden of satisfying the Exchange that a continued trading halt or suspension would be appropriate.

Note :(1) The Exchange is under an obligation to maintain an orderly and fair market for the trading of all Exchange listed securities and listed securities should be continuously traded save in exceptional circumstances.

(2) The Exchange considers that the continuation of any trading halt or suspension beyond such period as is absolutely necessary denies reasonable access to the market and prevents its proper functioning.

(3) See Practice Note 11.

10. Paragraph 4 of Practice Note 11 of the Listing Rules provides that:

In the interests of a fair and continuous market, the Exchange requires a suspension period to be kept as short as is reasonably possible. This means that an issuer must publish an appropriate announcement as soon as possible after the suspension arises. Under normal circumstances, the Exchange will restore dealings as soon as possible following publication of an appropriate announcement, or after specific requirements have been met.

Failure by an issuer to make an announcement when required, may, if the Exchange feels it to be appropriate, result in the Exchange issuing its own announcement and a restoration of dealings without an announcement by the issuer.

The Exchange wishes to re-emphasize the importance of proper security within an issuer, and the responsibility of the directors to ensure a proper and timely disclosure of all information necessary to investors to establish a fair and realistic valuation of securities traded in the market.

Analysis

11. The Exchange is under an obligation to maintain an orderly and fair market for the trading of all listed securities, and listed securities should be continuously traded except in exceptional circumstances. Continuation of any suspension beyond such period as is absolutely necessary denies reasonable access to the market and prevents its proper functioning. The structure of the Listing Rules and the continuing obligation regime place the onus on issuers to avoid any suspension of trading.

12. Any request for suspension must be supported by specific reasons and the burden is on the issuer to satisfy the Exchange that a suspension would be appropriate. Where trading has been suspended, it is the issuer's responsibility to provide the Exchange with all relevant information to enable it to take an informed decision whether or not the suspension continues to be appropriate.

13. In this case, trading in Company X's H shares was suspended at its request pending an announcement relating to the Proposal which it considered to be price sensitive. In the facts and circumstances of the case, the reason for suspension no longer applied upon publication of the Announcement and suspension should be lifted as soon as possible after the Announcement was made.

14. The Exchange had considered Company X's request for a continued suspension of trading in its H shares, but was not satisfied that the additional reasons given by Company X warranted it. Suspension of trading in the H shares to facilitate discussions or determination of the Proposal's final terms was inappropriate as it denied investors reasonable access to the market and prevented its proper functioning.

15. The Exchange did not see any exceptional circumstances or compelling grounds for the continued suspension of trading of Company X's H shares after the publication of the Announcement.

16. The Exchange therefore informed Company X of its decision to direct resumption of trading. Company X was required to publish an announcement notifying the market of the resumption of trading, following the publication of which the Exchange would direct resumption. If Company X failed to make such announcement, the Exchange would direct the resumption of trading following the publication of an announcement by the Exchange.

Conclusion

17. The Exchange informed Company X of its decision to direct resumption of trading of the suspended H shares of Company X. After being informed by the Exchange of its decision to direct resumption of trading in Company X's H shares, Company X requested resumption of trading in its H shares and published an announcement.

Whether the Exchange would allow a listed issuer to resume trading in its shares when it had restored its public float to 15 per cent

Parties

- **Company A** – a Main Board issuer
- **Company B** – Company A's controlling shareholder

Facts

1. Company B made a general offer for Company A's shares under the Takeovers Code after it had acquired a controlling interest in Company A.

2. When the offer closed, the percentage of Company A's shares in public hands fell to 13 per cent. There was a lack of open market for the shares. As a result, trading in the shares was suspended.

3. Company A noted from the Rules that the Exchange will normally require suspension of trading in an issuer's securities when its public float falls below 15 per cent. It asked whether trading in its shares could resume when it had restored the public float to 15 per cent.

Relevant Listing Rules

4. Rule 8.08(1) states that:

   There must be an open market in the securities for which listing is sought. This will normally mean that:

   (a) at least 25 per cent of the issuer's total number of issued shares must at all times be held by the public.

   …

   (Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

5. Rule 13.32 states that:

   (1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …

(3) If the percentage falls below the minimum, the Exchange reserves the right to require suspension of trading in an issuer's securities until appropriate steps have been taken to restore the minimum percentage of securities in public hands. In this connection, the Exchange will normally require suspension of trading in an issuer's securities where the percentage of its public float falls below 15 per cent...

Analysis

6. Rules 8.08 and 13.32 seek to ensure an open market for trading in listed securities and require at least 25 per cent of the securities be held by the public.

7. Therefore, when the issuer's public float falls below 25 per cent, trading will be suspended if it is necessary to avoid a disorderly market. The Exchange will allow resumption of trading when appropriate steps have been taken to restore a 25 per cent public float.

8. The Rules also provide guidance that the Exchange would normally consider a public float of less than 15 per cent be too small to maintain an orderly market and require a suspension of trading in this situation. This does not mean that the Exchange would accept a public float of 15 per cent for resumption of trading.

Conclusion

9. Company A was required to restore its public float to at least 25 per cent before resumption of trading.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether trading in a listed issuer's shares would be suspended due to the delay in publication of its annual results announcement

Parties

- **Company A** – an overseas issuer listed on the Main Board
- **Subsidiary** – a wholly-owned subsidiary of Company A

Facts

1. Company A and its subsidiaries (**Group**) were principally engaged in manufacturing and selling electronic consumer products.

2. In the fourth quarter of the financial year ended 31 December 2006, an agreement was entered into by the Company, the Subsidiary and other parties to restructure the Group's loss-making operations in Europe which were then mainly conducted by the Subsidiary. The restructuring would result in the amicable wind-down of the Subsidiary's operations. Company A made an announcement disclosing details of the restructuring and the expected financial impact on the Group.

3. Rule 13.49(1) required Company A to publish its preliminary results in respect of the financial year ended 31 December 2006 (**Annual Results**) as soon as possible but in any event not later than 4 months after the year end date (i.e. 30 April 2007). Under Rule 13.49(2), the preliminary announcement should be based on Company A's financial statements for the financial year which should have been agreed with the auditors.

4. In April 2007, Company A submitted that it was unable to publish the preliminary announcement under Rules 13.49(1) and (2) due to the delay in finalising the audit of the Subsidiary. It explained that:

    - The Subsidiary's financial statements were prepared using the liquidation basis of accounting.
    - The Subsidiary had been undergoing substantial restructuring involving ceasing most of its operations and laying off most of its employees. The audit of its financial statements had been complicated by the closure of its businesses and the departures of key personnel with knowledge of those businesses.

- The Subsidiary entered into a conciliation process in March 2007 which involved negotiation and settlement of outstanding claims. The outcome could affect its financial position and would need to be accounted for in the 2006 financial year. The Subsidiary's liabilities could not be ascertained and hence its audit could not be finalised pending the outcome of the conciliation process which was expected to conclude in May 2007.

- In view of the uncertainties arising from the conciliation process, Company A's board considered it appropriate to delay the announcement of the audited Annual Results and the despatch of the annual report. It expected that the results announcement and the annual report would be published in the second half of May 2007 and in any event no later than 15 June 2007.

5. Company A would comply with Rule 13.49(3). It would publish an announcement by 30 April 2007 to inform its shareholders of its unaudited Annual Results. These were prepared based on the draft financial statements of the Group which had not taken into account any potential adjustment arising from the conclusion of the conciliation process. They had yet to be agreed with Company A's auditors but had been reviewed by the audit committee which had no disagreement with the accounting treatment adopted. The announcement would also contain a full explanation for Company A's failure to announce its Annual Results according to the Listing Rules and the uncertainty as to any potential adjustments arising from the conciliation process.

Relevant Listing Rules

6. Rule 13.49 provides that:

(1) an issuer shall publish … its preliminary results in respect of each financial year as soon as possible, but in any event not later than the time that is 30 minutes before the earlier of the commencement of the morning trading session or any preopening session on the next business day after approval by or on behalf of the board. The issuer must publish such results:

(i) for annual accounting periods ending before 31 December 31 December 2010 – not later than four months after the end of the financial year; and

…

(2) The preliminary announcement shall be based on the issuer's financial statements for the financial year which shall have been agreed with the auditors.

(3) Where an issuer is unable to make an announcement of its preliminary results based on its financial statements in accordance with rules 13.49(1) and 13.49(2), it must make an announcement:

(A) for annual accounting periods ending before 31 December 2010 – not later than four months after the end of the financial year.

…

The announcement must contain at least the following information:-

(a) a full explanation for its inability to make an announcement based on financial statements which have been agreed with the auditors. Where there are uncertainties arising from the lack of supporting evidence or relating to the valuation of assets of liabilities, sufficient information to allow investors to determine the significance of the assets or liabilities;

(b) the expected date of announcement of the financial results for the financial year which shall have been agreed with the auditors; and

(c) so far as the information is available, results for the financial year based on financial results which have yet to be agreed with the auditors. Where possible, those results must have been reviewed by the issuer's audit committee. In the event that the audit committee disagreed with an accounting treatment which had been adopted or the particulars published in accordance with rule 13.49(3)(i)(a), full details of such disagreement.

…

7. Rule 13.50 provides that:

… the Exchange will normally require suspension of trading in an issuer's securities if an issuer fails to publish periodic financial information in accordance with the Exchange Listing Rules. The suspension will normally remain in force until the issuer publishes an announcement in accordance with rule 2.07C containing the requisite financial information.

Analysis

8. Financial information is essential to enable investors to make informed investment decisions. If an issuer fails to publish its financial information on time, its shareholders and the market do not have the necessary information to appraise its financial position. To protect investors, trading in securities of an issuer that fails to publish its periodic financial information by the due date under the Listing Rules will normally be suspended until publication of that information.

9. The facts of this case indicated that the delay in release of the audited Annual Results was not due to Company A's failure to duly observe the financial reporting requirements. Instead, it was necessary for Company A to take into account any material adjustments to the Annual Results arising from a future event. Company A had also taken appropriate steps to enable its shareholders and the market to have necessary information to appraise its financial position. The Exchange was satisfied that there were exceptional and justifiable circumstances that warranted a departure from the normal operation of Rule 13.50.

Conclusion

10. In light of Company A's proposed actions and the exceptional circumstances of the case, the Exchange would not require suspension of trading in Company A's shares under Rule 13.50.

Trading halt, suspension and resumption

1. Part 9 of the Financial Institutions (Resolution) Ordinance (Cap.628) (FIRO) empowers a resolution authority (being the Monetary Authority, the Securities and Futures Commission or the Insurance Authority) to temporarily defer certain entities' disclosure obligations under section 307B of the SFO in certain circumstances (including that the disclosure would cause or contribute to the non-viability of the entity or its group company or impede the ability of the resolution authority to achieve orderly resolution), and in that case, the entities' disclosure obligations under the Rules will also be deferred automatically.

Where a listed issuer's disclosure obligations are deferred under the FIRO, will dealings in securities of such listed issuer be suspended?

There is no automatic suspension of dealings in securities of such listed issuer, but the FIRO provides that the resolution authority may direct the Exchange to suspend, or not to suspend, dealings in securities of a listed issuer despite its disclosure obligations have been deferred under the FIRO.

According to Part 9 of the FIRO, the resolution authority must consult the SFC (if the SFC is not the resolution authority) before its exercise of any powers to defer disclosure obligations or suspend, or not suspend, dealings to enable the SFC's views to be ascertained (including e.g. on the effects of deferral, suspension or non-suspension on the market, and financial stability).

Any decision to exercise such powers would not be taken lightly by a resolution authority given their potential risks and ramifications for the stability and effective functioning of the financial system. Ultimately, the extent to which the resolution authority would use any of these powers on failure of an institution would depend upon its assessment of the risks posed to the orderly resolution, its balancing of the resolution objectives in the context of securing its financial stability objectives as set out in the FIRO and the operational mechanics (to be developed by the resolution authorities) for the implementation of the FIRO stabilization options.

MB Rule 6.01
GEM Rule 9.01
First released: October 2017; last updated: May 2024

2. An issuer dually listed on the Exchange and an overseas stock exchange has announced the launch of an offering of securities before the market opens in Hong Kong. Can the listed issuer apply for a trading halt on the Exchange to facilitate the bookbuilding and finalise the pricing and allocation of the securities?

No, a trading halt is not justified where inside information (such as an agreement on pricing after the bookbuilding) has not yet crystalised. It is inappropriate for the listed issuer to request for a trading halt to facilitate the offering.

MB Rule 13.10A and HKEX-GL83-15
GEM Rule 17.11A and HKEX-GL83-15
First released: May 2024

Guidance on long suspension and delisting

I. Background and purpose

1. This letter provides guidance to long suspended issuers[1] on the operation of the delisting framework under the Listing Rules (**Rules**), their general obligations and the Exchange's regulatory actions during the resumption process, and guidance specific to certain types of suspension cases.

2. The Exchange closely monitors the delisting process, in particular the circumstances where a remedial period may be specifically imposed and where an extension of time to a remedial period may be allowed, and the guidance given on time periods in this guidance letter. Based on this experience the Exchange may revise its procedures or policies from time to time, with the objectives of ensuring the integrity of the process, providing certainty to the delisting process and keeping trading suspension to a minimum. The Exchange also intends to revisit the duration of the fixed period in due course and may consider shortening these fixed periods at an appropriate time.

3. All Rule references in this letter are to the Main Board Listing Rules. As the relevant requirements under the GEM Board Rules are substantially similar to that of the Main Board, the guidance set out in this letter also applies to GEM issuers.

4. This letter supersedes the previous guidance for long suspended companies set out in Guidance Letter GL66-13.

II. The delisting framework

5. Under Rule 6.01 the Exchange may at any time suspend or cancel the listing of any securities to protect investors or maintain an orderly market. The rule specifies three circumstances under which the Exchange may also do so, comprising where an issuer (a) fails to maintain a sufficient public float; (b) fails to maintain sufficient operations or assets; and (c) is no longer suitable for listing.

6. Under Rule 6.10 which sets out the procedures for delisting an issuer under Rule 6.01, the Exchange may,

   (a) issue a delisting notice specifying a remedial period (**specific remedial period**). If the issuer fails to remedy the issues and resume trading before the end of the remedial period, the Exchange may cancel its listing; or

   (b) delist the issuer immediately.

7. Under Rule 6.01A(1), without prejudice to its rights under Rules 6.01 and 6.10, the Exchange may delist a suspended issuer which fails to remedy the issues causing its suspension of trading and resume trading within 18 months from the date on which the trading suspension begins (**prescribed remedial period**).

[1] Issuers whose securities have been suspended from trading for more than three months

Application of Rule 6.01 or 6.01A(1)

8. The objective of the delisting Rules is to keep the necessary trading suspension to the minimum, by facilitating the timely delisting of issuers that no longer meet the continuing listing criteria. This, in turn, provides certainty to the market on the delisting process. The delisting Rules are also aimed at incentivising suspended issuers to act promptly towards resumption and deterring issuers from committing material breaches of the Rules.

9. Following this principle, where both Rule 6.01A and Rule 6.01 are applicable, the Exchange will exercise its right under Rule 6.01 and impose a specific remedial period under Rule 6.10 ending earlier than the prescribed remedial period if it considers that the issuer:

   (a) given the nature of the issues to be remedied, ought to remedy the issues and resume trading within a period shorter than the prescribed remedial period of 18 months (for example, insufficient public float, see paragraph 56 below); or

   (b) has failed to take adequate action to remedy the issues, prolonging the duration of suspension. For example, the Exchange may impose a specific remedial period of 6 months on an issuer which does not take adequate action to remedy the matters rendering it no longer suitable for listing, as with the decision in Listing Decision LD114-2017.

10. The Exchange may delist an issuer immediately under Rule 6.01 only in exceptional circumstances where the matters triggering the application of a delisting criterion are fundamental to the general principles for listing and are beyond remedy. This may happen, for example, where an issuer becomes no longer suitable for listing after its management and controlling shareholder are found by a court to have operated a fraudulent scheme to overstate its business and profits.

III. General obligations of suspended issuers and the Exchange's regulatory actions

11. Under the Rules, a suspended issuer must, among others,

   (a) keep the duration of any trading suspension to the shortest possible period as required under Rule 6.05;

   (b) comply with its continuing obligations under the Rules at all times, for example, those applying to notifiable and/or connected transactions under Chapters 14 and 14A of the Rules and financial results and reports under Rules 13.46 to 13.49;

   (c) disclose inside information required to be disclosed under the Inside Information Provisions[2]; and

   (d) announce quarterly updates under Rule 13.24A on its business operations, resumption plan and timetable, and the progress of implementing such resumption plan and satisfying the resumption conditions/guidance given by the Exchange (including the reasons for and impact of delay, if any).

[2] Part XIVA of the Securities and Futures Ordinance

12. **Under the Rules, the Exchange will cancel the listing of a long suspended issuer upon the expiry of the remedial period (prescribed or specific) if the issuer has not remedied the issues causing the suspension and re-complied with the Rules. This remedial period sets a deadline referenced to the resolution of the relevant issues and resumption of trading, as opposed to submission of a resumption proposal.**

13. Accordingly, the issuer must devise its own resumption plan setting out the actions that it considers appropriate to remedy the issues, announce such resumption plan, work according to that plan, and announce regular updates on its resumption progress and business developments. Based on these announcements, the Exchange will monitor the issuer's resumption status and, where appropriate, give guidance to the issuer. While the Exchange may give guidance to assist the issuer, it is the issuer's primary responsibility to devise its own resumption plan in order to ensure that it will remedy the relevant issues and re-comply with the Rules before the end of the remedial period to avoid delisting. The issuer may also consult[3] the Exchange at any stage. When the issuer considers that it has remedied the issues and re-complied with the Rules, it must then seek a confirmation from the Exchange that this is the case. Trading will resume after the Exchange gives the confirmation.

14. In light of the above, the steps that a suspended issuer should take include:

    (a) promptly after trading is suspended, review the matter giving rise to the suspension and identify the relevant issues;

    (b) devise a resumption plan with actions that it intends to take to remedy the issues and re-comply with the Rules. The resumption plan should be accompanied with a clear timeframe in respect of each stage of work under the plan to ensure that the relevant issues can be remedied and the Rules can be re-complied with as soon as practicable and, in any event, before the remedial period ends. The timeframe should take into account not only the time required by it to implement the resumption plan, but the time that may be reasonably required by the Exchange to be satisfied that the issues have been remedied and the Rules re-complied;

    (c) work diligently towards resumption in accordance with the resumption plan. In case of any delay, it should promptly assess its impact and make appropriate adjustments to the timetable but, in any event, continue to ensure trading to resume before the remedial period ends;

    (d) timely announcement of the resumption plan and its timetable, any material change in the plan and timetable, and any material developments to the fulfillment of the resumption conditions/guidance (for example, the outcome of any forensic investigation or internal control review);

    (e) where applicable, make announcements about corporate actions under its resumption plan described above in accordance with the requirements set out in the Rules (for example, an announcement on a very substantial acquisition or a reverse takeover);

[3] Please refer to the Guide on Interpretation on Listing Rules and Request for Individual Guidance.

(f) announce quarterly updates under Rule 13.24A on its business operations and the progress of implementing its resumption plan and satisfying the resumption conditions/guidance given by the Exchange (including the reasons for and impact of delay, if any). These disclosures would provide transparency to the market and enable the Exchange to monitor its resumption progress and, where appropriate, give guidance to the issuer;

(g) publish its periodic financial results and reports and, if they are not available, management accounts under Rules 13.46 to 13.49;

(h) maintain adequate internal controls and procedures to ensure full compliance with its continuing obligations under the Rules and the disclosure requirements under the Inside Information Provisions at all times; and

(i) where it considers that it has remedied the issues and re-complied with the Rules, seek the Exchange's confirmation that this is the case. It must ensure that it provides the Exchange with sufficient information to properly assess the situation, avoiding the risk of the Exchange not being satisfied with the issuer's position for lack of information. When seeking the Exchange's confirmation, the issuer should also provide the Exchange with a draft resumption announcement for pre-vetting.

15. Trading can resume only after the Exchange has confirmed that the issuer has remedied the issues and re-complied with the Rules to its satisfaction. Before such confirmation is given, the issuer must state in each of its announcements that trading will remain suspended with an explanation of the reasons for the continued suspension.

The Exchange's regulatory actions

16. During a suspended issuer's remedial period, the Exchange will:

(a) issue resumption conditions/guidance to the issuer, setting out the requirements that the issuer must fulfill before trading can resume. These conditions/guidance are primarily based on the issuer's announcement(s) about the matter giving rise to the suspension and the issues identified by the issuer, and are generally issued within the first three months of the suspension of trading. The Exchange may revise these resumption conditions/guidance from time to time as the issuer's circumstances change (for example, a suspended issuer subsequently found to be involved in fraudulent activities will be required to conduct a forensic investigation). For the avoidance of doubt, the issuer must comply with all the Rules before resumption. The resumption conditions/guidance are set out, based on information provided by the issuer from time to time, to guide the issuer toward re-compliance with the Rules. As such, the issuer is not entitled to an extension of the remedial period in cases where the Exchange modifies or adds resumption conditions/guidance;

(b) review the issuer's quarterly announcements published under Rule 13.24A and other announcements to monitor its on-going compliance with the Rules and resumption progress. Where appropriate, the Exchange may make enquiries and require the issuer to publish supplemental announcements to disclose additional information or clarification, or give guidance to the issuer. The Exchange may also request the issuer to provide any documents relevant to the matters mentioned in an announcement (for example, a report of forensic investigation or internal control review) for review;

(c) give guidance sought by the issuer from time to time;

(d) pre-vet the issuer's announcements under Rule 13.52(2) including, for example, an announcement for any very substantial acquisition or reverse takeover (and any other announcements that the Exchange has requested to pre-vet under Rule 13.52A) and the circulars as required under the Rules, in the same manner as it does for other listed issuers;

(e) process the issuer's A1 applications where the resumption plan is treated as a new listing application;

(f) publish monthly long suspension reports on the HKEXnews website which summarise the suspension status of issuers suspended for three months or more; and

(g) upon the issuer's request (as noted in paragraph 14(i) above), confirm whether it is satisfied that the issuer has remedied the issues and re-complied with the Rules to meet the resumption conditions/guidance.

17. The Exchange will respond to a suspended issuer's request for confirmation about its resumption status (as described in paragraph 16(g) above) or guidance as soon as practicable, and generally not more than 10 business days after receipt of the issuer's written request and the relevant information.

18. Under the Rules, the Listing Committee reserves to itself the power to decide whether to delist an issuer[4]. Therefore, if the Listing Division is not satisfied with the issuer's resolution of the relevant issues and re-compliance with the Rules within the remedial period, it will take the matter to the Listing Committee for consideration and recommend the Listing Committee to delist the issuer.

19. The Listing Committee regulates its meeting(s) in such manner as it thinks fit[5]. The Rules do not mandate the Listing Committee's decision-making process to be subject to a right of the issuer to make submissions. Generally, the Listing Committee will consider and decide the matter administratively, without conducting an adversarial hearing.

20. The issuer will be informed of the Listing Committee's decision (together with the reasons thereof) by a decision letter. The issuer will then be entitled under the Rules to apply for a review of the decision by the Listing Review Committee[6] in accordance with the review procedure under the Rules[7].

21. The review is a de novo review on the merits so that the Listing Review Committee will consider the issuer's case and decide it afresh, after considering all the relevant evidence and arguments[8]. The Listing Review Committee will convene an oral hearing. The issuer may make written submissions and also attend the hearing to provide oral submissions to the Listing Review Committee in accordance with the procedures adopted by the Listing Review Committee.

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4 Rule 2A.08
5 Rules 2A.28 and 2.04
6 In Brightoil Petroleum (Holdings) Limited [2020] HKCFI 1601, the court endorsed the approach adopted by the Listing Committee set out in paragraphs 18 to 20 in this Guidance Letter and considered that such approach strikes a fair balance between administrative efficiency and fairness.
7 Rule 2A.37K
8 Rule 2A.37L

IV. Extension of remedial period

22. To ensure the effectiveness and credibility of the delisting framework and prevent undue delay of the delisting process, the Listing Committee may only extend the remedial period in exceptional circumstances. It may do so where:

    (a) an issuer has substantially implemented the steps that, it has shown with sufficient certainty, will lead to resumption of trading; but

    (b) due to factors outside its control, it becomes unable to meet its planned timeframe and requires a short extension of time to finalise the matters. The factors outside the issuer's control are generally expected to be procedural in nature only.[9]

    This may happen where, for example, an A1 application has been approved by the Exchange but, due to a delay in the court hearing for approving a scheme of arrangement, the issuer requires additional time to implement the relevant transactions. The Exchange envisages that if an extension of time is given on the expiry of the remedial period, the Listing Committee would not normally extend the remedial period for a second time.

23. The Exchange recognises that in assessing whether exceptional circumstances exist to warrant a time extension, it is not restricted to the description stated in paragraph 22 above[10]. That said, given the overriding objective of the delisting Rules, the Exchange envisages that situations in which the Listing Committee may consider it appropriate to exercise its discretion to extend the remedial period (other than those set out in paragraph 22 above) are rare. In particular, even if an issuer can demonstrate that its ability to remedy the issues causing the suspension and re-comply with the Rules within the remedial period has been inhibited by factors outside its control, the Listing Committee is not obliged to consider such situation exceptional. The Listing Committee will still consider the specific facts of the issuer's case in deciding whether to extend the remedial period. The factors that the Listing Committee will consider include, among others:

    (a) whether the issuer has taken adequate action and acted promptly throughout the remedial period to take steps for achieving compliance with all the resumption conditions/guidance and the Listing Rules (in particular for such conditions for which the issuer's ability to take steps for compliance has not been inhibited by factors outside the issuer's control); and

    (b) whether there is sufficient certainty that the issuer will be able to comply with all the resumption conditions/guidance and the Listing Rules within the requested time extension.

    In addition, any time extension, if given, should be short as envisaged in paragraph 22 above.

V. Guidance for issuers suspended for various reasons

24. Below sets out guidance specific to certain types of suspension cases.

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[9] For circumstances regarding a disclaimer or adverse opinion involving issues outside the issuers' control, see paragraph 48 below.

[10] As noted in the judgment of China Wood Optimization (Holding) Limited and The Stock Exchange of Hong Kong Limited *[2023] HKCFI 1000, dated 4 May 2023*

A. Failure to maintain sufficient operations or assets under Rule 13.24

25. In our experience, an issuer suspended for failure to comply with Rule 13.24 may have either (i) completely or substantially ceased its operations or otherwise maintained only a minimal level of operations; or (ii) suspended all or most of its operations due to financial difficulties or loss of its major operating subsidiary/ies. Trading will resume after it has re-complied with Rule 13.24.

26. The Exchange will normally apply the prescribed remedial period of 18 months under Rule 6.01A(1) to issuers that fail to maintain sufficient operations and sufficient assets to support its operations to warrant a continued listing under Rule 13.24.

27. To re-comply with Rule 13.24, an issuer must demonstrate to the Exchange's satisfaction that it has a business that has substance and is viable and sustainable in the longer term. On this issue, the Exchange has published guidance materials on the application of the Rules to individual circumstances. Such guidance includes:

    (a) In a case where an issuer ceased to carry on its original principal business and retain any material operating assets, the Exchange found that the issuer was a listed shell and any acquisition of a material asset or business would constitute an attempt to achieve the listing of the asset or business and be treated as a new listing application. See Guidance Letter on Application of the Reverse Takeover Rules (GL104-19).

    (b) In a case where an issuer started a business substantially different from or unrelated to its original business, the Exchange found that this new business did not meet the requirements under Rule 13.24 because given its short operating history, the viability and sustainability of the new business was not substantiated by any track record or otherwise. The Exchange may also consider a new business not to be a business of substance, having regard to its specific business model and the particular facts and circumstances of the issuer. For further guidance, see Guidance Letter on Sufficiency of Operations (GL106-19).

    (c) Where an issuer proposes a large scale issue of securities to an investor for cash to finance the development of a new business, the Exchange may apply Rule 14.06D and refuse to grant listing approval for the shares to be issued, particularly if the cash injection (i) is very significant to the issuer and has little correlation with its existing business, (ii) would raise funds largely for greenfield operations of the new business; and (iii) would result in the investor obtaining control (or de facto control) of the issuer. In these circumstances, the Exchange may consider the issuer to be in effect a listed vehicle for the investor to achieve a listing of the new business and to circumvent the new listing requirements. For further guidance, see Guidance Letter on Large Scale Issues of Securities (GL105-19).

Process for resumption

28. Where an issuer's resumption plan involves an acquisition of a business, it must make an announcement and comply with the applicable requirements under Chapters 14 and/or 14A of the Listing Rules. If the acquisition constitutes a very substantial acquisition or a reverse takeover, the announcement must be pre-vetted by the Exchange before publication.

29. The issuer may consult the Exchange at any stage about the Rule implications on an intended acquisition, for example, whether the acquisition would constitute a reverse takeover and, if so, whether the Exchange, subject to a formal A1 application, has any initial concerns about its compliance with the new listing requirements.

30. Where an acquisition constitutes a reverse takeover, the issuer must file an A1 application to the Exchange with the required documentation. As the issuer must obtain the Exchange's approval for the application and complete the implementation of the relevant transactions and arrangements in time to ensure trading to resume before the remedial period ends, the issuer is advised to file its A1 application as soon as practicable, taking into account the time that may be required, among others, by:

    (a) the Exchange to process the A1 application. Under Rule 9.03(3), the information submitted to the Exchange in support of a new listing application must be substantially complete except in relation to information that by its nature can only be finalised and incorporated at a later date. In our experience, the Exchange's processing time could be prolonged by the substandard documentation provided by the issuer; and

    (b) the issuer to implement the relevant transactions and arrangements after the Exchange gives an in-principle approval for the A1 application. This may include, for example, the time for obtaining shareholder approval and/or going through the court procedures for a scheme of arrangement, if required.

    As guidance, an issuer should generally allow at least a 6 month period from the date of the filing of an A1 application to the date of resumption for the processing of the application, obtaining any required shareholder approval and completing the relevant transactions. It should consider its own circumstances and adjust the time period accordingly.

31. Where, without being required to submit a new listing application, an issuer considers that its business operations have re-complied with Rule 13.24, it must demonstrate to the Exchange's satisfaction that its business is one of substance and is viable and sustainable in a longer term. For this purpose, the issuer must ensure that it announces quarterly updates on its resumption progress under Rule 13.24A (for example, in the case of loss of a major subsidiary, updates on the progress of regaining control of the subsidiary). The issuer must also announce its financial results and reports under Rules 13.46 to 13.49 to demonstrate its financial performance and position. The Exchange's assessment of the issuer's re-compliance with Rule 13.24 is a continuing process, based primarily on these disclosures. The issuer should be prepared to provide additional information to the Exchange to support its compliance, for example, a profit forecast to demonstrate that it has a viable and sustainable business.

32. Where an issuer's failure to meet Rule 13.24 is caused by financial difficulties, the issuer is required to announce the corporate actions that it takes to resolve the financial difficulties. Such corporate actions generally involve a capital reorganisation, equity fundraising(s) and a scheme of arrangement. The issuer must announce these corporate actions in a timely manner. To demonstrate its re-compliance with Rule 13.24, the issuer must set out in the relevant circular (or, if a circular is not required under the Rules, an announcement) information to support the viability and sustainability of the restructured group's business. Such information may include, for example, pro forma financial statements about its restructured group, a detailed description of the business model of the restructured business, a clear and detailed plan for its future developments and how the issuer would achieve it, and the restructured group's profit forecast. The Exchange may give guidance to the issuer on the viability of the corporate actions for resumption based on the disclosures, and may make enquiries for additional information (such as profits forecasts).

33. Where an issuer's corporate actions include any equity fundraising(s), the Exchange would consider granting the required listing approval only if the issuer satisfies the Exchange that upon completion of the equity fundraising(s), the issuer will then have fulfilled all the resumption conditions/guidance, re-complied with the Listing Rules, and be eligible for trading resumption. Therefore, the Exchange will not grant listing approval to a suspended issuer which has not demonstrated that taking into account the equity fundraising(s), it would have sufficient operations and assets to warrant its continued listing under Rule 13.24.

Others

34. Where an issuer fails to publish periodic financial results as required under the Rules, the Exchange is unable to monitor the issuer's business activities, operation status and financial performance to assess whether the issuer has sufficient operations and assets under Rule 13.24 to warrant its continuing listing. In these circumstances, as resumption conditions/guidance, the Exchange would require the issuer to demonstrate compliance with Rule 13.24 before trading can resume. As noted in paragraph 12 above, a suspended issuer must comply with the Rules before the remedial period ends to avoid delisting.

B. Failure to publish financial results or inside information due to material irregularities

35. Trading will be suspended if an issuer fails to announce periodic financial results or inside information, due to alleged material accounting or corporate governance irregularities or significant weaknesses in internal controls. The suspension will remain in force until the relevant issues are addressed or remedied and the outstanding financial results and/or inside information announced.

36. Irregularities that may result in an issuer's failure to announce financial results or inside information include, among others, the following:

(a) Accounting irregularities identified by the issuer's auditors during the auditing process. The auditors may have disclaimed the issuer's accounts (or resigned before the accounts are published) for the issuer's inability to explain or provide sufficient evidence to address the material issues to the auditors' satisfaction. These issues may include, among others:

- discrepancies between the group's accounting records on transactions and balances with certain customers and/or suppliers and the information independently obtained by the auditors;
- concern about the authenticity of documents in the group's accounting records on bank balances;
- lack of information and evidence to substantiate the existence or ownership of material assets;
- concern about the nature and commercial substance of some material transactions; and/or
- failure to keep proper books and records for the group (for example, due to loss of accounting records of a major subsidiary during relocation of office).

(b) Corporate irregularities which may be discovered by the board of directors (sometimes with forensic investigators' assistance), the issuer's auditors, media, market commentaries or rumours or investigations undertaken by the Securities and Futures Commission (**SFC**), the ICAC or other regulators. These irregularities may include potentially fraudulent activities such as misappropriation of corporate assets through an unauthorised transfer of material assets or provision of loans or guarantees to third parties.

37. These irregularities could give rise to serious issues about the accuracy and credibility of the issuer's published financial statements or records in material respects, the integrity of its management and the lack of adequate internal controls or procedures over its financial, operations and compliance matters to safeguard its assets and protect shareholders' interests. These issues are detrimental to maintaining confidence in the market and are not in the interest of the investing public. This, in turn, would call the issuer's suitability for continued listing into question. See Listing Decision LD114-2017.

(I) Criteria for resumption

38. Before trading can resume, the issuer must satisfy the Exchange that it has addressed or remedied all the material issues as follows:

(a) Address any audit issues raised by the auditors.

(b) Address any other allegations or findings of material irregularities raised by forensic investigators, media, market commentaries or rumours, or regulators.

(c) Rectify any material misstatements or errors in its financial statements and publish information that is accurate and not misleading, to enable the investing public to appraise its position.

(d) Publish any outstanding financial statements and address any audit modifications.

(e) If there are issues about management integrity, demonstrate that there is no reasonable regulatory concern about management integrity which may pose a risk to shareholders and investors or damage market confidence (for example, making necessary changes to the board of directors to ensure compliance with Rules 3.08 and 3.09).

(f) If there are issues about material weaknesses in internal control systems, demonstrate adequate internal controls and procedures to rectify such weaknesses, ensure compliance with the Listing Rules and safeguard the interests of the issuer.

(g) Announce all inside information required to be disclosed under the Inside Information Provisions and inform the market of all other material information for the issuer's shareholders and investors to appraise its position.

(II) Process for resumption

39. Once trading is suspended, an issuer should promptly review the matter, identify the relevant issues and devise a plan to address the relevant issues and re-comply with the Rules, taking account of the resumption condition/guidance and any other guidance that may from time to time given by the Exchange.

40. The steps that an issuer is expected to take include:

    (a) If any director is, or is suspected to be, involved in the issues, consider setting up an independent committee to review the matter. This is to avoid any conflict of interests which may arise during the review process. The independent committee should also assess whether the director in question can discharge his director's duties and comply with Rule 3.08 and remains suitable to act as a director of the issuer under Rule 3.09, while the internal investigation/review process (or any regulatory investigation) continues.

    (b) If the matter involves or indicates potentially fraudulent activities (such as false accounting or misappropriation of assets), engage forensic accountants to investigate the matter. The forensic accountants to be engaged should have sufficient resources and professional staff with relevant qualifications and experiences in handling cases of similar nature and complexity.

        The board or independent committee should review the findings of the forensic investigation once available, and consider whether the findings have adequately addressed the relevant issues and, if not, what further actions should be taken (e.g. extending the scope of the investigation or conducting an internal control review if any potential internal control failure is identified).

    (c) If the matter raises concerns about the adequacy of the internal control system, engage independent experts to review the internal control system and to identify material weaknesses with remedial actions. Such concerns may arise, for example, where the issuer has failed to (i) provide sufficient evidence to support the completeness and accuracy of its financial statements in material respects, leading to a disclaimer audit opinion, (ii) prevent or detect corporate misconduct such as misappropriation of assets or funds, or (iii) disclose material information to shareholders and potential investors in a timely manner.

        Again, the board or independent committee should review the findings of the internal control review once available and determine whether and, if so, what remedial actions should be taken to ensure that adequate internal controls and procedures are in place to rectify such weakness, ensure compliance with the Listing Rules and safeguard the interests of the issuer.

    (d) If the issuer fails to publish financial results due to unresolved audit issues, consider with the auditors as to how to resolve the audit issues. If the auditors have resigned, the issuer should appoint a replacement promptly.

41. The issuer must continue to publish its periodic financial results and reports under Rules 13.46 to 13.49 (see paragraph 11(b) above). Where an issuer is unable to do so, it must publish its management accounts and unaudited financial results.

42. The issuer must keep the market updated by publishing quarterly announcements as required under Rule 13.24A. The Exchange assessment's of the issuer's resumption progress is also a continuing process, primarily based on these announcements and additional information that may be provided by the issuer to the Exchange. In particular,

(a) where a report of a forensic investigation or internal control review is available, the issuer must announce the findings of the report together with the view of the board or independent committee on the report and any plan for further actions. The Exchange will review the announcement and request the issuer to provide it with a copy of the report (if not already provided). The Exchange may provide guidance to the issuer on concerns or issues that may arise from the report, the views of the board or independent committee and/or the remedial actions to be taken by the issuer (for example, any outstanding or further issues that require further investigation, or adequacy of the remedial action).

(b) Where the issuer has failed to publish financial results/reports, it must announce all the outstanding results and reports with any audit modifications addressed. If the Exchange considers that there are any issues that the issuer and/or the auditors should clarify, the Exchange will inform the issuer.

43. To minimise the risk of delisting as a result of not being able to complete a forensic investigation (and/or an internal control review) or implement all the remedial measures, a suspended issuer must properly devise its action plan with a detailed timeframe taking into account the time that may be required by the relevant process (including, among others, the time may be required by Exchange to be satisfied that the relevant issues have been remedied).

44. Where the issuer considers that it has, or will have after completion of certain transactions or arrangements, remedied the issues and re-complied with the Rules, it should seek a confirmation from the Exchange. For this purpose, the issuer must make a written submission and provide the Exchange with all the relevant information. Also see paragraphs 14(i), 16(g) and 17 above.

C. Disclaimer and adverse audit opinion on financial statements

45. Under Rule 13.50A, trading will normally be suspended if an issuer publishes a preliminary results announcement for a financial year as required under Rules 13.49(1) and (2) and the auditor has issued, or has indicated that it will issue, a disclaimer of opinion or an adverse opinion on the issuer's financial statements.

46. The suspension will normally remain in force until the issuer has addressed the issues giving rise to the disclaimer or adverse opinion, provided comfort that a disclaimer or adverse opinion in respect of such issues would no longer be required, and disclosed sufficient information to enable investors to make an informed assessment of its financial positions.

47. Examples on how an issuer could provide comfort that a disclaimer or adverse opinion in respect of such issues would no longer be required include (a) a full financial year audit or a special interim audit of the issuer's financial statements; or (b) a special engagement of the auditor to perform an audit on a single financial statement of the issuer or a specific element, account or item of a financial statement under HKSA805 (Revised). These are only examples to provide guidance on the possible actions that an issuer may take, having communicated with its auditors, and must be considered case by case to fit the particular circumstances. It is the issuer, and not the auditor, which is responsible for providing comfort that a disclaimer or adverse opinion would no longer be required. The issuer should take all necessary actions to support the provision of such comfort.

Remedial period for circumstances outside issuer's control

48. Disclaimer or adverse opinions may involve issues outside the issuers' control. Where an issuer suspended under Rule 13.50A has satisfied the Exchange that it has made all reasonable efforts to resolve the issues but, due to reasons outside its control, such underlying issues remain unresolved upon expiry of the 18 month period, the Exchange would consider allowing a longer remedial period, with the duration of the period to be determined case by case. The issuer must demonstrate to the Exchange's satisfaction that it reasonably expects to resolve all underlying audit issues within the proposed extended remedial period. Such extension would be brought to the Listing Committee for consideration. The Listing Committee would not normally allow a further extension of the remedial period. Accordingly, issuers are reminded to provide sufficient information to the Exchange to make an informed assessment on the circumstances.

49. Examples of circumstances that may be considered to be outside the issuer's control include (i) delay in a government granting a requisite approval due to change in government policies, where due applications and filings had been made by the issuer, and where it has no influence on the outcome and timing of the grant; (ii) a temporary suspension of business upon the request of a regulatory or government authority due to a change in the regulatory requirements; and (iii) the audit issue can only be fully resolved upon a court order or a final arbitral awards with respect to outstanding proceedings is obtained or granted.

50. Circumstances that would be considered to be within the issuer's control include circumstances where actions that can be taken by issuers or can be pre-empted by proper internal controls or risk management controls. For example, the issues remain unresolved because the issuer has failed to obtain an independent valuation to support the valuation of its assets or take actions against its debtors to assess the recoverability of bad debts in a timely manner. Circumstances would also not be considered to be outside the issuer's control where the disclaimer or adverse opinion is attributed to the issuer's lack of adequate internal controls or risk management controls. These may include, for example, the issuer's failure to put in place adequate measures to control and manage its jointly-controlled entities or associates or keep the books and records of its subsidiaries.

51. An issuer should consult the Exchange in advance if it is in doubt as to whether its specific circumstances leading to a disclaimer or adverse audit opinion on its financial statements would be considered to be outside its control. Such issuer must provide sufficient information to the Exchange to make an informed assessment of the circumstances.

D. Insufficient public float

52. Where trading is suspended due to insufficient public float, the Exchange will expect the issuer to address the matter within a reasonably short period of time.

53. For this purpose, the board of the issuer should, promptly after the public float shortfall occurs, devise and announce a concrete and viable action plan to restore the required minimum public float (for example, placing of existing shares by the controlling or substantial shareholder(s), or placing of new shares by the issuer). The action plan should include a clear timeframe in respect of each stage of work under the plan to demonstrate and ensure that the required minimum public float will be restored and trading will resume within a reasonable period of time. The Exchange may give guidance on the adequacy of the plan and comments on the timeframe, where appropriate.

54. Based on experience, prolonged suspensions due to insufficient public float are mostly caused by major shareholders' refusal to cooperate with the management of the issuer to resolve the issue. As the Exchange generally expects issuers suspended due to insufficient public float to resolve the issue within a reasonably short period of time, an issuer's inability to obtain cooperation from major shareholders would not be considered a valid ground for the Exchange to refrain from delisting the issuer if it fails to restore sufficient public float within the remedial period.

55. Where the Exchange considers that an issuer fails to take adequate action to restore the minimum public float, it may impose on it a specific remedial period of not more than 6 months under Rule 6.01.

56. During the suspension of trading, the issuer must announce any material developments and progress of its action plan from time to time and at least quarterly as required under Rule 13.24A. In applying for resumption of trading, the issuer must announce completion of any relevant transactions and arrangements resulting in the issuer restoring its public float and seek confirmation from the Exchange that trading can resume.

VI. Issuers directed to be suspended by SFC

57. The SFC has the power to direct the Exchange to suspend trading in an issuer's securities under Rule 8 of the Securities and Futures (Stock Market Listing) Rules (**Rule 8 suspension**), whether or not trading is already suspended under the Rules.

58. For an issuer that is suspended under the Rules (for example, for failure to publish financial results or inside information, or to maintain sufficient operations or assets), the Exchange may commence or continue the procedures to delist the issuer under Rule 6.01 or 6.01A even if the SFC has issued a Rule 8 suspension. Where an issuer's trading suspension is attributed only to a Rule 8 suspension, the Exchange may still delist the issuer if the issuer fails to resume trading after a continuous trading suspension for a prescribed remedial period under Rule 6.10A.

59. The Exchange would discuss with the SFC before exercising its right to delist an issuer which is subject to a Rule 8 suspension.

HKEX Guidance Letter
HKEX-GL120-24

November 2024

Guidance on investigations conducted by long suspended issuers

I. Introduction

1. Trading in an issuer's shares will be suspended if it fails to publish financial results or inside information due to unaddressed allegations of material accounting or corporate irregularities (collectively, **irregularities**). The issuer is normally required as resumption conditions/guidance to, among others, conduct an independent investigation into the irregularities, announce the findings and take remedial action.[1] Based on our observations from past cases, we set out below guidance on what the Exchange expects from directors when they procure a suspended issuer to meet such resumption conditions/guidance.

2. This guidance is not intended to be an exhaustive list of directors' obligations or responsibilities in these circumstances. Directors should apply due skill, care and diligence based on the specific circumstances of each case and take prompt and adequate action in the resumption process, with the aim that the issuer can resume trading as soon as practicable,[2] and in any event within the remedial period to maintain its listing status.

3. Among other factors, the Listing Committee and, insofar as an issuer applies for a review of the Listing Committee's delisting decision, the Listing Review Committee will consider the matters stated in this guidance letter and the Guidance Letter on long suspension and delisting (GL95-18) as they think appropriate when determining whether an issuer has complied with the relevant resumption conditions/guidance and the merits of an application for extending the remedial period.

II. Objective of Investigation

4. For trading in its shares to be allowed to resume, a suspended issuer is required to conduct a thorough and comprehensive independent investigation which enables it to achieve the following:

   (a) ascertain whether the alleged irregularities in fact occurred, and if so, details of such irregularities;

   (b) identify the issues having arisen from the irregularities (including the root cause(s) of the irregularities);

   (c) assess the impact of the irregularities and the issues referred to above;

   (d) formulate and implement remedial action; and

   (e) announce the information necessary for its shareholders and other investors to make an informed assessment of the issuer.

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[1] Rule references in this letter are to the Main Board Rules. The guidance in this letter applies equally to GEM issuers.
[2] Under Rule 6.05, a suspended issuer must keep the duration of any trading suspension to the shortest possible period.

5. For this purpose, an investigation should aim to find out, among others:

   (a) the details of the irregularities and the events leading to their occurrence with:

      (i) the sequence and timing of the events;

      (ii) the identities of the persons and entities involved in or being aware of such events and irregularities at the material time, and the extent of such involvement and awareness; and

      (iii) the background of such persons and entities, and their relationship or connection with the issuer or its connected person(s), whether business or otherwise.

      Such persons and entities may include (i) the relevant directors and other management staff of the issuer, and (ii) the other involved parties which may include, for example, any counterparties of the relevant transactions or arrangements, and the beneficiaries of the irregularities.

      For any director or other management staff of the issuer found to be aware of the irregularities, the investigation should find out (i) whether he/she had taken action after becoming aware of the irregularities and, if so, (ii) the details of, and the reason for, such action. If no subsequent action was taken, the investigation should find out the reason for his/her inaction;

   (b) the purpose or rationale for which the irregular acts were conducted, which may require a critical assessment of the credibility and reasonableness of the explanation given by each of the persons involved in light of other relevant evidence;[3] and

   (c) the outcome of such irregular acts, including any material impact on the issuer, financially or otherwise.

6. Additional irregularities may be identified during an investigation. For instance, when investigating a specific unauthorised loan, an examination of the issuer's books and records or an interview with a witness may uncover evidence of (i) other unauthorised loans or irregularities, and/or (ii) the involvement of other persons or entities in or their awareness of the irregularities at the material time.

7. In such an event, the issuer should give timely consideration to extending the scope of investigation to cover the additional irregularities and/or the additional persons or entities identified, so that the investigation can be thoroughly and comprehensively conducted.

8. The investigation findings should help to identify the issues that must be addressed before trading resumption. Such issues may include, for example, (i) audit issues to be resolved before financial results can be published or a disclaimer of opinion addressed, (ii) concerns about the integrity, character and competence of the issuer's directors and other persons with substantial influence over the issuer's business and affairs,[4] (iii) material internal control deficiencies, and (iv) other Listing Rule non-compliance. This, in turn, helps determine the remedial action that must be taken and material information that must be announced by the issuer before trading can resume.

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3 Also see paragraphs 37 to 40 of this guidance letter.
4 See also Guidance Letter on Listed Issuer's Suitability for Continued Listing (GL96-18), paragraphs 16 to 17.

III. The Exchange's expectations of directors

(A) Cooperation of directors

9. All directors are expected to provide full cooperation in the investigation. As elaborated below, while an independent committee is tasked with the primary responsibility to conduct the investigation, directors (whether he/she is a member of the independent committee) should procure the issuer and its personnel to provide the independent committee with necessary resources and assistance and facilitate the investigation. In addition, except for those implicated or conflicted, they should understand the causes of the irregularities and evaluate the advice and opinions of the independent committee and the investigator when deciding and implementing remedial action(s).

(B) Preservation of evidence and provision of assistance in the investigation

10. For an investigation to be conducted on a timely and proper basis, it is imperative that all potentially relevant evidence[5] is preserved and is readily accessible to the investigator. Otherwise, the integrity of the evidence collected through the investigation and the credibility of the investigation may be undermined.

11. Therefore, upon becoming aware that a material irregularity might have occurred, the directors should promptly identify what the issues are and where potentially relevant evidence may be kept. They are then expected to take adequate steps to preserve such evidence.[6]

12. In particular, directors should make prompt and specific arrangements to prevent any potentially relevant evidence from being tampered with or lost.

13. For example, to protect the integrity of potentially relevant information which might be stored on electronic devices, directors should take prompt and adequate measures to prevent the device from being further used or reformatted. As an additional precautionary measure, they should also consider arranging for all the data stored on the device to be imaged and for the safekeeping of the imaged data.

14. In addition, to facilitate the investigator to collect evidence, directors should allow the investigator to have all reasonable access to the electronic devices, documents, records and data, etc that may contain potentially relevant evidence. In addition, they should make themselves available to meet the investigator and provide him/her with such information as he/she may reasonably request.[7] They should also assist the investigator to contact and make enquiries of other relevant personnel directly.

15. Evidence may be lost after the departure of employees or the disposal of subsidiaries. Directors are particularly reminded of the following:

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5 Including emails and other types of correspondence, minutes of meetings, other types of documents and records, and data on electronic devices, etc.

6 This is on top of their general obligation to procure the issuer to maintain proper books and records at all times.

7 There were cases where directors of the issuer of a transaction declined the investigator's requests for interview or information. This prevented the investigator from ascertaining the facts relevant to the irregularities and the extent of the directors' involvement or knowledge. As a result, the issuers were unable to properly investigate the irregularities and demonstrate the integrity of the issuer's management as required under our resumption conditions/guidance.

(a) when an employee who is likely to possess relevant evidence is leaving the issuer, directors should ensure the timely return by the employee of all the issuer-owned assets and properties (such as electronic devices, books and records) to the issuer. Directors should procure the leaving employee, before his/her departure, to meet and provide information to the investigator, if engaged. Directors should also obtain the leaving employee's contact details so that he/she will remain contactable by the investigator after his/her departure. If possible, directors should obtain a commitment or an understanding from the employee that he/she will, after leaving the issuer, provide (or continue to provide) information to the investigator as it may reasonably request; and

(b) before an issuer disposes of a subsidiary which is likely to possess relevant evidence, the directors should put in place adequate arrangements (for example, obtaining the buyer's agreement) to ensure that the issuer and the investigator will remain able to access the relevant information after the disposal.

16. Third parties involved in the events relevant to the irregularities (such as the issuer's controlling or substantial shareholder, banker, customer or supplier) may possess potentially relevant evidence. Directors are expected to assist the investigator in contacting these parties to obtain information from them directly.

17. Apart from the above, directors should ensure that the issuer deploys, or provides the investigator with, adequate resources including financial, technological, and human resources to facilitate the investigation.

(C) Independence of investigation

18. The investigation should be independently conducted. This helps avoid actual and potential conflicts of interest and maintain the impartiality and objectivity of the investigation, in turn enhancing the credibility of the investigation findings.

19. Therefore, the issuer should promptly set up an independent committee to conduct the investigation. For this purpose, the issuer should use its best endeavors and take appropriate measures to scrutinise the independence of each member of the independent committee. The independent committee should exclude directors whose independence may be reasonably questioned including, among others, those who might have been involved in or aware of the irregularities at the material time.[8]

20. In addition, each member of the independent committee should confirm in writing that he/she is not aware of factors that may affect his/her independence in conducting the investigation.

21. On matters relating to the investigation, the independent committee should not engage or otherwise seek advice from advisers who (i) act for the issuer, its connected persons, or persons/entities involved in or aware of the irregularities or (ii) have been involved in a transaction or arrangement relating to the irregularities.

22. Where accounting irregularities are involved, the independent committee should include at least one incumbent director with appropriate professional qualifications or accounting or related financial management expertise.

[8] Where, during an investigation, the independence of an independent committee member is found to be questionable, he/she is expected to be excluded from the committee immediately. The independent committee should then assess the completeness and credibility of the investigation conducted so far.

23. Directors who are not members of the independent committee should not in any way, directly or indirectly, interfere with or exert undue influence over the investigation process or otherwise impair the independence of the investigation.

(D) Overview of independent committee's responsibilities

- **Selection of investigator**

24. To ensure the independence and impartiality of an investigation, the independent committee should avoid engaging an investigator whose independence may be reasonably questioned (see paragraph 21 above).

25. In addition, the investigator engaged by the independent committee must have the necessary expertise, competence, resources and time to perform the engagement. It should consider, for example, the investigator's experience and reputation in investigating cases of similar nature and complexity, and the auditors' advice on the qualification or expertise required of the investigator, if any.

26. Where the alleged irregularities involve potentially fraudulent activities (for example, false accounting or misappropriation of assets), the independent committee should engage a forensic investigator to conduct the investigation.[9] An issuer which does not engage an investigator in a timely manner with the necessary forensic accounting capabilities could end up being unable to complete the required investigation to meet the resumption conditions/guidance within the remedial period, and risks being delisted.

27. The independent committee is expected not to change the investigator without valid justification. If the independent committee considers a change to be necessary, it should:

    (a) give a full explanation of its justification for the change, and procure the issuer to announce the same;

    (b) procure the outgoing investigator to pass all investigation materials in its possession together with its observations and queries, if any, to the incoming investigator; and

    (c) procure the incoming investigator to consider and assess the work that has been performed and the observations and queries raised by the outgoing investigator. The incoming investigator should understand from the outgoing investigator the latter's observations and queries and perform specific procedures to fully address them. The incoming investigator should reflect on how it has done so in its investigation report.

- **Planning, monitoring, assessing and reporting an investigation**

<u>Planning and monitoring</u>

28. The independent committee should devise an investigation plan, having regard to the guidance below.

[9] Also see Guidance Letter on Long Suspension and Delisting (GL95-18), paragraph 40(b).

29. First, the independent committee should agree with the investigator on the objectives of the investigation and its scope[10] and methodology.

30. For this purpose, the independent committee should bear in mind the matters set out in section II above and our expectation that the investigation report should include, among other relevant information:

    (a) the background, objectives, and scope of the investigation;

    (b) identification of the documents and sources of information relied upon to prepare the report and how any assumptions were made;

    (c) the methodology adopted, including a description of the approaches used (such as the procedures used to source the relevant and credible evidence) and rationale for selecting such approaches;

    (d) details of, and the extent of reliance on, the work of others, if any;

    (e) the findings and conclusions, with sufficient information to (i) relate them to the supporting information, documents, analysis and search results, and (ii) present a thorough examination of the evidence that uncovers the root cause(s) of the relevant issue(s); and

    (f) any scope or other limitations that might affect the findings and conclusions, together with any unresolved queries that the investigator might still have upon completion of the investigation.

31. If accounting irregularities are involved, the independent committee should also discuss with the issuer's auditors before agreeing the objectives, scope and methodology with the investigator. The independent committee should also provide the auditors with regular updates and discuss with them on any additional accounting-related issues or irregularities identified during the investigation.

32. Second, the independent committee should agree with the investigator a clear timeframe for each stage of the investigation work, with the aim of completing the investigation as soon as practicable, and ensuring that the resumption conditions/guidance can be met before the remedial period ends.

33. Third, after the investigation plan is agreed, the independent committee should keep monitoring the investigation progress. It should set up a reporting mechanism where the investigator is required to provide regular and timely updates.

[10] For reference, there was a case where the controlling shareholder of the suspended issuer was found to have received the issuer's unauthorised financial assistance. To address concerns about the integrity of the controlling shareholder which was able to exert substantial influence over the issuer's business and affairs and, in turn, the issuer's suitability for continued listing, the issuer's independent forensic investigation was extended to cover the controlling shareholder's involvement and the matters set out in paragraphs 7 to 8 of this guidance letter.

34. The independent committee should regularly meet and discuss with the investigator the progress of the investigation and the issues that have arisen (which may include additional irregularities identified[11] and any difficulties the investigator has encountered during the investigation), and how such issues are to be resolved. Where additional irregularities are identified during an investigation, the independent committee should give timely consideration to extending the investigation scope to cover the same (also see paragraphs 6 and 7 above).

35. Where there is any potential delay in the progress of an investigation, the independent committee should ascertain the cause of the delay and its impact on the agreed timeframe. It should agree with the investigator the action to be taken to minimise the impact of the delay without compromising the standard or quality of the investigation. It should provide details to the board of directors, who should then procure the issuer to announce the same to keep the market informed.

Assessment

36. The independent committee should assess the investigation findings once available and provide an impartial and objective view on:

(a) whether the investigation has been properly conducted in accordance with the objectives, scope and methodology agreed with the investigator;

(b) whether the investigation conducted is adequate to find out the relevant facts, address the issues identified[12] and meet its objectives, in particular, whether the findings and any conclusion reached are supported with sufficient factual basis, analysis and/or search results; and

(c) if (a) and/or (b) is/are negative, whether any further investigation or other appropriate action should be conducted and, if so, in what aspects and how.

37. In this process, the reliance placed by the independent committee on the investigator's work must be reasonable. It should avoid placing excessive or unquestioning reliance on the investigation findings and the conclusions made by the investigator. Instead, the independent committee is expected to exercise appropriate scepticism and, where appropriate, apply common sense when identifying and analysing the relevant information and assessing its completeness and credibility, bearing in mind that the information may be biased, false, unreliable and/or incomplete.

38. In particular, the independent committee should assess and procure the investigator to take additional steps to (i) verify unsubstantiated or generic assertions of facts, market or industry practices or government policies, and (ii) if inconsistent evidence is found, assess the credibility of the evidence or explain the inconsistencies.

39. For example,

(a) the credibility of an interviewee's bare denial of involvement in or knowledge of an unauthorised transaction should be assessed against his position and responsibilities at the material time and verified, rather than being accepted at face value.

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11 See paragraphs 6 to 8 of this guidance letter.
12 Also see paragraph 8 of this guidance letter

Hence, if, at the material time, the interviewee was tasked to be an approver of transactions of a similar nature, the investigator should try to find out with a clear basis why and how the interviewee could be (and was in fact) ignorant of the fund outflow relevant to the unauthorised transaction as asserted. If the investigator cannot do so, it should state this fact in the investigation report (i.e. that it was unable to establish why the interviewee was ignorant of the relevant fund outflow, as claimed by the interviewee), rather than simply stating that there was no evidence to suggest that the interviewee knew about the relevant fund outflow.

(b) where an issuer is found to have provided unauthorised financial assistance, the issuer's internal records purporting to show the magnitude of such financial assistance should, as far as practicable, be verified by independent third party documents including, for example, written confirmations from the issuer's banks involved in related fund transfers; and

(c) likewise, where the commercial rationale of a transaction is at issue, the credibility of any explanation given by the person who procured the issuer to enter into such transaction (including any self-serving document provided by him/her) should be critically assessed together with all the other relevant evidence and, as far as practicable, be verified by other objective evidence such as independent third party documents or witness(es).

40. When in doubt, the independent committee should consult the investigator and explore whether there are alternative methodologies, procedures or approaches that can be adopted to verify the information that has been collected.

41. Where applicable, the independent committee should also obtain and take into account the auditors' view on whether the investigation findings are sufficient to address the relevant audit issues raised by the auditors (or their predecessor, if any) and the basis for that view.

Reporting

42. The independent committee should ensure that the information contained in the investigation report is clearly presented, accurate and complete in all material respects, and not misleading or deceptive. The report must not (i) omit material facts of an unfavourable nature or fail to accord them with appropriate significance or (ii) present favourable possibilities as certain or as more probable than is likely to be the case.[13]

43. The issuer should provide the Exchange with a copy of the investigation report as soon as practicable. After review, the Exchange may raise queries with the independent committee and require the investigation report to be further elaborated upon to address the queries. This may, in some cases, reflect the deficiencies of the investigation conducted so far and lead to further investigation being required.

(E) Examples of investigation defects

44. Below are non-exhaustive examples of defects in investigations that have, in past cases, raised issues about the completeness and accuracy of the investigations.

- **Unclear selection criteria adopted for investigation**

[13] This is in line with the general principles for presentation of information under Rule 2.13.

45. Where the criteria adopted for selecting, among others, the entities, persons or time period covered by the investigation are unclear, the scope of the investigation may be inadequate to achieve its objectives.

46. For example, it is questionable whether the investigation could uncover:

    (a) all the relevant subsidiaries involved in the irregularities if the investigation covers mainly the issuer's non-operating subsidiaries rather than the operating subsidiaries which are more likely to have been involved in the irregularities; and

    (b) all the personnel involved in or aware of the relevant events if the investigator has only selected the personnel at the working level for investigation, but not those who were likely to be involved in deciding or approving the unauthorised transactions in question.

47. Similarly, where the period under investigation failed to cover the full period up to the time when (i) the director who orchestrated the identified unauthorised financial assistance left the issuer's group, and (ii) the relevant internal control deficiencies of the issuer were rectified, the investigation may not be able to reveal all the relevant events leading to the irregularities and/or other similar irregularities.

48. The independent committee should therefore ensure that there is a clear and reasonable basis for the selection criteria and that the criteria are suitable to achieve the objectives of the investigation.

49. Likewise, when sample testing is conducted to try to generalise inferences and findings, it is expected that there is a clear and reasonable basis for selecting the samples in order to support the reliability of the inferences or findings drawn from the sample testing results.

50. For example, when investigating the magnitude of unauthorised fund flows during a particular period, an investigator may consider it more practical to conduct a sample testing (say, based on a minimum fund flow amount) than an investigation into each of the fund flows during the period. Nevertheless, the investigator is expected to clearly explain in the investigation report the basis and reasonableness of the selected sample size for the investigation. The reliability of a sample test is questionable where the sample size selected is too small or the nature of the transactions selected for sample testing is different from that of the irregular transactions identified.

- **Inadequate investigation scope to cover all material irregularities and key issues relevant to them**

51. The lack of an adequately defined scope of investigation may result in material irregularities or important aspects being overlooked or left unexamined, causing the underlying root cause(s) of the issues to be left undiscovered.

52. For example, there were cases where the investigator identified the internal control deficiencies that allowed certain unauthorised financial assistance to occur undetected. However, the scope of the investigations did not cover (i) the identities of the persons who made use of the internal control deficiencies or bypassed the internal controls and procedures to effect the unauthorised financial assistance, and (ii) whether such financial assistance was provided with any commercial rationale. As a result of the inadequate scope of the investigations, we remained concerned with the integrity, character or competence of the issuer's management, which could be an additional cause of the occurrence of the unauthorised financial assistance.

53. Therefore, the independent committee should ensure that the objectives, scope and methodology of an investigation are adequately defined at the outset of the investigation.

- **Lack of adequate alternative procedures to address the limitations of investigation**

54. The limitations to an investigation, if unaddressed, may call into question the completeness and accuracy of the investigation findings. Such limitations to an investigation may arise, for example, when an investigator is unable to conduct a forensic review due to loss of records or reformatting of the computer operating system, or when the investigator is unable to interview outgoing or uncooperative staff or other relevant parties.

55. The independent committee should discuss with the investigator and, where appropriate, the auditors as to whether and, if so, what alternative procedures are available to address the limitations.

(F) Announcement of findings

56. When an investigation report is available, the directors should procure the issuer to issue an announcement in a timely manner not only to summarise the contents of the report but also state the independent committee's:

(a) assessment of the issues identified in or arisen from the investigation findings (such as audit issues, concerns about integrity, character and competence of management personnel, internal control deficiencies and other Listing Rule non-compliance, etc), together its view on whether the irregularity identified is an isolated incident, a recurring incident and/or a systemic failure and the basis of that view;

(b) assessment of the adequacy of the investigation conducted; and

(c) recommended remedial action.

57. The announcement should also state (i) the board of directors' assessment of the impact of the irregularities on the issuer, financially and otherwise, and (ii) the remedial action taken and to be taken and the timeline for such remedial action. If the board does not intend to implement any remedial action recommended by the independent committee, it should procure the issuer to announce such intention with reason.

58. A few issuers were considered not to have announced the investigation findings in compliance with the resumption conditions/guidance and Rule 2.13, as their announcements omitted to mention all the key limitations encountered by the investigators (including directors' refusal to provide information to the investigators) and the key issues encountered by the investigators to ascertain whether any officers of the issuers' group (past or present) were involved in the unauthorised transactions and, if so, the extent of their involvement.

59. Where an investigation is not completed within the remedial period of the issuer, directors are expected to procure the issuer to announce this fact with reason and, if possible, the investigation findings that are available so far.

IV. Others

60. As a general reminder, a long suspended issuer must remedy all the issues causing the trading suspension, meet all our resumption guidance and re-comply with the Rules before the remedial period ends in order to maintain its listing status.

61. Separately, for the avoidance of doubt, where the Exchange is satisfied with a suspended issuer's compliance with the resumption conditions/guidance and allows trading in its shares to resume, this is without prejudice to the Exchange continuing its investigation into any possible breach of the Listing Rules and/or bringing disciplinary action under Chapter 2A of the Listing Rules against the issuer or any other parties as and when it considers appropriate.

Whether the Exchange would cancel the listing of a listed issuer whose shares had been suspended from trading for a prolonged period due to insufficient public float

Facts[1]

1. Trading in shares of a Main Board issuer (**Company A**) had been suspended pending restoration of its public float.

2. At the time of trading suspension, Company A had two major shareholders (each holding about 45% of Company A's issued shares) and its public float was below 10%. After the suspension, there were certain takeover related matters involving a possible general offer of Company A's shares which might have affected Company A's plans to resolve the public float issue.

3. About eight months ago, Company A noted that those takeover related matters were resolved and there was no general offer of Company A's shares. Company A announced its intention to issue new shares to independent placees to restore the public float to at least 25%.

4. Since then, Company A had some discussions with its financial advisers but there was no material development on the proposed placing. It also submitted an alternative proposal to the Exchange but the proposal could not satisfactorily address the public float issue and did not proceed. In response to the Exchange's concern about the prolonged suspension of Company A's shares, Company A requested for an extension of time to resolve the public float issue until the market conditions had improved. However, no concrete plan or timetable was provided.

[1] Time reference is the time to date of the decision.

Relevant Listing Rules

5. Rule 6.01 provides that:

"Listing is always granted subject to the condition that where the Exchange considers it necessary for the protection of the investor or the maintenance of an orderly market, it may at any time direct a trading halt or suspend dealings in any securities or cancel the listing of any securities in such circumstances and subject to such conditions as it thinks fit, whether requested by the issuer or not. The Exchange may also do so where:— …

…

(2) the Exchange considers there are insufficient securities in the hands of the public …

…"

6. Rule 6.04 provides that:

"Where dealings have been halted or suspended, the procedure for lifting the trading halt or suspension will depend on the circumstances and the Exchange reserves the right to impose such conditions as it considers appropriate. The issuer will normally be required to announce the reason for the trading halt or suspension and, where appropriate, the anticipated timing of the lifting of the trading halt or suspension…The continuation of a suspension for a prolonged period without the issuer taking adequate action to obtain restoration of listing may lead to the Exchange cancelling the listing."

7. Rule 6.10 provides that:

"There may be cases where a listing is cancelled without a suspension intervening. Where the Exchange considers that any circumstances set out in rule 6.01 arise, it may:

(1) publish an announcement naming the issuer and specifying the period within which the issuer must have remedied those matters which have given rise to such circumstances. Where appropriate the Exchange will suspend dealings in the issuer's securities. If the issuer fails to remedy those matters within the specified period, the Exchange will cancel the listing. The Exchange may treat any proposals to remedy those matters as if they were an application for listing from a new applicant for all purposes, in which case, the issuer must comply with the requirements for new listing applications as set out in the Listing Rules; or

… "

8. Rule 8.08 provides that:

"There must be an open market in the securities for which listing is sought. This will normally mean that:

(1) (a) at least 25 % of the issuer's total number of issued shares must at all times be held by the public.

…"

(Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

9. Rule 13.32 provides that:

> *"(1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …*
>
> *(2) Once the issuer becomes aware that the number of listed securities in the hands of the public has fallen below the relevant prescribed minimum percentage the issuer shall take steps to ensure compliance at the earliest possible moment.*
>
> *…*
>
> *(3) If the percentage falls below the minimum, the Exchange reserves the right to require suspension of trading in an issuer's securities until appropriate steps have been taken to restore the minimum percentage of securities in public hands. In this connection, the Exchange will normally require suspension of trading in an issuer's securities where the percentage of its public float falls below 15%...*
>
> *…"*

Analysis

10. Rule 6.01 provides that where the Exchange considers it necessary for the protection of the investor or the maintenance of an orderly market, it may suspend trading or cancel the listing of any securities. The Rule also specifies certain circumstances under which the Exchange may suspend trading or cancel a listing, which include insufficient public float.

11. The continuation of a suspension for a prolonged period is detrimental to maintaining order or confidence in the market. It deprives shareholders' right from trading their shares or realising their investments in the market; and is not in the interest of the investing public. Rule 6.04 sets out the general principle that the continuation of a suspension for a prolonged period without the issuer taking adequate action to obtain restoration of listing may lead to the Exchange cancelling the listing.

12. For delisting under any of the circumstances set out in Rule 6.01, the Exchange may under Rule 6.10 specify a remedial period for the issuer to address the matter that gives rise to the trading suspension before delisting. The length of the remedial period will depend on the nature and complexity of the matter which the Exchange requires the issuer to rectify. Where trading is suspended due to insufficient public float, the Exchange will expect the issuer to address the matter within a reasonably short period of time.

13. In this case, trading in Company A's shares had been suspended for a prolonged period due to insufficient public float. Whilst Company A had announced its intention to restore the public float through placing of new shares, there was no material development over a period of eight months. In its latest submission, Company A was still unable to put forward any concrete plan or timetable to address the public float issue. The Exchange considered that Company A had not taken adequate actions to address the public float issue for resumption of trading.

14. Having considered the facts and circumstances of this case, the Exchange decided to commence the delisting process and gave Company A a six-month period to address the public float issue.

Conclusion

15. The Exchange served a notice to Company A on the commencement of the delisting process under Rules 6.01(2) and 6.10 on the ground that Company A had insufficient public float for a prolonged period. If Company A failed to address the public float issue within six months, the Exchange would proceed with cancellation of Company A's listing.

Subsequent development

16. Company A's public float had been restored to 25% within the six-month period as a result of the issue of new shares by Company A and the sale of existing shares by its controlling shareholder to independent placees. As a result, trading in Company A's shares had resumed.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

5

Continued listing criteria

5.1 Suitability for listing

Guidance letter – Guidance on listed issuer's suitability for continued listing	GL96-18	5.1 – 1
Listing decision – Whether a listed issuer was no longer suitable for listing due to its failure to address audit issues and forensic findings that resulted in continued trading suspension	LD114-2017	5.1 – 8

5.2 Sufficient operations and assets

Guidance letter – Guidance on sufficiency of operations	GL106-19	5.2 – 1

Guidance on listed issuer's suitability for continued listing

I. Purpose

1. This letter provides guidance on the general approach relating to the Exchange's assessment of the suitability of a listed issuer or its business for continued listing.

II. Concept of "suitability for listing"

2. The Exchange, as frontline regulator of listed issuers, has a statutory duty under the Securities and Futures Ordinance (**SFO**) to ensure, as far as reasonably practicable, an orderly, informed and fair market for the trading of securities. In discharging this duty, the Exchange acts in the interest of the public, having particular regard to the interest of the investing public.

3. MB Rule 8.04 / GEM Rule 11.06 provides that both the issuer and its business must, in the opinion of the Exchange, be suitable for listing. MB Rule 6.01(4) / GEM Rule 9.04(4) provides that if the Exchange considers a listed issuer or its business is no longer suitable for listing, it may direct a trading halt or suspend dealings in the listed issuer's securities or cancel the listing of these securities.

4. MB Rule 2.06 / GEM Rule 2.09 states that suitability for listing depends on many factors. Compliance with the Listing Rules may not of itself ensure a listed issuer's suitability for continued listing. The Exchange has a broad discretion to interpret and apply the concept of suitability for the purpose of maintaining market confidence with reference to the currently acceptable standards in the market place. It will pay particular regard to the general principles for listing under MB Rule 2.03 / GEM Rule 2.06, which include ensuring:

   - all holders of listed securities are treated fairly and equally;
   - investors and the public are kept fully informed of material factors which might affect their interests; and
   - directors act in the interests of the listed issuer and its shareholders as a whole.

5. Suitability is a broad and flexible concept that applies in a wide range of circumstances. The suitability criterion provides the Exchange with discretion to meet its regulatory objectives and its obligations to act in the best interest of the market as a whole and in the public interest. It is not possible or desirable for decisions on suitability to be subject to "bright line" criteria, or to seek to reduce the requirements of suitability to a list of "pass-fail" requirements.

6. In an IPO application, the listing applicant must satisfy the Exchange that it and its business are suitable for listing. This is a basic condition that must be met before the listing of its equity securities is approved. Once listed, the issuer must ensure that it and its business continue to be suitable for listing.

7. The Exchange may cancel a listing where the suitability issues are fundamental to the general principles for listing and are beyond remedy, or the listed issuer fails to demonstrate a reasonable prospect of addressing the issues and resuming trading within a reasonable period of time.

8. This Guidance Letter sets out examples of situations where the Exchange may question an issuer's suitability for continued listing. The Exchange's assessment on the suitability for continued listing of a listed issuer is on an individual basis and in light of all pertinent facts whenever it deems appropriate. Where there are concerns that an issuer has suitability issues, the Exchange has discretion to suspend trading in the securities of the issuer, and give the issuer a reasonable period to address such concerns and take appropriate remedial action. If the issuer fails to address such concerns within the reasonable period, the Exchange may cancel its listing.

III. Guidance

A. Issuers with "shell" characteristics

9. The Exchange noted a number of listed issuers whose controlling shareholders had sold down their interests, and/or the issuers had undertaken a series of actions that led to a diminution of their original businesses and the operation of new businesses. For example, the issuers disposing of or winding down their principal businesses; the existing management of the company resigning; and the issuers establishing or acquiring new businesses unrelated to their original businesses. These new businesses may have a very low barrier to entry and/or can be easily established and discontinued without significant costs, may be asset-light or the assets may be highly liquid or marketable.

10. In certain individual cases, it is unclear whether these new businesses have substance and are sustainable in the longer term; are operated commercially with the proper infrastructure, processes and controls normally associated with businesses in those industries; are managed by officers with expertise in the business; and the size of the operation and the level of activities are sufficient to support the costs associated with a listing. These issuers may have market capitalizations disproportionate to the size and prospects of their businesses, and may be "blue sky companies"[1] susceptible of speculative activities and market manipulation. This raises similar concerns about the impact of such activities on the orderliness, quality and reputation of the market. The Exchange has concerns that in these individual cases, the issuers may be carrying on these activities for the purpose of maintaining a listing status rather than genuinely operating and developing the new business. The media commonly refer to these activities as "shell maintenance".

[1] "Blue sky companies" are those where public investors have no or little information about their business plans and prospects, leaving much room for the market to speculate on their possible acquisitions. These activities create opportunities for market manipulation.

11. The Exchange noted that certain types of businesses, such as proprietary securities trading, money lending and indent trading may be employed in these circumstances as they can be operated in a manner that fit the characteristics described in paragraph 10 above. Where, based on the specific facts and circumstances, the business models employed by these listed issuers exhibit such characteristics, there may be questions about their suitability for continued listing. For example, the Exchange may question an issuer's suitability for continued listing if there is a concern that the issuer's money lending business, being a material part of its business, is not a business of substance having regard to its business model, operating scale and history, source of funding, size and diversity of customer base, loan portfolio and internal control systems[2]. Where the Exchange becomes concerned that a material part of the company or its businesses is no longer suitable for listing, it may suspend the trading in the company's securities and request the company to address its concerns (see paragraph 8).

12. It should be noted that an assessment of the suitability of an issuer or its business(es) for continued listing must be made case by case, based on the specific business model employed by the issuer and the particular facts and circumstances of that issuer. For the avoidance of doubt, it is the specific business model adopted by issuers, and not the specific type(s) of business themselves cited in paragraph 11 above, that may render the company or business unsuitable for listing.

B. Prolonged suspension

13. The Listing Rules require the duration of any trading suspension to be for the shortest possible period. This ensures the proper functioning of the market and prevents shareholders and other investors from being denied reasonable access to the market. The directors of a suspended issuer are obliged to take adequate action for the issuer to remedy the issues resulting in the suspension and resume trading as soon as practicable. This fulfills their undertakings given to the Exchange to procure the issuer to comply with the Listing Rules.

14. If an issuer fails to remedy the issues resulting in the suspension, the trading suspension will be prolonged. This would deprive shareholders from trading their shares and/or realizing their investments in the market. The issuer's suitability for continued listing will become an issue when, for example, the issuer fails to demonstrate a reasonable prospect of remedying the issues and resume trading within a reasonable period of time, or its directors become uncontactable by the Exchange or otherwise fail or refuse to respond to the Exchange's enquiry as to the resumption plan or its progress. This will not prejudice the Exchange's right to consider an issuer no longer suitable for listing on the basis of the underlying issues causing the trading suspension themselves or other reasons as it considers appropriate.

C. Other instances of non-suitability

(1) Suitability issues concerning directors or persons with substantial influence

15. Directors of a listed issuer are, collectively and individually, responsible for the issuer's management and operations.

[2] See also Guidance Letter GL106-19 on Sufficiency of Operations. The Exchange may consider the issuer not to meet the continued listing criteria under Rule 13.24 in these circumstances.

16. An individual may not be suitable to be a director if an incident involving him raises a serious doubt as to his character or integrity and his ability to fulfill his duty to act honestly, in good faith and for a proper purpose[3]. A non-exhaustive list of examples include: involvement in fraud, theft or other types of dishonesty (such as false accounting, bribery, conspiracy to defraud, misappropriation of funds, money laundering and provision of false and misleading testimony to regulators), or breach of securities law, rules or regulations (either personally or through the company of which he is or was a director). This assessment is on a case-by-case basis.

17. If a director is no longer suitable to act as director, the retention of office by the director is prejudicial to the interests of shareholders. If he is also a person being highly likely to be able to exert control or substantial influence over the issuer's operation and management, the concern about the company's suitability for continued listing would exist irrespective of whether he ceases to be a director.

(2) Material breach of the Listing Rules

18. Listed issuers must comply with the requirements under the Listing Rules. Persistent failure to comply with the Listing Rules in a material manner prevents the operation of a fair, orderly and informed market for the trading of securities and undermines the interests of investors. This raises a serious concern about whether the issuer is suitable for continued listing.

19. For example, the Listing Rules require listed issuers to publish audited financial statements at regular intervals, enabling shareholders and potential investors to appraise their current financial position. Failure to publish the required financial statements will result in a trading suspension of the issuer's shares. An issuer's continued failure to rectify the breach would deprive shareholders and potential investors of (i) the financial information to appraise the issuer's position, and (ii) reasonable access to the market for trading their shares and/or realizing their investments in the market. This calls into question whether the issuer remains suitable for listing.

(3) Inability to disclose material information

20. To keep shareholders and potential investors fully informed of material factors which might affect their interests[4], listed issuers have various general and specific continuing disclosure obligations under the Listing Rules (including, among others, disclosure of inside information required to be disclosed under Part XIVA of the SFO and periodic financial statements).

21. If an issuer engages in arrangements, transactions, or businesses which impose secrecy obligations (e.g. state secret), thereby prohibiting the listed issuer from disclosing material information to the market, or providing necessary information to its auditors for finalizing their reports, this would deprive shareholders and potential investors of the information necessary to make an informed investment decision. This gives rise to the issue of suitability for continued listing.

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3 See MB Rules 3.08 and 3.09 / GEM Rules 5.01 and 5.02.
4 MB Rule 2.03(3) / GEM Rule 2.06(3).

(4) Non-compliance with laws and regulations

22. Listed issuers should comply with applicable laws and regulations at all times. Intentional, systemic and/or repeated breaches of laws and regulations by a listed issuer may affect its suitability for listing. The concern may not only be about a lack of management integrity (in the case of intentional breaches), but also about a lack of competence or capacity, borne out by systemic or repeated breaches, even if not deliberate.

23. Relevant factors for an assessment of an issuer's suitability for listing on this basis include:

- The nature, extent and seriousness of the breaches.
- The reasons for the breaches, whether they were intentional, fraudulent, or due to negligence or recklessness.
- The impact of the breaches on the issuer's operation and financial performance.

For example, an issuer may be considered no longer suitable for listing if the non-compliance leads to revocation of a licence or permit which is a prerequisite for or essential to the continued principal business operations of the issuer.

(5) Trade or economic sanctions

24. Reference is made to paragraphs 5 to 10 of Chapter 4.4 of the Guide for New Listing Applicants (the **Guide**), providing guidance on suitability for listing of listing applicants engaging in activities in countries subject to trade or economic sanctions imposed by overseas jurisdictions and listing applicants which are sanctioned targets, among others.

25. A listed issuer may become exposed to sanction risks due to its new business / activity which is sanctionable by law or a change in law or regulation which makes its existing business become sanctionable. It must timely disclose any sanctions risks, regulatory action/litigation or sanctions and their impact as required under the Inside Information Provisions[5]. Such disclosure enables investors to make a properly informed assessment of the issuer and hence an informed investment decision. If a disclosure is made under the Inside Information Provisions, the Exchange may ask the issuer for further details of the relevant activities and a legal opinion assessing the sanctions risk to the issuer, investors and the Exchange (including related companies). Depending on the nature and materiality of the sanctions risk, a listed issuer may be required to adopt certain measures and to make certain disclosure as described in paragraphs 6 to 8 of Chapter 4.4 of the Guide.

26. A listed issuer's suitability for continued listing would become an issue in extreme cases where (i) the sanction risks and sanctions imposed have materially undermined the issuer's business and the issuer does not have sufficient operations or assets required under the Listing Rules to maintain a listing status; or (ii) the sanction risks to investors and the Exchange (including related companies) are significant.

[5] Part XIVA of the Securities and Futures Ordinance and MB Rule 13.09(2)(a) / GEM Rule 17.10(2)(a)

27. Listed issuers may conduct secondary equity fundraisings. The Exchange would consider their listing applications case by case. In particular, if the funds are raised to finance sanctionable activities, the Exchange would unlikely give the listing approval. If the funds are intended for activities which are likely to attract sanctions under an applicable sanction law, the Exchange may ask the issuer for a legal opinion assessing the sanctions risks to the issuer, the investors and the Exchange (including related companies) before deciding whether to give the listing approval.

(6) Business structure

28. A listed issuer should ensure that its business structure or arrangements can adequately safeguard its assets and shareholders' interests, failing which the Exchange may consider the issuer no longer suitable for listing.

29. As an example, reference is made to our Guidance Letter GL77-14, setting out guidance on the use of contractual-based arrangements or structures by listed issuers to indirectly own and control any part of their businesses. Under such arrangements, the issuer does not directly own the operating company, relying solely on structured contracts to control the operating company and enjoy the economic benefits derived from it. Given the inherent risks associated with such arrangements to the issuer's interests, the Exchange may consider an issuer adopting such arrangements unsuitable for continued listing unless such arrangements are in strict compliance with the conditions set out in Guidance Letter GL77-14.

(7) Gambling

30. Listed issuers which engage in gambling business will be considered unsuitable for listing unless they satisfy the requirements set out in our Guidance Letter GL71-14 on "Gambling activities of new listing applicants and listed issuers".

(8) Material reliance on various parties

31. Material reliance on a controlling shareholder / substantial shareholder, a single major customer / supplier, or another party (the **Relevant Counterparty**) may raise serious concerns on whether the business model is viable and sustainable, particularly if any material adverse change to or termination of the relationship with the Relevant Counterparty would result in material impact on the issuer's financial condition.

32. Some Relevant Counterparties dominate the industries in which they operate due to regulatory restrictions, high entry barriers or other factors. As an issuer that operates in such industries is unlikely to diversify or reduce its reliance on the Relevant Counterparties (i.e. such reliance is an industry norm), the Exchange will examine whether there are any red flags indicating its relationships with the Relevant Counterparties are likely to be terminated or otherwise materially adversely change.

33. An issuer may be able to demonstrate that despite its material reliance on a Relevant Counterparty, any change in the relationship will not have a material adverse impact on its business because it is or will be able to effectively mitigate its exposure (e.g. decrease in sales, increase in raw material costs and/or production time, cost of business disruption). For example, if the Relevant Counterparty is a supplier for raw materials that are readily available or for which there are reasonable substitutes, the issuer may easily procure such raw materials from a different supplier at a similar price or substitute with another product.

34. Further, where the Relevant Counterparty is also a connected person, it may heighten our concern that the issuer is no longer suitable for continued listing. For example, if the issuer's supply and sales are both dominated by the controlling shareholder (or its associates), and the transactions become the issuer's sole or primary source of revenue, there is a serious concern that the issuer would be a captive company merely serving the controlling shareholder. In this context and, in such circumstances, it is likely that the business will not be viable and sustainable without these transactions. As an issuer's ongoing viability is wholly dependent on the financial position of the controlling shareholder, if such financial position is unknown, the public shareholders and potential investors of the issuer would not have the necessary information for properly assessing the issuer's position. In these circumstances, the issuer may be considered no longer suitable for continued listing.

(9) Fraud

35. There are cases where an issuer is considered no longer suitable for listing if it is found that its published financial statements were based on fraudulent accounts with significant overstatement of profits, or false documents (e.g. invoices, sales records), or there existed serious discrepancies among different sets of books and accounts which the issuer failed to explain or reconcile. In these circumstances, shareholders and potential investors are deprived of the necessary financial information for making an informed assessment of the issuer and there is a serious question over the management integrity.

(10) Material internal control failures

36. Listed issuers should maintain a sound system of internal controls over their financial, operational and compliance matters to safeguard their assets and protect the interests of shareholders [6]. There are cases where an issuer fails to (i) provide sufficient evidence to support the completeness and accuracy of its financial statements in material respects (leading to a disclaimer audit opinion), (ii) prevent or detect corporate misconduct such as misappropriation of assets or funds, or (iii) timely disclose material information to shareholders and potential investors. This may result from significant internal control failures, and is detrimental to the interests of shareholders and the fair, orderly and informed market for trading of securities. In these circumstances, the issuer may be considered unsuitable for continued listing.

(11) Failure to provide information to the Exchange

37. The Listing Rules require listed issuers to provide the Exchange with information requested by the latter to protect investors, ensure the smooth operation of the market or verify compliance with the Listing Rules. Compliance with this requirement is essential to the Exchange performing its statutory duty of maintaining an orderly, informed and fair market.

38. An issuer's suitability for continued listing may be called into question in an extreme case where without the issuer providing the required information to the Exchange, there is a serious concern about whether an orderly, informed and fair market can be maintained.

[6] Paragraph C2 of Appendix C1 to the MB Rules / Paragraph C2 of Appendix C1 to the GEM Rules.

Whether a listed issuer was no longer suitable for listing due to its failure to address audit issues and forensic findings that resulted in continued trading suspension

Facts

1. Trading in shares of a Main Board issuer (**Company A**) was suspended pending release of an announcement about a very substantial acquisition. The acquisition was terminated subsequently but trading remained suspended due to Company A's failure to publish audited annual results.

2. Company A's auditors questioned the recognition of sales and trade receivables, the reasonableness of expenses relating to a distribution channel restructuring plan, and the rationale for providing guarantees to certain parties.

3. As resumption conditions, the Exchange required Company A to conduct a forensic investigation into the audit issues, publish all outstanding financial results and address any auditors' modifications, and inform the market of all material information.

4. The forensic investigation found that:

   (a) Company A had not issued value added tax invoices for most of its domestic sales under PRC tax rules, casting doubts on whether the recognized sales were in fact made.

   (b) Company A had paid substantial cash rebates to four distributors, allegedly under the distribution channel restructuring plan agreed with the distributors. However, it was found not to have monitored whether the distributors used the rebates in accordance with the requirements set out in the plan. Without a plausible explanation, Company A was also found to have paid substantial cash rebates to entities which were not parties to the plan. The forensic accountants questioned the rationale and justification for the cash rebates.

   (c) Absent any internal controls or procedures, Company A had guaranteed loans granted to related parties by banks. The loans were subsequently in default and Company A had paid and made a full provision for the guaranteed debts.

5. The forensic accountants encountered significant limitations that prevented it from conducting a proper investigation. As a result, they were unable to form a view on the audit issues.

6. This gave rise to the following regulatory issues:

   (a) that Company A's financial statements and/or records were not accurate and complete in material respects or were materially misleading;

   (b) that investors had not been given the necessary information to make an informed assessment of Company A;

   (c) the integrity of Company A's management; and

   (d) the lack of adequate internal controls to safeguard Company A's assets and protect shareholders' interests.

7. More than two years had lapsed since the trading suspension. Company A had yet to (i) resolve the audit issues or the forensic findings that resulted in its continued failure to publish financial results and the continued trading suspension; and (ii) fully comply with the resumption conditions.

8. Given the above, the Exchange advised Company A of its (i) concern about the latter's suitability for continued listing and (ii) intention to commence procedures to cancel its listing.

9. In response, Company A's special investigation committee (comprising of all the independent non-executive directors) confirmed that the management of the company had not taken or proposed any action to address the forensic findings and considered that the management was unable to resolve the relevant issues. As an attempt to resolve the issues, the committee then appointed a firm of legal advisers to understand the audit issues and the forensic findings and consider possible remedial measures.

Relevant Listing Rules

Cancellation of listing

10. Rule 6.01 states that:

"Listing is always granted subject to the condition that where the Exchange considers it necessary for the protection of the investor or the maintenance of an orderly market, it may at any time direct a trading halt or suspend dealings in any securities or cancel the listing of any securities in such circumstances and subject to such conditions as it thinks fit, whether requested by the issuer or not. The Exchange may also do so where:— …

…

(4) the Exchange considers that the issuer or its business is no longer suitable for listing."

11. Rule 6.04 states that:

"Where dealings have been halted or suspended, the procedure for lifting the trading halt or suspension will depend on the circumstances and the Exchange reserves the right to impose such conditions as it considers appropriate. The issuer will normally be required to announce the reason for the trading halt or suspension and, where appropriate, the anticipated timing of the lifting of the trading halt or suspension…The continuation of a suspension for a prolonged period without the issuer taking adequate action to obtain restoration of listing may lead to the Exchange cancelling the listing."

12. Rule 6.10 states that:

"… Where the Exchange considers that any circumstances set out in rule 6.01 arise, it may:

(1) publish an announcement naming the issuer and specifying the period within which the issuer must have remedied those matters which have given rise to such circumstances. Where appropriate the Exchange will suspend dealings in the issuer's securities. If the issuer fails to remedy those matters within the specified period, the Exchange will cancel the listing. The Exchange may treat any proposal to remedy those matters as if they were an application for listing from a new applicant for all purposes, in which case, the issuer must comply with the requirements for new listing applications as set out in the Listing Rules; or

(2) cancel the listing of the issuers' securities following the Exchange's publication of an announcement notifying the cancellation of the listing."

Suitability for listing

13. Rule 2.03 states that:

"The Listing Rules reflect currently acceptable standards in the market place and are designed to ensure that investors have and can maintain confidence in the market and in particular that:

(1) applicants are suitable for listing;
(2) the issue and marketing of securities is conducted in a fair and orderly manner and that potential investors are given sufficient information to enable them to make a properly informed assessment of an issuer…;
(3) investors and the public are kept fully informed by listed issuers…of material factors which might affect their interests;
(4) all holders of listed securities are treated fairly and equally;
(5) directors of a listed issuer act in the interest of shareholders as a whole, particularly where the public represents only a minority of the shareholders; and
(6) all new issues of equity securities by a listed issuer are first offered to the existing shareholders by way of rights unless they have agreed otherwise."

(Rule 2.03(6) was amended on 11 June 2024. See Note below.)

14. Rule 2.06 states that:

"Suitability for listing depends on many factors. Applicants for listing should appreciate that compliance with the Exchange Listing Rules may not of itself ensure an applicant's suitability for listing. The Exchange retains a discretion to accept or reject applications and in reaching their decision will pay particular regard to the general principles outlined in rule 2.03. … "

Analysis

15. Rule 6.01 provides that where the Exchange considers it necessary for the protection of investors or the maintenance of an orderly market, it may suspend trading or cancel the listing of any securities. The Rule also specifies certain circumstances under which the Exchange may suspend trading or cancel a listing, which include where the Exchange considers an issuer or its business to be no longer suitable for listing.

16. Suitability for listing, as set out in Rule 2.06, depends on many factors. The Exchange has a broad discretion to interpret and apply the concept of suitability case by case for the purpose of maintaining market confidence with reference to the currently acceptable standards in the market place. It takes account of its underlying regulatory objectives to, as far as reasonably practicable, ensure an orderly, informed and fair market for the trading of securities listed on it and to act in the interest of the public, having particular regard to the interest of the investing public.

17. The existence of issuers which are unsuitable for listing would undermine the quality of the market and bring it into disrepute. Rule 6.10 sets out the delisting procedures applicable to an issuer or its business which is no longer suitable for listing.

18. In this case,

    (a) The audit issues and the forensic findings raised a serious question about the accuracy and credibility of Company A's financial statements or records in material respects, the integrity of its management, and the lack of adequate internal controls or procedures to safeguard its assets and protect shareholders' interests.

    (b) As the management failed to take actions to address the audit issues or the forensic findings, Company A was not able to properly comply with its financial reporting obligations under the Rules despite a prolonged period of suspension. This deprived shareholders and investors of the financial information necessary for appraising its position.

19. The above issues were detrimental to maintaining confidence in the market and were not in the interest of the investing public. In these circumstances, there was a serious issue about Company A's suitability for continued listing.

20. Having considered the facts and circumstances of this case and the special investigation committee's actions as described in paragraph 9, the Exchange commenced the delisting process and gave Company A six months to remedy the matters rendering it no longer suitable for listing.

Conclusion

21. The Exchange served a notice on Company A to commence the delisting process under Rule 6.01(4) on the ground that Company A was no longer suitable for listing. If Company A failed to remedy the matters within six months, the Exchange would proceed with cancellation of Company A's listing.

Note: Rule 2.03(6) was amended on 11 June 2024 to apply the existing requirements for an issue of new shares to a resale of treasury shares. The Rule amendments would not change the analysis and conclusion in this case.

Guidance on sufficiency of operations

I. Background and purpose

1. On 1 October 2019, amendments to Rule 13.24 came into effect. The amended Rule 13.24 imposes a continuing listing obligation on a listed issuer to maintain a business with a sufficient level of operations and assets of sufficient value to support its operations to warrant its continued listing.

2. In recent years the prevalence of backdoor listings has resulted in a substantial increase in the value of a listing status, leading to extensive activities related to investors acquiring controls of listed issuers for their listing platforms (rather than the underlying business) for eventual backdoor listings, and listed issuers undertaking corporate actions (such as disposals of businesses) to facilitate the sale of their listing platforms. There were also cases where the listed issuers, after disposing of or otherwise winding down their principal businesses, established or acquired new businesses that have very low barriers of entry and/or can be easily established and discontinued without significant costs. These actions may leave listed issuers with minimal operations or businesses without substance. This, in turn, leads to speculative trading activities and opportunities for market manipulation, and undermines investors' confidence in our market. Where an issuer undertakes shell creation or maintenance activities leading to the issuer operating a business with minimal operations, the Exchange would apply Rule 13.24(1). Where the Exchange considers that an issuer is not operating a business of substance, it may apply Rule 13.24, and may also question the issuer's suitability for continued listing under Rule 6.01(4) (see Guidance on listed issuer's suitability for continued listing (HKEX-GL96-18)).

3. This letter provides guidance on the purpose behind and the general approach relating to the Exchange's application of Rule 13.24, with an appendix setting out examples to illustrate how the Exchange applies Rule 13.24. All Rule references in this letter are to the Main Board Listing Rules. As GEM Rule 17.26 is the same as Main Board Rule 13.24, the guidance set out in this letter also applies to GEM issuers. In addition, Listing Review Committee decisions on Rule 13.24 also offer guidance on this subject.

II. Rule 13.24

4. Rule 13.24 states:

"(1) An issuer must carry out, directly or indirectly, a business with a sufficient level of operations and assets of sufficient value to support its operations to warrant the continued listing of the issuer's securities.

Note: Rule 13.24(1) is a qualitative test. The Exchange may consider an issuer to have failed to comply with the rule in situations where, for example, the Exchange considers that the issuer does not have a business that has substance and/or that is viable and sustainable.

The Exchange will make an assessment based on specific facts and circumstances of individual issuers. For example, when assessing whether a money lending business of a particular issuer is a business of substance, the Exchange may consider, among other factors, the business model, operating scale and history, source of funding, size and diversity of customer base and loan portfolio and internal control systems of the money lending business of that particular issuer, taking into account the norms and standards of the relevant industry.

Where the Exchange raises concerns with an issuer about its compliance with the rule, the onus is on the issuer to provide information to address the Exchange's concerns and demonstrate its compliance with the rule.

(2) Proprietary trading and/or investment in securities by an issuer and its subsidiaries (other than an issuer which is an investment company listed under Chapter 21) are normally excluded when considering whether the issuer can meet rule 13.24(1).

Note: This rule would not normally apply to proprietary securities trading and/or investment activities carried out in the ordinary and usual course of business by a member of an issuer's group that is:

(a) a banking company (as defined in rule 14A.88);

(b) an insurance company (as defined in rule 14.04); or

(c) a securities house (as defined in rule 14.04) that is mainly engaged in regulated activities under the SFO. It should be noted that proprietary securities trading and/or investment is not a regulated activity under the SFO and accordingly, this exemption is not available where proprietary securities trading and/or investment constitutes a significant part of the business of the securities house."

5. One of the objectives of Rule 13.24 is to address the issue of "shell companies". Shell companies are often associated with issuers operating at a low level of activities whose size and prospects do not support the costs or purpose associated with a public listing. In particular,

   (a) Under Rule 13.24(1), an issuer must carry out a business with a sufficient level of operations to warrant its continued listing. An issuer that holds significant assets but does not carry out a sufficient level of operations is not compliant with this Rule.

   (b) Under Rule 13.24(2), an issuer's proprietary trading and/or investment in securities is normally excluded when examining its sufficiency of operations and assets under Rule 13.24(1)[1].

   The exception applies to proprietary securities trading and/or investment activities carried out in the ordinary and usual course of business by a member of an issuer's group that is a banking company, an insurance company or a securities house, provided that, in the case of a securities house, that member is mainly engaged in regulated activities under the SFO. It should be noted that proprietary securities trading and/or investment is not a regulated activity under the SFO and accordingly, this exemption is not available where proprietary securities trading and/or investment constitutes a significant part of the business of the securities house.

6. An assessment of Rule 13.24 is generally based on the current operations of the issuer. Where an issuer fails to meet Rule 13.24(1), the Exchange would suspend trading in the issuer's securities under Rule 6.01(3). The issuer would generally be given a period to remedy the issue, failing which the Exchange may cancel the listing of the issuer's securities[2].

III. General application of Rule 13.24(1)

(A) Listed issuers with minimal operations

(i) Business deterioration / discontinuation

7. The Exchange notes a number of cases where the listed issuers completely or substantially ceased their operations or otherwise maintained only minimal operations. This might have resulted from (a) the issuers having gradually scaled down or discontinued their principal business (or a material part thereof), or (b) continual deterioration of the issuers' business due to, for example, decline in the demand for the relevant products or services or deterioration in the business condition of the specific industry. In these circumstances, they failed to maintain a viable and sustainable business to comply with Rule 13.24(1)[3].

8. Among other situations, a listed issuer with the following characteristics would normally be considered not to have a viable and sustainable business that meets Rule 13.24(1):

   (a) The issuer maintains a very low level of operating activities and revenue, raising an issue that the size and prospects of the issuer do not appear to justify the costs or purpose associated with a public listing. This may happen, for example, where the issuer's business does not generate sufficient revenue to cover corporate expense, resulting in net losses and negative operating cashflow.

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1 Before the amendments to Rule 13.24, there were cases where proprietary securities trading was employed to maintain listed shells and was not demonstrated to be a business of substance. Also see paragraphs 11 to 14 of this guidance letter.

2 See Rules 6.01A and 6.10 and Guidance on long suspension and delisting (HKEX-GL95-18).

3 See the note to Rule 13.24(1)

(b) This current scale of operations does not represent a temporary downturn, as the issuer's business has been operating at a very small scale and incurring losses for years.

However, an issuer experiencing a temporary reduction or suspension of operations due to market conditions or business strategies would not be considered to have failed Rule 13.24(1) only because of the temporary circumstances[4].

(c) The issuer fails to demonstrate that it has sufficient assets to support an operation that generates sufficient revenue and profits to warrant a continued listing.

An assessment of sufficiency of assets is with reference to and commensurate with the particular nature, mode and scale of the issuer's operations. It is acknowledged that there are asset-light businesses which, compared to asset-heavy businesses, require assets of lesser value to support their viability and sustainability. Assets that are not used to support an issuer's operations are disregarded.

(ii) Corporate actions leading to minimal operations

9. The Exchange also notes other cases where the issuers structured their corporate actions to substantially scale down their operations through, for example, (i) disposing of the core business which generated the majority of revenue or profit, or (ii) artificially carving out a substantial part of the core business. This caused a significant reduction in their assets, revenues and profits, leaving behind minimal operations which were loss making or generated minimal profits. An issuer conducting a corporate action involving a disposal of or having the effect of discontinuing its principal business (or a material part thereof) must satisfy the Exchange that after the corporate action, it would maintain a business which is viable and sustainable and has substance to comply with Rule 13.24(1). Otherwise, the Exchange will suspend trading in the issuers' securities upon completion of their corporate actions (see Rule 6.01(3)).

(iii) Other circumstances

10. Based on our experience, other circumstances that may lead to issuers having minimal operations and failing to comply with Rule 13.24(1) include:

(a) financial difficulties which seriously impair an issuer's ability to continue its business or which lead to the suspension of some or all of its operations;

(b) the issuer becoming insolvent, as may be evidenced by an uncontested petition for winding up, an order of winding up or the appointment of a liquidator (provisional or not); or

(c) the issuer losing its major operating subsidiaries.

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[4] Examples include:
(i) An issuer suspended its breeding farms and slaughter house in early 2018 upon the outbreak of the Asian Swine Flu in Mainland China. It then refurbished the facilities, redesigned the quality control procedures, maintained continuous dialogue with the government and reapplied for licenses. In late 2020, the issuer obtained licenses to recommence part of its operations.
(ii) A small property development consultant experienced significant business downturn in the past few years due to the US-China trade dispute and tightened housing policies affecting small developers. Recently, the government lifted certain restrictions which would stimulate market demand. The issuer provided a profit forecast (supported by signed contracts with customers) which demonstrated recovery in its operations.
(iii) A mining issuer with its mines being suspended on a temporary basis.

(B) Business model that lacks business substance

11. Where an issuer's business or a material part of its business is not demonstrated to have substance, the Exchange would also consider that the issuer does not have a viable and sustainable business to comply with Rule 13.24(1)[5].

12. The Exchange notes that there were cases where the issuers, given their specific business models and the specific facts and circumstances, were not operating a business of substance. These issuers carried on their activities for the purpose of maintaining their listing status rather than genuinely developing their underlying businesses. Certain types of businesses, such as money lending and indent trading[6], are commonly employed for such purpose.

13. For example, subject to the specific facts and circumstances, a business of money lending or indent trading with the following business models would raise a concern that the business is operated to maintain the issuer's listing status rather than being operated commercially, hence a concern that the business does not have substance:

    (a) Money lending business – the business is carried out without a clear business objective or strategy, a reliable source of funding, or an appropriate infrastructure of credit evaluation, risk management, collections and other functions that are typical of a publicly-listed money lending business. The business maintains a minimal scale of operation, with only a few employees, a high concentration of customers and a small loan portfolio which comprised mainly short term and unsecured loans.

    (b) Indent trading business – the business involves only the issuer sourcing products from suppliers and selling them to a few customers on a back-to-back basis. The issuer provides limited value added services, and does not have demonstrable competitive advantages in procuring new sales orders or expanding customer base. The business is operated by a few employees and generates minimal revenue or gross profits.

14. Based on our experience, other circumstances that may lead to a concern about the substance of a business include:

    (a) reliance on a limited number of transactions or customers, and/or a single source of business (for example, referrals by a connected person or a particular employee);

    (b) the business in question being of a type which has a very low barrier of entry, can be easily established and discontinued without significant costs and/or is asset-light; and

    (c) the basis for generating substantial fees/revenue from the relevant transactions being unclear or questionable.

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5 See the note to Rule 13.24(1).

6 There were also cases where proprietary securities trading was employed to purportedly maintain a listing status. Under the new Rule 13.24(2), subject to a few specific exceptions stated therein, such business is excluded when examining an issuer's compliance with Rule 13.24(1). See paragraph 5 of this guidance letter.

(C) Newly established or acquired business

15. We have also noted cases where an issuer, after disposing of or otherwise substantially scaling down its business, established or acquired a new business to purportedly comply with Rule 13.24(1). Such business may have a limited historical track record to demonstrate its viability and sustainability. While the Exchange would consider its business forecast, such forecast must be supported by a concrete and credible business plan, with projections based on signed contracts and supportable customer demand.

16. We have also noted cases where an issuer asserted that the new businesses had some relationships with its original business and should be regarded as a continuation or reactivation of the same business, and the historical track record of the original business should be considered in assessing the viability and sustainability of the new business. The Exchange noted that while those businesses were in the same industry, they operated with different product types, geographical locations, operating model (e.g. trading vs manufacturing) or required different management expertise. In this circumstance, the historical track record of the disposed (or discontinued) business and/or its management had little or no relevance in assessing the viability and sustainability of the new business.

IV. The Exchange's assessment process and general obligations of listed issuers

17. In our assessment of an issuer's compliance with Rule 13.24, the Exchange would review the following areas:

(i) *Business model* – The issuer must operate a business that is viable and sustainable. The Exchange would review the business model with reference to the industry norm, including whether the business is operated with the proper infrastructure (e.g. property, plant and equipment, patents, experienced personnel), processes and controls normally associated with businesses in those industries; managed by officers with expertise in the business; and whether the size of the business and the level of activities are sufficient to support the costs associated with a listing.

(ii) *Operating scale and history* – An assessment of Rule 13.24 would generally be based on the current operations of the issuer, with reference to its historical track record. For a new business without sufficient operating history, the Exchange would also take into account its future prospects, including its business plans and forecasts. However, the issuer should also have concrete and credible business plans and strategies to support its projections, including, for example, signed contracts or other evidence of customer demand to support its forecasts.

Where there are questions about the credibility of the business plans or forecasts, the issuer would not be considered to comply with Rule 13.24. It would have a remedial period (as noted in paragraph 6 above) to demonstrate that its business plans and forecasts are credible.

(iii) *Sufficient assets to support its operations* – Rule 13.24 also requires the issuer to have sufficient assets to support its operations. This would include, among others, whether it has sufficient funds to develop the business and implement the business plan.

(iv) *Business of substance* – Businesses with little or no substance would not comply with Rule 13.24. These would include businesses that rely on a limited number of transactions or customers, have very low barriers of entry and can be discontinued without significant cost (see paragraphs 11 to 14 for further details). This aligns with the objective of the amendments to Rule 13.24 to address the issue of "shell companies" in a more effective manner.

18. It is a listed issuer's continuing listing obligation under Rule 13.24 to maintain a business with a sufficient level of operations and assets of sufficient value to support its operations to warrant its continued listing. To demonstrate compliance, an issuer must ensure that it makes adequate disclosure of its business affairs, the status of its operations and financial performance. In particular, an issuer is specifically required to publish financial results and reports in compliance with under Rules 13.46 to 13.49 and disclose inside information required to be disclosed under the Inside Information Provisions[7]. These disclosures provide transparency to the market and enable the Exchange to monitor its compliance with Rule 13.24.

19. As part of its regulatory supervision on listed issuers, the Exchange monitors issuers' activities and compliance with the Listing Rules primarily on the basis of their disclosures. Based on an issuer's periodic financial results and other disclosures, the Exchange makes a preliminary assessment of the issuer's compliance with Rule 13.24 on an ongoing basis.

20. If the Exchange is concerned with a particular issuer's compliance with Rule 13.24 upon such preliminary assessment, the Exchange may write a letter to the issuer setting out the observations giving rise to the concern and requesting the issuer to provide a written submission within a specified time period (normally three weeks) showing cause with reasons as to why, despite the matters set out in the letter, it still complies with Rule 13.24 and hence the Exchange should not commence the procedure to cancel its listing. The Exchange will make a ruling on the basis of the information available to it upon the expiry of the specified time period.

21. In response to the Exchange's request, the issuer must provide information to address the Exchange's observations and concerns set out in the letter. Without prejudice to the generality of such request, the issuer is also specifically expected to provide the following information (if not in the issuer's public documents) to demonstrate that it has a business which is viable and sustainable and has substance:

(a) the business objective, strategy and plan;

(b) the business model including how the business operates and generates revenue and profits, and the source of funding;

(c) the operating scale, management expertise and scale of staff or manpower;

(d) the size and diversity of customer base and source of supply;

(e) the role of and relationship with key business stakeholders;

(f) the infrastructure and other functions in support of the operations (e.g. internal systems or controls), together with a comparison with industry norms and standards if appropriate; and

[7] Part XIVA of the Securities and Futures Ordinance

(g) the board's views on the business prospect supported by a credible profitable forecast, if any, which is prepared on the basis of substantiated evidence.

22. Rule 13.24 is a qualitative test and is assessed based on the specific facts and circumstances of individual cases. Therefore, a numerical comparison with other listed issuers (for example, in terms of revenue, profit or assets) would not be an appropriate approach for an issuer to address the Exchange's concerns.

23. If the issuer fails to address the Exchange's concerns, the Exchange will inform the issuer of its decision that the issuer does not meet Rule 13.24. The issuer should publish an announcement on the Exchange's decision and its reasons before 8:30 a.m. on the next business day after it received the decision letter. In addition, the issuer should also include a statement that the trading in its shares will be suspended[8] after the expiry of seven business days from the date of the decision letter, unless the issuer applies for a review of the decision in accordance with its rights under Chapter 2B[9]. The issuer should make a further announcement on the suspension or its decision to review.

24. Further, as a general principle, Rule 2.03(2) requires that the issue and marketing of securities are conducted in a fair and orderly manner and that potential investors are given sufficient information to enable them to make a properly informed assessment of an issuer. Where the Exchange has raised a concern about the issuer's compliance with Rule 13.24 and this concern is not addressed, it will normally refuse to grant listing approval for any issuance of new securities by the issuer.

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8 Under Rule 6.01(3) trading in an issuer's securities will be suspended where the Exchange considers that the issuer has failed to comply with Rule 13.24.

9 Under Chapter 2B, the issuer has the right to have the Listing Division's decision referred to the Listing Committee for review. Any request for review must be served on the Secretary of the Listing Committee within seven business days from the date of the decision.

Appendix

This appendix sets out cases to illustrate how the Exchange applies Rule 13.24 in circumstances described in the guidance letter.

Case number	Description
Case 1	Issuer with minimal operations due to business deterioration
Cases 2, 3 and 4	Issuer who sought to rely on newly established or acquired businesses to support its continued listing after discontinuing or substantially scaling down its principal businesses
Cases 5 and 6	Issuer with minimal operations after disposing of its principal business
Cases 7 and 8	Issuer who sought to rely on newly established or acquired businesses to support its continued listing after disposing of its principal business

Note: While these cases happened before the amendments of Rule 13.24 (or GEM Rule 17.26) in October 2019, such amendments would not change the analysis and conclusion in these cases.

Case number / Listing Rule reference	Background and Decision
Case 1 Rule 13.24	**Background** 1. Company A and its subsidiaries (**Group**) were engaged in coal mining and coal trading. (a) The coal mining business had not generated any revenue since Company A acquired the mining rights of its coal mines about nine years ago. The Group's mining exploration activities had been restricted due to regulatory prohibitions and it had fully impaired the values of the mining rights. (b) The coal trading business commenced about three years ago. Its revenue decreased from HK$30 million in the first year to about HK$11 million in each of the last two financial years. It had a few customers only and recorded a segment loss over the last three years. 2. The Group recorded substantial losses (in the range of HK$25 million to HK$140 million) and negative operating cash flows over the last five financial years. As at the latest year end date, it had total assets of HK$20 million comprising mainly cash and bank balances and trade and other receivables. Its net liabilities amounted to HK$60 million. 3. Company A submitted that it had plans to improve its business operations and financial position. (a) Company A intended to increase the number of customers to up to seven within two years to expand its coal trading business. It also planned to cut the administrative costs and expenses of the Group and raise funds through placing of new shares to repay outstanding indebtedness and reduce finance costs. Based on the above, Company A expected that the Group would record a significant increase in revenue from the coal trading business to more than HK$120 million and HK$140 million in the current and next financial year. It would start making net profits of about HK$6 million in the next financial year. (b) Company A had also identified some potential acquisition targets for business expansion and diversification and expected to complete one within 12 months.

	Decision 4. The Exchange considered that Company A had failed to comply with Rule 13.24 because: (a) The Group maintained a low level of operations. Its coal trading business recorded revenue of HK$11 million only from a few customers with a segment loss, while its coal mining business had never generated any revenue due to regulatory prohibitions. This situation was not a temporary decline or downturn. (b) The Group's plans to improve its business operations and financial position were preliminary and not substantiated. Company A did not provide any detailed information about its business plans or acquisition targets to support a substantial improvement of the Group's scale of operations and financial results as projected. Company A failed to demonstrate that its businesses were viable and sustainable. (c) The Group had total assets of HK$20 million only and net liabilities of HK$60 million. As noted above, the operation of these assets did not generate sufficient revenue and profits to support a continued listing.
Case 2 Rule 13.24	**Background** 1. Company A and its subsidiaries (**Group**) were principally engaged in retail sales of second-hand motor vehicles (**Second-hand Vehicles Business**) in Hong Kong. It started a money lending business (**Money Lending Business**) two years ago. These businesses were operated by a small number of employees. 2. Over the past five years, the Second-hand Vehicles Business had diminished substantially, with its revenue dropped by 95% to less than HK$5 million. The Group had recorded net losses and negative operating cashflows. As at the latest financial year end, the Group had total assets and net assets of HK$50 million and HK$40 million respectively. 3. Company A would cease the Second-hand Vehicles Business and reallocate its resources to wholesale distribution of new branded motor vehicles in the PRC (**Vehicles Wholesale Business**). The Money Lending Business would continue to generate minimal revenue. 4. Company A submitted that it was able to satisfy Rule 13.24 because: (a) The Group commenced the Vehicles Wholesale Business following the relaxation of relevant PRC regulation a few months ago. It sourced new branded motor vehicles in fleet from overseas suppliers and sold them to a small number of car dealers in the PRC on an indent basis.

(b) According to Company A's forecasts, the Vehicles Wholesale Business would significantly increase its revenue for the second half of the current financial year. This was based on a few confirmed orders, non-legally binding framework agreements with a few customers, and an assumption about the average monthly increase in the sales volume during the forecast periods (for which Company A did not provide a clear basis). Company A expected to incur a loss for the current financial year and only record a minimal profit in the next financial year.

Decision

5. The Exchange considered that Company A had failed to comply with Rule 13.24 because:

(a) The Group's existing level of operations had, for years, remained very low and recorded net losses and negative operating cashflows. It would cease the Second-hand Vehicles Business and did not expect the Money Lending Business to grow substantially in the future.

(b) Company A sought to rely on the Vehicles Wholesale Business and its revenue forecasts for the next two financial years to meet Rule 13.24. However, the Exchange noted that:

- The Vehicles Wholesale Business had a short operating history and a limited customer base. Its business model was substantially different from that of the Second-hand Vehicles Business. The Vehicles Wholesale Business was a business of wholesale distribution of new branded motor vehicles in the PRC conducted on an indent basis relying on a small number of car dealers, compared to the Second-hand Vehicles Business involving retail sales in Hong Kong of second-hand motor vehicles selected and acquired by Company A.

- A significant portion of the revenue projections from the Vehicles Wholesale Business was based on non-legally binding framework agreements and assumptions which were not supported by signed agreements or committed sales orders.

- Without a track record of performance, a reliable customer base and credible financial projections, the Vehicles Wholesale Business was not demonstrated to be viable and sustainable.

(c) The Group's assets comprised mainly cash, and trade and other receivables. As noted above, the operation of these assets did not generate sufficient revenue and profits to support a continued listing.

Case 3 GEM Rule 17.26	**Background** 1. Company A and it subsidiary (**Group**) were originally engaged in trading of metals and beverage products. It also held exploration rights of iron mines. It had been loss making for many years. 2. About six months ago, Company A: (a) failed to renew the exploration rights of iron mines and fully impaired its mining assets of about HK$150 million; (b) discontinued its metal trading business which was the Group's main business and generated 90% of its revenue (about HK$12 million) in the last financial year; and (c) started a number of new businesses including trading of cosmetics and skincare products, stainless steel wire, nephrite, listed securities and chartering of vessel (**New Businesses**). The New Businesses had no correlation with each other. They were mostly trading businesses relying on one to two customers and each operated by a small number of employees. 3. The remaining beverage trading business and the New Businesses together generated revenue of HK$30 million in the last six months. The Group recorded a gross profit of HK$6 million, which was insufficient to cover its expenses, resulting in a net loss of HK$60 million. It had net liabilities amounted to HK$400 million. 4. Company A was of the view that it was able to meet GEM Rule 17.26. It submitted that: (a) the New Businesses would enable the expansion of its business portfolio, diversify its income sources and enhance its financial performance; (b) its revenue had increased to HK$50 million for the first nine months of the current financial year. The performance of the New Businesses was in line with the management's projection; and (c) based on its financial forecast, the Group would continue to maintain growth in revenue from the New Businesses and exercise effective control over its corporate expenses. It expected to record revenue of about HK$100 million and a substantial loss in the coming 12 months.

	Decision 5. The Exchange considered that Company A had failed to comply with GEM Rule 17.26 because: (a) The Group had substantially ceased all its principal businesses after discontinuing the metal trading business. The remaining business in trading of beverage products recorded minimal revenue and a segment loss. (b) Company A failed to demonstrate the viability and sustainability of the New Businesses: ▪ The New Businesses had no correlation with each other and involved a low level of activities. They were mostly trading businesses relying on a few customers and suppliers and operated by a few employees. In the last six months, it generated minimal revenue which was insufficient to cover its expenses. Despite its projection of an increase in revenue, the Group would continue to record a substantial loss during the forecast period. ▪ Company A had not provided any concrete business plan for the New Businesses or otherwise demonstrated the prospects of substantially improving the scale of its operations. (c) The Group had a significant net liabilities position. As noted above, the operation of its assets did not generate sufficient revenue and profits to support a continued listing.
Case 4 Rule 13.24	**Background** 1. Company A and its subsidiary (**Group**) were principally engaged in the manufacturing and sale of fashion accessories (**Fashion Accessories Business**) and the development and sale of software related applications (**Software Business**). 2. Over the past few years, the Group had gradually scaled down the Fashion Accessories Business by disposing of its manufacturing arms, outsourcing such function to other subcontractors, and closing its retails shops. Revenues from this business segment decreased from about HK$200 million to HK$9 million during the last five financial years. Company A had decided to discontinue this business, and the revenue of HK$9 million in the latest financial year was mostly generated from the sale of obsolete inventories. 3. Company A started the Software Business through its acquisition of a company (**Acquisition**) engaging in such business about a year ago. It was noted that:

(a) In the latest financial year, the Group recorded revenue of around HK$6 million from this business and an impairment loss of HK$9 million on goodwill arising from the Acquisition. As at the latest year end date, the Group had total assets of HK$280 million which included (i) goodwill of HK$140 million arising from the Acquisition; (ii) a deposit of HK$31 million paid for the acquisition of certain trademarks relating to the Fashion Accessories Business under an agreement signed two years ago; and (iii) cash and trade receivables.

(b) The Group's auditor had issued a disclaimer opinion on the Group's financial statements due to, among others, issues concerning the revenue recorded from the Software Business and the carrying value of the goodwill. In particular, the auditor had raised concern about the carrying value and recoverability of the goodwill having considered the short history of the Software Business, the difficulties faced by the management in executing the business plan and the lack of supporting information relating to the revenue from this business. Further, there was insufficient evidence to satisfy the auditors as to the recoverability of the deposit paid for the acquisition of trademarks.

(c) Towards the end of the latest financial year, all the staff for the development team of the Software Business left their employment, resulting in suspension of its operation. The operation resumed only after new staff were recruited three months later.

4. Company A submitted that it had plans to improve its business operations:

(a) The Group had entered into sales contracts of about HK$16 million for the Software Business and was in discussion with potential customers on new contracts of HK$6 million. Company A expected a significant increase in revenues from this business to HK$23 million and HK$35 million in the current and the next financial year respectively, but did not provide details or basis for its business plans or forecasts.

(b) Company A also planned to commence certain regulated activities under the Securities and Futures Ordinance (**Securities Business**). It expected to obtain the relevant licenses within 3 months and record revenue of about HK$2.5 million from this business in the next financial year.

(c) Based on the above, Company A expected that it would record net profits of about HK$2 million and HK$16 million in the current and next financial year respectively.

	Decision 5. The Exchange considered that Company A had failed to comply with Rule 13.24 because: (a) Company A had a low level of operations. Its original Fashion Accessories Business had diminished substantially, causing the Group to record losses and negative operating cashflows in each of the last five years. Company A had decided to discontinue this business. (b) Company A failed to demonstrate the viability and sustainability of its new businesses: ▪ The Software Business had a short operating history. It generated minimal revenue of HK$6 million in the latest financial year, which was insufficient to cover the corporate expenses. ▪ Company A expected to record total revenue of HK$58 million from the Software Business in the current and next financial years, of which Company A had entered into sale contacts of HK$16 million only. Company A had not provided any details of its business plans to support a substantial increase in the scale of operations of the Software Business as projected. ▪ The Securities Business was still in at the planning stage and had not commenced operations. Based on Company A's projection, even if the business would proceed to operate as planned, it would generate revenue of HK$2.5 million only in the next financial year. (c) The Group's auditors had raised concerns about the recoverability of the goodwill relating to the Software Business and the deposit paid for acquisition of trademarks, which accounted for a majority of its assets. As noted above, Company A failed to demonstrate that it had sufficient assets to support the operation of a viable and sustainable business.
Case 5 Rule 13.24	**Background** 1. Company A and its subsidiaries (**Group**) were engaged in the manufacturing and distribution of multimedia and communication products. 2. Subsidiary B, a major operating subsidiary of Company A, was engaged in the manufacturing and distribution of communication products of a major brand of Company A (**Disposal Business**). It accounted for about 90% and 75% of the Group's revenue and assets. It was loss making in the latest financial year and recorded a profit of over HK$30 million in each of the past few years.

3. Company A and Mr. X (the controlling shareholder of Company A) proposed to enter into the following transactions:

   (a) Company A would sell Subsidiary B to Mr. X for cash (**Disposal**).

   (b) Mr. X would sell his entire shareholding in Company A to Mr. Y who would then make an offer to acquire all the remaining shares in Company A from other shareholders. This transaction was conditional on the completion of the Disposal.

4. Upon completion of the Disposal, Company A would continue its existing business in the manufacturing and distribution of multimedia and communication products, excluding the product line owned by Subsidiary B (**Remaining Business**).

5. Company A submitted that the product line of Subsidiary B was loss making and the Disposal would allow it to focus on other product lines with better prospect and more profitable. Company A would use the proceeds from the Disposal as general working capital and for future business opportunities.

6. Company A was of the view that it would be able to meet Rule 13.24 upon completion of the Disposal because:

   (a) The Remaining Business comprised distinct product lines and operated independently from the Disposal Business with its own manufacturing and distribution teams. It recorded revenue and profit of over HK$200 million and HK$4 million for the latest financial year. Based on Company A's profit forecast, the Remaining Business would continue to record profit and grow steadily.

   (b) Upon the Disposal, Company A would have total assets of about HK$450 million, including trade and other receivables, cash, inventories, fixed assets and trademark.

   (c) The Disposal would improve Company A's financial performance by disposing of the loss making business.

Decision

7. The Disposal formed part of the arrangements between Mr. X and Mr. Y and was made to facilitate the sale of a controlling interest in Company A.[1] Company A had been engaged in the Disposal Business and Remaining Business since its listing on the Exchange. The Disposal Business accounted for the bulk of Company A's existing businesses and had been profitable in the past except in the latest financial year. The Exchange considered that Company A would not meet Rule 13.24 upon completion of the Disposal because:

	(a) While Company A asserted that the Disposal would improve its financial performance, it failed to support its case or demonstrate that the Remaining Business was viable and sustainable. The Remaining Business only consisted of minor brands which were historically loss making and recorded a minimal profit in the latest financial year. It did not generate sufficient revenue and profits to justify a listing. The profit forecast submitted by Company A also failed to show substantial improvement in its operations and financial performance after the Disposal. (b) The assets of the Remaining Business mainly included trade and other receivables, cash, inventories, fixed assets and trademark. As noted above, the operation of these assets did not generate sufficient revenue and profits to justify a continued listing. The other asset of Company A would be the cash proceeds from the Disposal, but it failed to demonstrate how the cash retained by it would enable it to substantially improve its operations. *Note 1: Rule 14.06E (which restricts an issuer from disposing of all or a material part of its existing business at the time of, or within 36 months from, a change in control) would also apply in the circumstances described in this case.*
Case 6 Rule 13.24	**Background** 1. Company A was principally engaged in event operation and entertainment business through Subsidiary B (a major subsidiary of Company A in terms of operations and assets). 2. Company A proposed to (i) sell a 25% interest in Subsidiary B to Company C (**Disposal**); and (ii) grant a call option (**Call Option**) to Company C over the remaining 75% interest in Subsidiary B upon completion of the Disposal. 3. Company A was of the view that it would be able to meet Rule 13.24 upon completion of the proposal (i.e. the Disposal and the grant of the Call Option) because: (a) Until and unless Company C exercised the Call Option, Company A would continue to control Subsidiary B and therefore its business operations and assets. (b) The Call Option was not exercisable until 24 months after the Disposal. By the time it was exercised, Company A would have been expanded into other businesses.

	Decision 4. The Exchange considered that Company A would not meet Rule 13.24 upon completion of the proposal because: (a) Company A's business operations and assets were primarily carried out and held through Subsidiary B. (b) The exercise of the Call Option was entirely at Company C's discretion. By granting the Call Option, Company A was prepared to lose its ownership and control over Subsidiary B. As Company A had no other material business operations or assets, it would no longer be suitable for listing upon completion of the proposal. Whether and when Company C would exercise the Call Option was irrelevant. (c) Company A stated its intention to carry out other businesses, but it could not demonstrate that it would have a new business suitable for listing upon completion of the proposal.
Case 7 Rule 13.24	**Background** 1. Company A and its subsidiaries (**Group**) were engaged in the property construction and related business (**Construction Business**) since its listing on the Exchange. Since last year, the Group had diversified into property management business (**Property Business**) and trading of financial products (**Trading Business**). 2. Company A proposed to sell the Construction Business to Mr. X (**Disposal**). Mr. X was a director of certain subsidiaries of Company A that carried on the Construction Business. He ceased to be Company A's controlling shareholder about three years ago when he sold his entire interest in Company A to the existing controlling shareholder. 3. Company A submitted that the Construction Business had been loss making in the last two years, and the Disposal would allow it to diversify into other businesses with growth potential. The sale proceed would be used by the Group as general working capital. 4. The Disposal would reduce the Group's revenue and assets by about 70%. Company A submitted that it would be able to meet Rule 13.24 upon completion of the Disposal because: (a) The Group would continue to carry out the Property Business and the Trading Business (together, **Remaining Businesses**).

(b) The Property Business involved the provision of management services to a number of small-scale property developers in the PRC and would provide a stable source of income to the Group in the coming years. The Group recorded minimal revenue and a segment loss from the Property Business in the last financial year because it only acquired this business for a few months. Company A expected the Property Business to generate revenue of about HK$20 million and a segment profit of over HK$10 million in the current financial year.

(c) Company A commenced the Trading Business last year and recorded revenue and a segment profit of over HK$500 million and HK$1 million. This business was expected to double its revenue and segment profit in the current financial year.

(d) Company A also held a residential property overseas (**Property**) with a book value of about HK$20 million. It planned to re-develop the Property for re-sale.

Decision

5. The Exchange considered that Company A would not meet Rule 13.24 upon completion of the Disposal because:

(a) The Disposal would substantially reduce the Group's scale of operations and assets. After the Disposal, the Group would be left with the Remaining Businesses that were acquired or established for less than one year. These businesses recorded a loss or minimal profit in the latest financial year. Based on Company A's projections in the current year, the Property Business would record revenue of HK$20 million and a segment profit of HK$10 million only. The segment profit from the Trading Business would also be minimal as it was only trading products on an indent basis with a very low profit margin. The scale of the Remaining Businesses was insufficient to justify a listing.

(b) While Company A asserted its intention to re-develop the Property, there was no detail about the re-development plan. Company A failed to demonstrate how it could substantially improve the Group's operations and financial performance after the Disposal.

(c) The assets of the Remaining Businesses were mainly cash, trade receivables and the Property. As mentioned in above, the operations of these assets could not generate sufficient revenue and profits to justify a listing.

Case 8 Rule 13.24	**Background** 1. Company A and its subsidiaries (**Group**) had been engaged in the manufacturing and sale of packaging products (**Packaging Business**) since its initial listing on the Exchange in 20x1. The Packaging Business accounted for the Group's entire revenue and net profit until Company A acquired a company (**Subsidiary B**), which operated an advisory business (**Advisory Business**), from Mr. X in November 20x6. 2. Before acquired by Company A, Subsidiary B recorded minimal revenue of HK$3 million for the 30 months from January 20x4 to June 20x6. This revenue was generated from providing corporate secretarial services. Subsidiary B recorded net losses and net liabilities in 20x4 and 20x5. 3. Subsidiary B's revenue increased significantly from July 20x6 onwards. For the 10 months between July 20x6 and April 20x7, it recorded total revenue of approximately HK$230 million, resulting in a net profit of HK$48 million for 20x6 and HK$19 million for the first four months in 20x7. Of such revenue of HK$230 million, only 2% was generated from recurring corporate secretarial services with the remaining 98% generated from different types of new services, mostly non-recurring in nature, including advice on financial accounting, valuation, merger and acquisition, loan referral, property agency, project agency and strategic planning. Of such revenue of HK$230 million, 70% was derived from one transaction with one client whilst 10% was derived from another transaction with the second largest client. 4. In April 20x7 Company A proposed to sell the Packaging Business to an independent third party (**Disposal**) as the profitability of the Packaging Business had persistently decreased in the past three years. The sale proceeds would be used by the Group to settle its liabilities. 5. Company A submitted that the Group would meet Rule 13.24 upon completion of the Disposal because: (a) The Advisory Business had recorded substantial revenue and profits since July 20x6. (b) It had secured advisory contracts for over HK$50 million in the next two financial years which would ensure the stability and continuity of the Group's income stream. (c) The Advisory Business was a substantiable business. It had established relationship with a number of new clients through Mr. X's personal network and referrals by those new clients.

Decision

6. The Exchange considered that Company A would not meet Rule 13.24 upon completion of the Disposal. In particular, the Exchange questioned the viability and sustainability of the Advisory Business after considering:

   (a) The history of Company A's operation and management of the Advisory Business was very short (less than 6 months when the Disposal was proposed).

   (b) The Advisory Business recorded minimal revenue and net losses in previous years. While such business recorded a significant increase in revenue in recent months, it had a very small customer base and a large majority of the revenue was generated from one transaction. The Exchange was concerned with the substance of this transaction, and the work performed by Subsidiary B to earn the substantial fees and the basis of determination of such fees.

   (c) Company A failed to demonstrate the viability and sustainability of the Advisory Business given its limited customer base and heavy reliance on Mr. X to generate business and the questionable basis for the substantial fees from the transaction with one client.

   (d) After the Disposal, the Group's assets would mainly comprise the goodwill arising from the acquisition of the Advisory Business, a vacant property and some cash. As noted above, Company A failed to demonstrate that these assets could support the operation of a viable and sustainable business.

Note: Listing Review Committee decisions on Rule 13.24 also offer guidance on this subject.

6

Issue of securities or resale of treasury shares and related matters

6.1 Shareholders' mandate for issue of shares or resale of treasury shares

6.2 Highly dilutive issue of shares or resale of treasury shares

6.3 Large scale issues of securities

Guidance letter – Guidance on large scale issues of securities	GL105-19	6.3 – 1

6.4 Rights issue

Listing decision – Whether a proposed rights issue of shares with bonus warrants required independent shareholders' approval	LD113-1	6.4 – 1
Listing decision – Whether a proposed rights issue that would increase the listed issuer's market capitalisation by more than 50 per cent required independent shareholders' approval	LD71-2013	6.4 – 3
Listing decision – Whether the proposed rights issue by a PRC issuer under general mandate would be subject to the 20 per cent discount limit on issue price	LD25-2012	6.4 – 5
Listing decision – Whether a listed issuer's arrangements to dispose of the excess rights shares under a rights issue were made on a fair basis	LD70-2013	6.4 – 8
Frequently asked questions – Rights issue	FAQ6.4 – No.1	6.4 – 10

6.5 Placing

Listing decision – Whether the Exchange would grant listing approval for a placing of new shares if there was a leakage of inside information before the announcement of the placing	LD10-1	6.5 – 1
Frequently asked questions – Placing	FAQ6.5 – No.1-4	6.5 – 2

6.6 Issue of convertible securities

Guidance letter – Guidance on the issue of convertible securities by listed issuers	GL80-15	6.6 – 1
Listing decision – Whether the Exchange would give consent to a listed issuer under Rule 10.06(3)(a) for share buyback to be conducted concurrently with its convertible bond offering	LD139-2025	6.6 – 6

Listing decision – Whether the Exchange would grant listing approval for new shares to be issued by a listed issuer upon conversion of convertible notes that could result in the listed issuer's public float falling below the minimum requirement	LD56-2013	6.6 – 9
Listing decision – Whether the Exchange would approve the proposed changes to the terms of convertible bonds issued by a listed issuer under general mandate	LD54-2013	6.6 – 11
Listing decision – Whether an issue of convertible non-voting redeemable preference shares should be treated as an issue of equity or debt instruments	LD7-3	6.6 – 15

6.7 Issue of warrants

Listing decision – Whether the Exchange would grant waiver for a warrant to be issued by a listed issuer in connection with its offering of equity-linked securities	LD140-2025	6.7 – 1
Listing decision – In respect of a proposed rights issue of shares with bonus warrants, whether the Exchange would waive the requirements on the number and spread of warrantholders at the time of listing of the warrants	LD83-2014	6.7 – 4
Listing decision – Whether Chapter 15 applies to unlisted warrants	LD20-2	6.7 – 6
Listing decision – Whether a listed issuer could issue convertible debentures with warrants while it had used up the 20 per cent warrant limit at the date of the agreement for the issue	LD5-2	6.7 – 7
Frequently asked questions – Issue of warrants	FAQ6.7 – No.1	6.7 – 9

6.8 Bonus issue / share subdivision

Guidance letter – Guidance on bonus issues of shares	GL88-16	6.8 – 1
Listing decision – Whether the Exchange would approve the proposed share subdivision and increase in board lot size shortly after the listed issuer completed a rights issue and a share consolidation	LD103-2016	6.8 – 4

6.9 Authorisation for prospectus registration

Guidance letter – Guidance on the electronic submission of prospectus and accompanying documents to the Exchange and the Companies Registry for authorisation and registration	GL118-23	6.9 – 1

6.10 Full circulation

Frequently asked questions – Conversion of PRC issuers' unlisted shares into H shares for listing on the Exchange	FAQ6.10 – No.1	6.10 – 1

Whether a listed issuer could seek a prior mandate from its shareholders for a proposed placing of new shares to finance an acquisition

Facts

1. A Main Board issuer (**Company X**) entered into a very substantial acquisition of a target engaged in natural resources exploitation. The consideration would be in cash, consideration shares and convertible securities.

2. It proposed to raise funds to finance the acquisition and the target's business by issuing new shares to independent placees (the **Placing**). It was discussing this with placing agents but had yet to enter into any agreement for the Placing.

3. To facilitate the fund raising exercise, Company X proposed to seek a specific mandate from its shareholders for the Placing at the same general meeting to consider the acquisition. The Placing would be made under the following framework:

   a. There was a limit on the number of shares to be issued, which represented approximately 35% of Company X's then issued share capital.

   b. The issue price would be determined on an arm's length basis with reference to the prevailing market conditions. In any event, it would be no less than the higher of:

      - a fixed amount; and
      - 80% of the higher of (i) the market price of the shares on the date of the relevant placing agreement; and (ii) the average market price of the shares for 5 trading days immediately before the Placing.

   c. Over 90% of the net proceeds were to be assigned to (i) settle the cash consideration for the acquisition; and (ii) finance the target's capital expenditure and specific expenses. Any remaining proceeds would be used for the target's working capital.

   d. Given the estimated time for Company X to negotiate and conclude the placing agreement and the timetable for the acquisition, the specific mandate was proposed to last three months.

Relevant Listing Rules

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

...

(2) the issue and marketing of securities is conducted in a fair and orderly manner and that potential investors are given sufficient information to enable them to make a properly informed assessment of an issuer … ;

(3) …

(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; and

(6) all new issues of equity securities by a listed issuer are first offered to the existing shareholders by way of rights unless they have agreed otherwise.

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;

…

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).

(b) …

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

(a) …

(b) If, … 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 …

…

(3) A general mandate given under rule 13.36(2) shall only continue in force until:

(a) the conclusion of the first annual general meeting of the issuer following the passing of the resolution at which time it shall lapse unless, by ordinary resolution passed at that meeting, the mandate is renewed, either unconditionally or subject to conditions; or

(b) revoked or varied by ordinary resolution of the shareholders in general meeting, whichever occurs first.

…

(Rules 2.03 and 13.36 were amended on 11 June 2024. See Note below.)

Analysis

6. Under the Rules, a shareholder should be able to protect his proportion of total equity by having the opportunity to subscribe for any new issue of equity securities, unless shareholders otherwise permit. The pre-emptive rights may be waived by shareholders on a general basis but only under Rules 13.36(2) and (3) (i.e. a general mandate) which restrict the size and price for the new shares that can be issued.

7. Accordingly, any proposal to issue new shares which exceed the limits of Rule 13.36(2) should be considered by shareholders on a case by case basis under Rule 13.36(1). In seeking the specific approval, the issuer must give shareholders sufficient information to enable them to make an informed assessment of the issue. The Exchange would not grant listing approval for the new shares if the mandate is in substance a "general" one and a means to circumvent Rule 13.36(2).

8. Here, Company X proposed to seek a mandate for the Placing with a specific purpose, i.e. to finance the acquisition and the target's business development. While Company X had yet to enter into any placing agreement, it had taken reasonable steps to ensure that sufficient information about the Placing would be provided to its shareholders to make an informed assessment, including the framework for determining the terms of the Placing and the specific use of proceeds. The case could be distinguished from a general mandate, which should follow the requirements under Rule 13.36(2).

Conclusion

9. The proposed specific mandate for the Placing would meet Rule 13.36(1)(a).

Note: Rules 2.03 and 13.36 were amended on 11 June 2024 to, among others, (i) apply the existing requirements for an issue of new shares to a resale of treasury shares; and (ii) exclude treasury shares in the calculation of issued shares for the purpose of determining the general mandate limit. The Rule amendments would not change the analysis and conclusion in this case.

Whether a listed issuer could seek a prior mandate from its shareholders for a proposed rights issue to finance an acquisition

Parties

- **Company A** – a Main Board issuer
- **Parent Company** – a state-owned enterprise, and Company A's controlling shareholder

Facts

1. Company A signed an agreement to acquire a target from the Parent Company for cash consideration. It was a very substantial and connected acquisition subject to independent shareholders' approval.

2. Company A would conduct a rights issue to finance the acquisition and the target's business. It had not yet entered into any underwriting agreement(s) for the rights issue, but it expected that the right issue would increase its share capital by more than 50% and therefore require independent shareholders' approval under Rules 7.19A(1) and 7.27A. The Parent Company intended to take up its entitlement to the rights shares.

3. As the Parent Company was a state-owned enterprise, the acquisition and the Parent Company's subscription of the rights shares were subject to the approval of Mainland regulatory authorities. Based on the legal advice, Company A should have obtained shareholders' approval for the rights issue before the parties could make formal applications to the Mainland regulatory authorities.

4. Company A submitted that it would be difficult to secure an underwriter and agree the terms of the rights issue before the general meeting given the uncertainty as to the additional time required to obtain the regulatory approval and the then market conditions. It enquired whether it could seek a mandate for the rights issue from the independent shareholders at the same general meeting to consider the acquisition. The rights issue would be made under the following framework:

    - the rights issue would be fully underwritten by independent licensed firm(s).
    - the number of rights shares and the issue price would be determined by the directors in consultation with the underwriter(s), taking into account the market conditions and the share trading price at the relevant time. In any event,
        - the basis of the rights issue would be up to one rights share for every existing share held; and

- the amount to be raised would fall within a range specified in the circular.

- the net proceeds would be used to settle the cash consideration for the acquisition. Any remaining balance would be assigned to finance the target's operations.

- there would be arrangement for shareholders to apply for excess rights shares.

5. The mandate was intended to last 12 months from the date it was approved by the independent shareholders, which would be in line with the long-stop date of the acquisition agreement.

Relevant Listing Rules

6. Rule 7.19A(1) states that

"A proposed rights issue must be made conditional on minority shareholders' approval in the manner set out in rule 7.27A if the proposed rights issue would increase either the number of issued shares or the market capitalization of the issuer by more than 50% (on its own or when aggregated with any other rights issue or open offers announced by the issuer …):-

…"

(Rule 7.19A(1) was amended on 11 June 2024. See Note below.)

7. Rule 7.27A states that

"Where minority shareholders' approval is required for a rights issue … under Rule 7.19A …:

(1) the rights issue … must be conditional on approval by shareholders in general meeting by a resolution on which any controlling shareholders and their associates or … shall abstain from voting in favour;

(2) …

(3) the issuer must set out in the circular to shareholders:

(a) the purpose of the proposed rights issue …, together with the total funds expected to be raised and a detailed breakdown and description of the proposed use of proceeds. …; and

(b) …"

Analysis

8. The purpose of Rule 7.19A(1) is to protect minority shareholders' interests when the potential dilution effect of a proposed rights issue (individually or together with any similar fund raising exercise(s) made in the previous 12 months) is material. In seeking the shareholders' approval, the issuer must provide sufficient information to enable shareholders to make an informed assessment of the rights issue, which normally include the number of rights shares and the issue price, and the principal terms of the underwriting agreement.

9. In this case, when considering whether to accept a prior mandate in lieu of a shareholders' approval on the terms of the rights issue, the Exchange noted that the rights issue was made with a specific purpose, i.e. to finance the acquisition and the target's business. Company A had taken reasonable steps to provide sufficient information about the rights issue to the independent shareholders to decide how to vote, including the purpose of the rights issue, its maximum dilution effect on shareholding, the amount to be raised, and details of the intended use of proceeds. The circular would also contain an independent financial adviser's opinion on the proposed right issue and its recommendation to the independent shareholders on how to vote.

10. However, the Exchange considered the proposed mandate period of 12 months was too long and unjustified. If the rights issue did not materialize within a reasonable period, independent shareholders should be given the opportunity to reconsider the proposal taking into account the company's circumstances and the market conditions at that time.

Conclusion

11. To address the Exchange's concern, Company A shortened the mandate period to 4 months having regard to the estimated timetable for obtaining the necessary regulatory approval for the acquisition, and the forthcoming long holidays in the Mainland.

Note: Rule 7.19A(1) was amended on 11 June 2024 to exclude treasury shares from the issuer's number of issued shares in determining whether the rights issue requires minority shareholders' approval. The Rule amendments would not change the analysis and conclusion in this case.

Whether a listed issuer could seek a prior mandate from its shareholders to issue new shares over a period of time under a share issuance proposal

Facts

1. A GEM issuer (**Company X**) entered with an independent investment fund a "share subscription facility" arrangement (**Facility**). Under the Facility, Company X might request the fund to subscribe for new shares in Company X from time to time over a three-year period.

2. The new shares would be issued at a 10% discount to Company X's share price over the ten trading days following the request, subject to a fixed minimum price. The maximum number of shares issuable under the Facility was approximately two times Company X's existing issued shares. Company X intended to utilize the proceeds for debt repayment, acquisitions of new businesses and expansion of existing businesses.

3. Company X proposed to seek a one-off advance mandate from its shareholders to issue new shares under the Facility over the next three years under GEM Rule 17.39. Company X represented that the Facility would allow it to have control throughout the three-year period as to when and how to draw down the Facility under specified limits.

Relevant Listing Rules

4. GEM Rule 17.39 states that:

   Except in the circumstances mentioned in rule 17.41, the directors of an issuer (other than a PRC issuer, to which the provisions of rule 25.23 apply) shall obtain the consent of shareholders in general meeting prior to allotting, issuing or granting: -

   (1) shares;

   …

   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 17.41 and 17.42."

5. GEM Rule 17.41 states that:

   No such consent as is referred to in rule 17.39 shall be required:

   (1) …

   (2) if,... 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...

6. GEM Rule 17.42 states that:

   A general mandate given under rule 17.41(2) shall only continue in force until:

   (1) the conclusion of the first annual general meeting of the issuer following the passing of the resolution at which time it shall lapse unless, by ordinary resolution passed at that meeting, the mandate is renewed, either unconditionally or subject to conditions; or

   (2) revoked or varied by ordinary resolution of the shareholders in general meeting, whichever occurs first.

7. GEM Rule 17.42B states that:

   In the case of a placing or open offer of securities for cash consideration, the issuer may not issue any securities pursuant to general mandate given under rule 17.41(2) if the relevant price represents a discount of 20% or more to the benchmarked prices of the securities, such benchmarked price being the higher of:…

   (GEM Rules 17.39, 17.41 and 17.42B were amended on 11 June 2024. See Note below.)

Analysis

8. Under GEM Rule 17.39, a shareholder should be able to protect his proportion of total equity by having the opportunity to subscribe for all new issues of equity securities. This pre-emptive right may be waived by shareholders themselves on a general basis but only within the limits of GEM Rules 17.41 and 17.42 (these rules describe a general mandate and allow share issuance subject to limits on the number of new shares and other restrictions such as price limits).

9. Accordingly, any issuance of new shares which exceeds the limits of GEM Rule 17.41(2) should be approved by shareholders on each occasion of share issuance under GEM Rule 17.39. The Exchange would not grant listing approval for the new shares if the mandate is in substance a "general" one and yet does not meet the requirements set out in GEM Rules 17.41(2) and 17.42B.

10. In this case, Company X proposed to seek a prior mandate from its shareholders for the possible issuance of new shares under the Facility. The prior mandate would give the directors the discretion to issue new shares under the Facility from time to time, with the size and issue price for each share issuance to be determined as and when Company X exercised its rights under the Facility. However, this mandate did not meet the size and price limits set out in GEM Rules 17.41(2) and 17.42B.

Conclusion

11. Company X cannot seek a prior mandate for the Facility on a one-off basis.

12. Company X subsequently announced that it would issue new shares under the Facility using the general mandate available at the time of each issuance.

Note: GEM Rules 17.39, 17.41 and 17.42B were amended and/or modified by GEM Rule 17.39A on 11 June 2024 to, among others, (i) apply the existing requirements for an issue of new shares to a resale of treasury shares; and (ii) exclude treasury shares in the calculation of issued shares for the purpose of determining the general mandate limit. The Rule amendments would not change the analysis and conclusion in this case.

Shareholders' mandate for issue of shares or resale of treasury shares

1. A listed issuer proposes to seek shareholders' approval for a bonus issue of shares at the forthcoming annual general meeting. Can the listed issuer take into account such bonus issue when determining the maximum number of shares that are allowed to be issued, or sold or transferred out of treasury under a new general mandate proposed at the same general meeting?

No, because the bonus shares are not yet issued at the time when the listed issuer seeks shareholders' approval for the new general mandate.

MB Rule 13.36(2)(b)
GEM Rule 17.41(2)
First released: November 2008; last updated: June 2024

2. Please explain the top-up arrangement for refreshment of general mandate after a pre-emptive issue of securities.

A listed issuer may seek shareholders' approval to top-up the unused portion of its previous general mandate based on the number of enlarged issued shares (excluding treasury shares). They can top up to the number of shares so that, in percentage terms, the unused part of the general mandate before and after the pre-emptive issue of securities is the same.

Example:
Existing issued shares (excluding treasury shares):
100,000 shares
General mandate before placing:
20,000 shares (20%)
Placing of shares under the general mandate:
5,000 shares
Issued shares (excluding treasury shares) after placing:
105,000 shares
Unused general mandate:
15,000 shares (15% of 100,000 shares)

New shares issued under a 1 for 2 rights issue:
52,500 shares
Issued shares (excluding treasury shares) after right issue:
157,500 shares

Shareholders' approval will be required to top-up the general mandate from 15,000 to 23,625 shares (15% of 157,500 shares). Independent shareholders' approval will be required for an additional mandate for 7,875 shares (i.e. 5% of 157,500 shares).

MB Rule 13.36(4)(e)
GEM Rule 17.42A(5)
First released: March 2004; last updated: June 2024

3. Does the price discount limit under MB Rule 13.36(5) / GEM Rule 17.42B apply if a listed issuer proposes to issue new shares or resell treasury shares under a general mandate to settle the amount due to a creditor?

Yes. The proposal is in substance an issue of new shares or a resale of treasury shares for cash consideration.

MB Rule 13.36(5)
GEM Rule 17.42B
First released: November 2008; last updated: June 2024

4. For a placing of new shares on a best effort basis under general mandate, is the listed issuer required to re-comply with the pricing requirement under MB Rule 13.36(5) / GEM Rule 17.42B if it extends the long stop date of the original agreement to give the placing agent additional time to procure potential investors to take up the new shares?

Yes. Such extension would constitute a material change to the original agreement and the listed issuer must ensure that the placing price could meet the pricing requirement with reference to the benchmarked price of the shares at the time of the extension.

MB Rule 13.36(5)
GEM Rule 17.42B
First released: May 2024

Whether there were exceptional circumstances for a listed issuer to conduct a highly dilutive issuance of shares

Facts

1. A Main Board issuer (**Company A**) and its subsidiaries (together, **Group**) were principally engaged in the provision of energy saving products and related services. Mr. X was the founder of the Group and had been the single largest shareholder and executive director of Company A since listing.

2. Company A was in financial difficulties. It proposed to repay part of its overdue indebtedness by issuing new shares to Mr. X to raise funds, and to certain creditors to settle the amounts owed to them (together, **Proposed Issue**). The theoretical dilution of the Proposed Issue was over 25%.

3. The Proposed Issue was subject to independent shareholders' approval. Upon completion of the issue, Mr. X's shareholding in Company A would increase from 10% to over 50%.[1] Company A would continue to operate its existing business under the same management.

4. Company A submitted that the high shareholder's value dilution was exceptional and justified in the circumstances:

   (a) The Group did not have sufficient funds to repay overdue indebtedness as its business performance and financial position deteriorated in the past two years due to the change in market conditions and the outbreak of COVID-19. The Group had received statutory demands for repayment from some of the creditors. Its auditor had issued a disclaimer of opinion on its financial statements due to the going concern issue.

   (b) The Proposed Issue formed part of the rescue plan of the Group. With part of the indebtedness to be repaid by the Group using the proceeds from the Proposed Issue, its creditors had conditionally agreed with the principal terms of a scheme of arrangement to settle the remaining indebtedness. Company A was also in discussion with a financing company for a loan facility to support its business operations, subject to the completion of the Proposed Issue.

   (c) Company A had explored other fundraising means but these attempts failed due to its deteriorated financial position. The rescue plan would substantially improve its financial position and provide sufficient working capital to the Group for at least the next 12 months.

[1] Mr. X also applied for whitewash waiver pursuant to Note 1 on dispensation from Rule 26 of the Code on Takeovers and Mergers.

Relevant Listing Rules

5. Rule 7.27B states that:

"A listed issuer may not undertake a rights issue, open offer or specific mandate placing that would result in a theoretical dilution effect of 25% or more…unless the issuer can satisfy the Exchange that there are exceptional circumstances (for examples, the issuer is in financial difficulties and the proposed issue forms part of the rescue proposal)…"

6. Rule 7.27B became effective in July 2018. As explained in the Exchange's Consultation Paper and Conclusions on Capital Raisings by Listed Issuers:

- The Rule was introduced to address concerns about abuses of highly dilutive capital raising transactions to the detriment of minority shareholders. Some highly dilutive issues lacked demonstrable commercial rationale and resulted in the introduction of new controlling or substantial shareholders. This raised questions on whether they were for the purpose of facilitating other activities, rather than to meet the issuers' capital requirements. In many of these cases, there was no pressing funding need to justify such a high level of value dilution and the directors could not clearly explain how the high value dilution was in the interests of the shareholders.

- The Rule is not intended to restrict legitimate capital raisings. There is an exemption for issues in "exceptional circumstances" where the highly dilutive terms are justified by particular circumstances. This applies to an issuer who is in financial difficulties and the proposed issue forms part of its rescue proposal.

Analysis

7. In this case, the Exchange was satisfied that there were exceptional circumstances for Company A to undertake the Proposed Issue. Based on Company A's submission, the Group was in financial difficulties and had a pressing funding need. Company A had demonstrated that it had exhausted other fundraising means and the Proposed Issue was in the interests of Company A and its shareholders as a whole. The Proposed Issue formed part of the rescue plan of the Group to settle overdue indebtedness and support its business operations.

Conclusion

8. Company A had demonstrated that there were exceptional circumstances for it to undertake the Proposed Issue under Rule 7.27B.

Highly dilutive issue of shares or resale of treasury shares

1. How should a listed issuer calculate the value dilution for a series of rights issues and specific mandate placing?

The cumulative value dilution is calculated by reference to (i) the aggregate number of shares issued or sold or transferred out of treasury during the 12-month period, compared to the number of issued shares (excluding treasury shares) immediately prior to the first offer or placing; and (ii) the weighted average of the price discounts (each price discount is measured against the market price of shares at the time of the offer).

For example, a listed issuer conducted the following capital raisings:
(i) a 1-for-2 rights issue with offer price at a price discount of 25%;
(ii) a 1-for-1 rights issue with offer price at a price discount of 40%; and
(iii) a specific mandate placing of 50% of existing issued shares (excluding treasury shares) at a price discount of 70%.

Theoretical value dilution of each pre-emptive offer / placing		**Rights issue August 2018**	**Rights issue November 2018**	**Placing March 2019**
No. of issued shares (excluding treasury shares) before capital raising	*A*	100	150	300
Issue size	*B*	50%	100%	50%
Number of offer/placing shares to be issued or sold or transferred out of treasury	*C = A x B*	50	150	150
Benchmarked price	*X*	HK$1.0	HK$0.92	HK$0.73
Price discount	*Y*	25%	40%	70%
Offer / placing price	*Z = X x (1-Y)*	HK$0.75	HK$0.55	HK$0.22
Shareholding value before rights issue / placing	*J = A x X*	HK$100.00	HK$137.50	HK$220.00
Subscription amount	*K = C x Z*	HK$37.50	HK$82.50	HK$33.00
No. of enlarged issued shares (excluding treasury shares)	*L = A + C*	150	300	450
Theoretical ex-price	*TEP = (J + K) / L*	HK$0.92	HK$0.73	HK$0.56
Theoretical value dilution	*TD = (TEP – X) / X*	**-8.3%**	**-20.0%**	**-23.3%**

Cumulative theoretical value dilution		**Rights issue August 2018**	**Rights issue November 2018**	**Placing March 2019**
Shares in issue (excluding treasury shares) immediately before 12-month period	*Sh*	100	100	100
Benchmarked price immediately before 12-month period	*Pr*	HK$1.00	HK$1.00	HK$1.00
Number of offer/placing shares to be issued or sold or transferred out of treasury	*C*	50	150	150
Aggregated number of offer/placing shares (i.e. Sum of C)	***D***	**50**	**200**	**350**
Price discount	*Y*	25%	40%	70%
Average price discount (i.e. weighted average of Y by reference to C)	***R***	**25%**	**36%**	**51%**
Shareholding value before 1st rights issue	*M= Sh x Pr*	HK$100.00	HK$100.00	HK$100.00
Cumulative subscription amount	*N = D x [Pr x (1 – R)]*	HK$37.50	HK$128.00	HK$171.50
No. of enlarged issued shares (excluding treasury shares)	*L*	150	300	450
Cumulative theoretical ex-price	*CTEP = (M + N) / L*	HK$0.92	HK$0.76	HK$0.60
Cumulative theoretical value dilution	***CTD = (CTEP – Pr) / Pr***	**-8.3%**	**-24.3%**	**-39.7%**

The cumulative value dilution can also be calculated by the following formula:

$$\frac{(C_1 \times Y_1) + (C_2 \times Y_2) + \cdots + (C_n \times Y_n)}{Sh + C_1 + C_2 + \cdots + C_n}$$

Sh = *Number of issued shares (excluding treasury shares) immediately before the 1st offer or placing*
C_1 = *Number of shares to be issued or sold or transferred out of treasury in the 1st offer or placing*
C_2 = *Number of shares to be issued or sold or transferred out of treasury in the 2nd offer or placing*
C_n = *Number of shares to be issued or sold or transferred out of treasury in the nth offer or placing*
Y_1 = *Price discount of the 1st offer or placing*
Y_2 = *Price discount of the 2nd offer or placing*
Y_n = *Price discount of the nth offer or placing*

MB Rule 7.27B
GEM Rule 10.44A
First released: May 2018; last updated: June 2024

2. If a listed issuer proposes to issue rights shares at a premium over the market price, what is the theoretical dilution effect of this rights issue?

Where the offer price is at a premium over the market price, the theoretical dilution effect as computed under MB Rule 7.27B / GEM Rule 10.44A would produce a positive figure, i.e. there is no value dilution to non-participating shareholders.

MB Rule 7.27B
GEM Rule 10.44A
First released: May 2018; last updated: May 2024

3. How should a listed issuer calculate the theoretical dilution effect of a proposed placing of convertible bonds or warrants?

The theoretical dilution effect should be calculated on an as-converted basis, i.e. applying the initial conversion price (or the sum of the initial placing price and the exercise price) and the corresponding number of conversion shares (or subscription shares) for the calculation.

MB Rule 7.27B
GEM Rule 10.44A
First released: May 2018; last updated: May 2024

Guidance on large scale issues of securities

I. Background and purpose

1. This letter provides guidance on the application of Rule 14.06D to large scale issues of securities by listed issuers.

2. In recent years the prevalence of backdoor listings has resulted in a substantial increase in the value of listing status, leading to extensive activities related to investors acquiring control of listed issuers for their listing platforms (rather than the underlying businesses) for backdoor listing. In particular, there were some issuers proposing large scale issues of securities to new investors with an intention to use the injected funds to start new businesses unrelated to the issuers' original businesses. The investors would be in effect listing, through the listed issuers, new businesses that would not have otherwise met the new listing requirements. In December 2015, the Exchange issued Guidance Letter GL84-15 on the application of the cash company Rules[1] to restrict these large scale issues of securities.

3. As part of the recent Rule amendments (effective on 1 October 2019) to address backdoor listings and shell activities, the Exchange codified the practices set out in Guidance Letter GL84-15 into Rule 14.06D. This guidance letter supersedes GL84-15.

4. All Rule references in this letter are to the Main Board Listing Rules. As GEM Rule 19.06D is the same as Main Board Rule 14.06D, the guidance set out in this letter also applies to GEM issuers.

II. Relevant Listing Rules

5. Rule 14.06D state that:

"Where a listed issuer proposes a large scale issue of new securities (including any shares, warrants, options or convertible securities) for cash to acquire and/or develop a new business, which, in the opinion of the Exchange, is a means to circumvent the new listing requirements and to achieve a listing of that new business, the Exchange may refuse to grant listing approval for the shares to be issued.

Note: This rule is an anti-avoidance provision to prevent circumvention of the new listing requirements. It is intended to apply to a large scale issue of securities for cash proposed by a listed issuer where there is, or which will result in, a change in control or de facto control of the issuer (by reference to the factor set out in Note 1(e) to rule 14.06B), and the proceeds are to be used to acquire and/or develop a new business that is expected to be substantially larger than the issuer's existing principal business. The effect of the proposal is to achieve a listing of the new business that would not have otherwise met the new listing requirements."

[1] Rules 14.82 to 14.84

III. Guidance

6. Rule 14.06D is an anti-avoidance provision designed to prevent circumvention of new listing requirements through large scale equity fundraisings. When applying this Rule, the Exchange's approach is targeted towards large scale equity fundraisings that are made to facilitate investors in acquiring controls of the issuers for listing of new businesses that would not have otherwise met the new listing requirements.

Application of Rule 14.06D

7. Rule 14.06D is a purposive test and is assessed based on all relevant facts and circumstances of the issuer. This assessment is not simply based on the size of the equity fundraising proposed by the issuer, but also other factors including the nature and scale of the issuer's business and its financial position before the fundraising, its business plans and the intended use of proceeds, and whether there is, or will be, any change in control or de facto control of the issuer[2].

8. In general, an equity fundraising with the following characteristics would normally be caught under Rule 14.06D:

   (a) The size of the fundraising would be very significant to the issuer and would bear little or no correlation with the needs of the issuer's existing principal business.

   (b) Funds raised would be used largely in developing and/or acquiring a new business with little or no relation to the issuer's existing principal business. This would include circumstances where the issuer has started the new business shortly before the proposed fundraising (e.g. obtained a money lending license or acquired a small size money lending company).

   (c) Employing the cash obtained from the fundraising, the issuer would proceed to operate the new business which is expected to be substantially larger than the original business.

   (d) The investor would obtain control or de facto control of the issuer through the subscription of securities in the issuer. The effect is that the investor would obtain a listing platform for listing the new business. This is a circumvention of the new listing requirements as the lack of a track record would render such business unsuitable for listing.

   Two examples are set out in Part IV below.

[2] In making the assessment, the Exchange will consider whether there is any change in the controlling shareholder of the issuer, or any change in the single largest substantial shareholder who is able to exercise effective control over the issuer as indicated by factors such as a substantial change in its board and/or senior management. Where the case involves an issue of restricted convertible securities to the investor, the Exchange will consider whether in substance, the issue serves to allow the investor to effectively "control" the issuer. Please refer to Note 1(e) to Rule 14.06B and paragraphs 19 to 25 of Guidance Letter GL104-19 for details.

Other points to note

9. Rule 14.06D is not intended to restrict fundraising activities of issuers for legitimate business expansions or diversifications. As general guidance, the Rule will not normally apply to an issue of securities if, taking into account the proceeds from the issue[3], less than half of the issuer's assets would consist of cash as a result of the fundraising. Nevertheless, if the Exchange considers that any fundraising, acquisition or other corporate action of the issuer in the future together with the current fundraising are a means to list a new business that is not suitable for listing or otherwise circumvent the new listing requirements, the Exchange may exercise its discretion under Rule 2.04 to impose additional requirements or conditions on such future arrangement(s).

10. Further, the Exchange acknowledges that issuers engaging in asset-light businesses (for example, technology companies in the new economy sector) may have a cash to asset ratio exceeding 50% after fundraising activities. As set out in paragraph 7 above, the Exchange will consider all factors in totality when determining whether an issuer's proposed equity fundraisings is an attempt to circumvent the new listing requirements. The assessment is not simply an analysis of the cash to asset ratio of the issuer.

11. For the avoidance of doubt, the Exchange may apply the RTO Rule 14.06B when issuers use the funds raised for acquisitions of new businesses. This may be the case where an equity fundraising was not caught under Rule 14.06D (e.g. there was no change in control or de facto control of the issuer as a result of the fundraising) but the subsequent acquisition using the funds raised constitutes an attempt to circumvent the new listing requirements under the principle based test of Rule 14.06B.

Consultation with the Exchange

12. Listed issuers who intend to undertake large scale equity fundraisings are encouraged to contact the Exchange at the earliest possible opportunity to seek guidance on the application of Rule 14.06D in individual cases.

IV. Examples

13. In each of the following two examples, the Exchange considers that Rule 14.06D would apply to the proposed issue of securities.

Example 1

14. Company A is principally engaged in the garment business. It recorded revenue of about HK$60 million and a net loss of about HK$20 million in the latest financial year, and its total assets value was about HK$100 million.

15. The proposed subscriptions: Company A signed subscription agreements to raise a total of HK$400 million by issuing restricted convertible bonds[4] to subscribers:

[3] These include any proceeds that are intended to be used for specific purposes (whether by way of legally binding agreements or other commitments)

[4] Convertible bonds with a restriction from conversion to avoid triggering a change in control under the Code on Takeovers and Mergers.

- Upon completion, over 85% of the company's assets would consist of cash. The proceeds from the subscriptions would be mostly used to develop a new mobile game business.

- Assuming full conversion of the bonds, the conversion shares would represent about 4 times of the company's existing issued shares, and the major subscriber would hold more than 60% of the company's shares as enlarged by the conversion shares.

The major subscriber is an entrepreneur.

16. Immediately after signing the subscription agreements, Company A completed an acquisition of a newly set up company engaged in distributing and marketing mobile games. Taking this into account, Company A's cash would represent 65% of its total assets upon completion of the subscriptions.

17. The Exchange's analysis: The Exchange considers that Rule 14.06D would apply to the proposed subscriptions for the following reasons:

    (a) Under the proposal, the subscription amount is significant to the company and the cash level would be 65% of the company's total assets upon completion. The company's assets would comprise substantially of cash.

    (b) The subscriptions would be a means to list a new business which is unsuitable for listing:

        - The company has been engaging in the garment business since listing. It acquired a company engaged in the mobile game business only after it signed the subscription agreements.

        - The subscription amount is significant to the company. It has no correlation, and is completely disproportionate, to the company's existing garment business. The proceeds would be used to develop and operate a new mobile game business that would be significant relative to the existing business after the subscription.

        - The company would in effect be a listed vehicle for the subscriber (who would acquire a de facto control of the company using the restricted convertible bonds) to develop and operate a new mobile game business which has no track record and does not meet the new listing requirements.

Example 2

18. Company B is principally engaged in the business of manufacturing toys. It recorded revenue of about HK$200 million and a loss of HK$38 million in the latest financial year, and its total assets value was about HK$500 million.

19. Two months earlier, Company B obtained a money lender licence in Hong Kong and commenced a money lending business.

20. The proposed subscriptions: Company B signed subscription agreements to raise HK$1 billion by issuing shares to subscribers:

- Upon completion, about 75% of its total assets would consist of cash. The proceeds from the subscriptions would be mostly used to develop the money lending business. In particular, Company B signed loan agreements to provide financial assistance of a total amount of HK$900 million to several independent third parties. These agreements were subject to completion of the subscriptions.

- The subscribers would hold about 55% of Company B's shares as enlarged by the new shares.

The major subscriber is a money lending company.

21. *The Exchange's analysis*: The Exchange considers that Rule 14.06D would apply to the proposed subscriptions for the following reasons:

(a) The subscription amount is significant to the company and the cash level would be 75% of the company's total assets upon completion. Company B's assets would comprise substantially of cash.

(b) The subscriptions would be a means to list a new business which is unsuitable for listing:

- Company B has been engaging in manufacturing toys. The money lending business commenced shortly before the subscriptions were agreed and is a new business of Company B.

- The subscription amount is significant to Company B. It has no correlation, and is completely disproportionate, to Company B's original toy business. The proceeds would be used to develop and operate the money lending business that would be significant relative to the existing business after the subscription.

- Company B would in effect be a listed vehicle for the subscribers (who would become controlling shareholders of Company B) to develop and operate the new money lending business that has no track record and does not meet the new listing requirements.

22. Whilst Company B has signed legally binding agreements (i.e. the loan agreements) to ensure that a substantial part of the subscription proceeds would be used shortly after completion of the subscriptions, this does not address the concern about backdoor listing of a new business to circumvention of new listing requirements. These proceeds would be counted for the purpose of calculating the cash to assets ratio of the issuer under Rule 14.06D.

Whether a proposed rights issue of shares with bonus warrants required independent shareholders' approval

Facts

1. A Main Board issuer (**Company A**) announced a rights issue of one rights share for every two existing shares, plus two bonus warrants for every five subscribed and fully paid rights shares. It had not conducted any rights issue or open offer during the past 12 months.

2. The rights shares excluding the new shares convertible from the bonus warrants would represent 50% of Company A's existing issued share capital. They together with the new shares convertible from the bonus warrants would represent 70% of the existing share capital.

3. Company A submitted that the rights issue was not subject to independent shareholder approval under Rule 7.19A(1) as the total amount of rights shares, excluding the new shares convertible from the bonus warrants, did not exceed the 50% threshold in the Rule. It excluded the bonus warrants because in its view, the Rule requires an issuer to take into account any bonus securities, warrants or other convertible securities granted as part of any rights issues and open offers in the past 12 months, but not those forming part of the proposed rights issue.

Relevant Listing Rules

4. Rule 7.19A(1) states that:

   A proposed rights issue must be made conditional on minority shareholders' approval in the manner set out in rule 7.27A if the proposed rights issue would increase either the number of issued shares… of the issuer by more than 50% (on its own or when aggregated with any other rights issues or open offers announced by the issuer (i) within the 12 month period immediately preceding the announcement of the proposed rights issue 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).

   (Rule 7.19A(1) was amended on 11 June 2024. See Note below.)

5. Rule 7.27A states that:

   Where minority shareholders' approval is required for a rights issue … under Rule 7.19A …:

   (1) the rights issue … 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; …

Analysis

6. The purpose of Rule 7.19A(1) is to protect minority shareholders' interests when the potential dilution effect of a proposed rights issue (individually or together with any similar fund raising exercise(s) made in the previous 12 months) is material.

7. The Exchange disagreed with Company A's view on the application of Rule 7.19A(1) to the bonus warrants. Under the Rule, an issuer must take into account the proposed rights issue and any other rights issues or open offers made in the past 12 months, together with any bonus securities, warrants or other convertible securities *"granted or to be granted to shareholders as part of such rights issues or open offers*". These bonus securities, warrants or other convertible securities include those forming part of (1) the proposed rights issue and (2) any previous rights issues or open offers.

8. Here, the bonus warrants formed part of the rights issue. When assessing the ownership dilution effect of the rights issue under Rule 7.19A(1), Company A should take into account the shares convertible from the bonus warrants.

Conclusion

9. As the rights issue would increase Company A's issued share capital by 70%, it required independent shareholder approval under Rules 7.19A(1) and 7.27A.

Note: Rule 7.19A(1) was amended on 11 June 2024 to exclude treasury shares from the issuer's number of issued shares in determining whether the rights issue requires minority shareholders' approval. The Rule amendments would not change the analysis and conclusion in this case.

Whether a proposed rights issue that would increase the listed issuer's market capitalisation by more than 50 per cent required independent shareholders' approval

Facts

1. A Main Board issuer (**Company A**) signed an underwriting agreement for a proposed rights issue and published the announcement after the market closed on Day X. It had not conducted any other rights issue or open offer in the past 12 months.

2. The rights issue would be made on the basis of one rights share for every two existing shares. It would increase Company A's issued share capital by 50%.

3. The issue price for the rights shares was determined by Company A and the underwriter with reference to the recent market price of Company A's shares. It represented a small discount to the average closing price of the shares in the five trading days ended on Day X, and a premium of about 10% to the closing price on Day X.

4. There was an issue whether the rights issue would increase Company A's market capitalization by more than 50% and therefore require independent shareholder approval under Rule 7.19A(1). Company A submitted that the rights issue would not exceed the 50% threshold based on its market capitalisation calculated using the average closing price of its shares in the five trading days ended on Day X.

Relevant Listing Rules

5. Rule 7.19A(1) states that:

   A proposed rights issue must be made conditional on minority shareholders' approval in the manner set out in rule 7.27A if the proposed rights issue 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 rights issues or open offers announced by the issuer (i) within the 12 month period immediately preceding the announcement of the proposed rights issue 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).

   (Rule 7.19A(1) was amended on 11 June 2024. See Note below.)

6. Rule 7.27A states that:

> Where minority shareholders' approval is required for a rights issue … under rule 7.19A … :
>
> (1) the rights issue … 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;
>
> …

Analysis

7. The purpose of Rule 7.19A(1) is to protect minority shareholders' interests when the potential dilution effect of a proposed rights issue (individually or together with any similar fund raising exercise(s) made in the previous 12 months) is material.

8. Under the Rule, a proposed rights issue that would increase the issuer's market capitalisation by more than 50% is subject to independent shareholder approval. The assessment should be made with reference to the issuer's market capitalisation at the time of the proposed rights issue. For this purpose, the Exchange generally considers it acceptable for the issuer to calculate its market capitalisation using the closing price of its shares on the date on which the terms of the rights issue are finalised.

9. Here the rights issue would exceed the 50% threshold based on Company A's market capitalisation calculated using the closing price of its shares on Day X.

Conclusion

10. The rights issue required independent shareholder approval under Rule 7.19A(1).

Note: Rule 7.19A(1) was amended on 11 June 2024 to exclude treasury shares from the issuer's number of issued shares in determining whether the rights issue requires minority shareholders' approval. The Rule amendments would not change the analysis and conclusion in this case.

Whether the proposed rights issue by a PRC issuer under general mandate would be subject to the 20 per cent discount limited on issue price

Facts

1. A PRC issuer listed on the Main Board (**Company A**) proposed a rights issue of 1 new H or domestic rights share for every 10 existing H or domestic shares held by its shareholders on the record date. The H rights shares and the domestic rights shares were to be issued at the same price after foreign exchange conversion. This represented a discount of about 40 per cent. to the average closing price of the H shares before the price determination date.

2. Under its articles of association, Company A was required to obtain shareholders' approval by special resolution in general meeting for any issue of new shares, including any pre-emptive issue.

3. Company A proposed to issue the rights shares under a general mandate. The mandate was granted to Company A by a special resolution of its shareholders passed at the annual general meeting held a few months ago. It allowed Company A to issue new shares of not more than 20 per cent. of each of the issued H shares and domestic shares within 12 months, and there was no restriction on the issue price of the new shares. Company A had not issued any new shares under the mandate.

4. It enquired whether the rights issue would be subject to a 20 per cent discount limit on issue price under the Rules.

Relevant Listing Rules

5. Rule 19A.38 states that the requirements of Rule 13.36(1) and (2) are replaced by the following provisions:

"13.36 (1) (a) Except in the circumstances mentioned in rule 13.36(2), the directors of the PRC issuer shall obtain the approval by a special resolution of shareholders in general meeting, and the approvals by special resolutions of holders of domestic shares and overseas listed foreign shares (and, if applicable, H shares) (each being otherwise entitled to vote at general meetings) at separate class meetings conducted in accordance with the PRC issuer's articles of association, prior to authorising, allotting, issuing or granting:—

(i) shares;

(ii) securities convertible into shares; or

(iii) options, warrants or similar rights to subscribe for any shares or such convertible securities.

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 PRC issuer must be offered to the existing shareholders (and, where appropriate, to holders of other equity securities of the PRC 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 rule 13.36(2).

(b) …

(2) No such approval as is referred to in rule 13.36(1)(a) shall be required in the case of authorizing allotting or issuing shares if, but only to the extent that,

(a) the existing shareholders of the PRC issuer have by special resolution in general meeting given approval, either unconditionally or subject to such terms and conditions as may be specified in the resolution, for the PRC issuer to authorise, allot or issue, either separately or concurrently once every twelve months, not more than twenty per cent. of each of the existing issued domestic shares and overseas listed foreign shares of the PRC issuer; or

(b) …

Notes: (1) Other than where independent shareholders' approval has been obtained, an issue of securities to a connected person pursuant to a general mandate given under rule 13.36(2) is only permitted in the circumstances set out in rule 14A.92.

…"

(Rule 19A.38 was amended on 1 August 2023. See Note 1 below.)

6. Rule 13.36(5) states that:

"In the case of a placing or open offer 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 benchmark price being the higher of:

(a) …; and

(b) …,

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 urgent rescue operation …"

(Rule 13.36 was amended on 11 June 2024. See Note 2 below.)

Analysis

7. Here Company A had obtained a general mandate from its shareholders that complied with Rule 19A.38. The rights shares proposed to be issued would not exceed the 20% limit on the number of new H and domestic shares issuable under the general mandate. Any issue of rights shares to its shareholders who were connected persons would fall under Rule 14A.92(1) and be exempt from the connected transaction requirements.

8. The 20 per cent discount limit on the issue price under Rule 13.36(5) did not apply to the proposed rights issue. The resolution on general mandate passed by Company A's shareholders did not set any restriction on the price of new shares to be issued under the mandate.

Conclusion

9. Company A could use the existing general mandate to issue the rights shares under Rule 19A.38.

Notes:

1. *Rule 19A.38 was amended on 1 August 2023 to, among others, (i) remove the class meeting requirements relating to the share issuance by PRC issuers; (ii) require the share issuance to be approved by ordinary resolution (rather than special resolution) in a general meeting; (iii) remove the shareholders' approval requirement for pre-emptive issuance of shares; and (iv) set the general mandate limit at 20% of a PRC issuer's total issued shares (instead of 20% of each of domestic shares and H shares). The amended Rule requirements for PRC issuers are in line with the Rule requirements applicable to other issuers. The Rule amendments would not change the analysis and conclusion in this case.*

2. *Rule 13.36 was amended on 11 June 2024 to, among others, (i) apply the existing requirements for an issue of new shares to a resale of treasury shares; and (ii) exclude treasury shares in the calculation of issued shares for the purpose of determining the general mandate limit. The Rule amendments would not change the analysis and conclusion in this case.*

Whether a listed issuer's arrangements to dispose of the excess rights shares under a rights issue were made on a fair basis

Facts

1. A Main Board listed issuer (**Company A**) announced a rights issue on the basis of one rights share for every two existing shares. The issue price represented a substantial discount to the recent trading price of its shares.

2. According to Company A's announcement and listing document for the rights issue, qualifying shareholders would be entitled to apply for any excess rights shares not subscribed by the allottees under the provisional letters of allotment or their renounces. The board of directors would allocate the excess rights shares being applied for at its discretion and on a fair and equitable basis under the following principles:

   (i) preference will be given to applications to top-up holdings to board lots (**Top-up Applications**) where it appears to the directors that the applications are not made with the intention to abuse such mechanism; and

   (ii) if any excess shares are available after allocation under principle (i), they will be allocated to other applicants based on a sliding scale with reference to the number of the excess shares applied for by them.

3. The rights issue was over-subscribed. Company A noted unusual patterns of excess applications and had reasons to believe that certain applications might have been made with the intention to abuse the mechanism to top-up holdings to board lots. The number of shareholders had increased significantly after the rights issue announcement, and there were over 10,000 excess applications for rights shares representing about 20 times the total number of rights shares available under the rights issue. It appeared that certain shareholders had split their shareholdings into odd lots to enable them to submit multiple Top-up Applications.

4. After reviewing the excess applications and related shareholding changes, Company A's board of directors found that only a small portion of the Top-up Applications did not appear to be made with an intention to abuse the mechanism to top-up holdings to board lots. The board decided to exercise its discretion to allocate the excess rights shares in full only to these Top-up Applications. The remaining excess rights shares would then be allocated to other applicants based on a sliding scale with reference to the number of excess rights shares applied by them.

5. Company A enquired if the arrangements to dispose of the excess rights shares would comply with Rules 7.21(1)(a) and 7.21(3)(a).

Relevant Listing Rules

6. Rule 7.21(1) states that:

"In every rights issue the issuer must make arrangements to:—

(a) dispose of securities not subscribed by allottees under provisional letters of allotment or their renouncees by means of excess application forms, in which case such securities must be available for subscription by all shareholders and allocated on a fair basis; or

(b) …

The arrangements described in rule 7.21(1)(a) or (b) must be fully disclosed in the rights issue announcement, listing document and other circular."

7. Rule 7.21(3) states that:

"Where arrangements described in rule 7.21(1)(a) are made:

(a) the basis of allocation of the securities available for excess applications must be fully disclosed in the rights issue announcement, listing document and any circular; and

(b) …"

Analysis

8. An issuer is required to treat its shareholders fairly and equally. In the case of a rights issue, Rule 7.21(1)(a) requires that if there is an arrangement to dispose of any excess rights shares through excess application forms, the directors must allocate the excess rights on a fair basis. If the issuer has identified any problems which may indicate a possible abuse of the mechanism for allocating the excess rights shares, it must look into the problems and take appropriate steps to avoid the abuse and to ensure fair treatment of shareholders. Rule 7.21(3)(a) also requires the issuer to fully disclose the intended basis of allocation to ensure that sufficient information is provided to shareholders to make an informed decision before they apply for the rights shares.

9. Here Company A had disclosed the intended basis of allocation of excess rights shares in its announcement and listing document, including that preference will be given to Top-up Applications where it appears to the directors that the applications are not made with the intention to abuse such mechanism. The Exchange noted the special circumstances of this case and was satisfied that Company A had taken reasonable steps to ensure the excess shares were allocated to its shareholders on a fair basis. It considered the allocation was made consistent with the principles disclosed in the company's documents.

Conclusion

10. The Exchange considered that Company A's arrangements to dispose of the excess rights shares complied with Rules 7.21(1)(a) and 7.21(3)(a).

Rights issue

1. A listed issuer has obtained independent shareholders' approval for its previous 1-for-1 rights issue according to MB Rule 7.19A(1) / GEM Rule 10.29(1). Does it need to seek independent shareholders' approval for its 1-for-5 rights issue proposed to be made within 12 months from the previous one?

Yes, as the proposed rights issue, when aggregated with the previous one, would increase the listed issuer's number of issued shares (excluding treasury shares) by more than 50%. The aggregation requirement applies to rights issues made within 12 months, regardless of whether independent shareholders' approval was obtained for the previous one.

MB Rule 7.19A(1)
GEM Rule 10.29(1)
First released: February 2013; last updated: June 2024

Whether the Exchange would grant listing approval for a placing of new shares if there was a leakage of inside information before the announcement of the placing

Facts

1. On Day 1, the price and trading volume of the shares of a listed issuer (**Company A**) started to increase. Such increase continued until Day 7. On Day 4, the increase in the share price intensified and the Exchange contacted a director of Company A enquiring into the reasons for such increase. The Exchange was advised by Company A that there was no information that ought to be released pursuant to Rule 13.09 or Rule 13.23. Accordingly a standard announcement pursuant to Rule 13.10 was released on the Exchange's teletext system on Day 5.

2. After trading hours on Day 6, the Exchange was informed by a financial adviser on behalf of Company A that Company A had concluded a placing agreement for the issue of new shares in Company A.

Analysis

3. Upon enquiry, Company A admitted that it had on Day 2 appointed a consultant to identify on a "no name" basis a suitable brokerage firm which would be interested in arranging a share placing for Company A. The instructions to the consultant were still open on Day 4 and Day 5 when Company A released its standard Rule 13.10 announcement.

4. Company A reiterated that it was not aware of the reasons for the increase in the price and trading volume of Company A's shares during the period from Day 1 to Day 6. Company A considered that the issue of the standard Rule 13.10 announcement was appropriate on Day 4 and Day 5 as Company A had not commenced any negotiations for a placing with any agent on or before Day 4 and a premature announcement at that stage might have led to unnecessary speculation in Company A's shares.

5. It appeared, however, that Company A or its advisers had permitted price-sensitive information regarding the proposed issue of new securities to leak out onto the market prior to its proper publication and certain people had acted upon this information and traded in Company A's shares.

Conclusion

6. Pursuant to paragraph 5 of Practice Note 11, the Exchange decided not to approve Company A's application for the listing of the placing shares.

Placing

1. What are the types of equity capital market transactions that require the appointment of a CMI to be made under a written engagement agreement before it conducts any of the specified activities?

An issuer is required to appoint a CMI by way of a written engagement agreement before such CMI conducts any specified activities under MB Rule 3A.32 / GEM Rule 6A.39 (Notes 1, 2 and 3).

An issuer is not under the above obligations in respect of offerings of equity securities or interests which do not involve bookbuilding activities (as defined under the Code of Conduct), such as:

(i) transactions as specified in Note (2) to MB Rule 3A.32(2) / Note to GEM Rule 6A.39(2);

(ii) selling of listed equity securities or interests by existing holders of equity securities or interests, other than a placing as referred to in MB Rule 3A.32(1)(b) / GEM Rule 6A.39(1)(b) (sometimes referred to as "secondary offering"); and

(iii) an offering of equity securities or interests which has been subscribed by an intermediary as principal deploying its own balance sheet, for onward selling to investors (sometimes referred to as "block transactions").

For the avoidance of doubt, if an equity offering involving bookbuilding or placing activities (as defined in the Code of Conduct) uses a back stop arrangement (where the CMI provides a guarantee or an underwriting commitment at a minimum price to the issuer), the CMI in this connection should be appointed under a written engagement agreement before it conducts the specified activities for such transaction under MB Rule 3A.33 / GEM Rule 6A.40, even if the CMI may have a right to acquire the equity securities or interests offered as principal under the relevant back stop / underwriting agreement, given that it is uncertain whether any equity securities or interests would be acquired by the CMI as principal by deploying its own balance sheet, for onward selling to investors.

Notes:

1. The scope of offerings to which the Listing Rules apply is the same as that set out in paragraph 21.1.2(a) of the Code of Conduct.

2. If a CMI does not perform, and is not and will not be appointed to perform, the specified activities in an offering set out in MB Rule 3A.32(1) / GEM Rule 6A.39(1), the requirement under MB Rule 3A.33 / GEM Rule 6A.40 will not apply to that CMI.

3. Placing and bookbuilding activities (as defined under the Code of Conduct) do not

include market sounding that is conducted to gauge investors' interest before an issuer has decided to pursue an offering. As the timing at which an issuer makes a decision to pursue an offering is solely within its knowledge and control, the issuer is expected to communicate its decision promptly to any CMI it has authorised to conduct market sounding and to appoint the CMI under a written engagement agreement before it conducts the specified activities in accordance with MB Rule 3A.33 / GEM Rule 6A.40.

MB Rules 3A.32, 3A.33 and 3A.35
GEM Rules 6A.39, 6A.40 and 6A.42
First released: April 2022; last updated: May 2024

2. Under the Listing Rules, a new applicant and its directors shall provide each syndicate member with a list of the directors and existing shareholders of the new applicant, their respective close associates and any person who is engaged by or will act as a nominee for any of the foregoing persons to subscribe for, or purchase shares in connection with a New Listing (Restricted Investors).

Does this requirement apply to a placing of shares by a listed issuer that falls under MB Rules 3A.32(1)(a)(ii) or 3A.32(1)(b) / GEM Rules 6A.39(1)(a)(ii) or 6A.39(1)(b)?

No, this requirement only applies to a placing in connection with a New Listing. However, listed issuers should comply with the requirement of the Listing Rules in connection with the placing of (a) equity securities or interests of a class new to listing or of a class already listed under a general or specific mandate or (b) listed equity securities or interests (if it is accompanied by a top-up subscription) to any "connected person" as defined in MB Chapter 14A / GEM Chapter 20. For example, a listed issuer may provide information to assist the syndicate members to identify the listed issuer's connected persons.

MB Rule 3A.46
GEM Rule 6A.48
First released: April 2022; last updated: May 2024

3. Does a listed issuer need to publish an OC Announcement on an appointment or termination of an OC in relation to the placings other than in connection with a New Listing?

No, the requirement for publication of an OC Announcement only applies to a new applicant effecting a placing involving bookbuilding activities (as defined in the Code of Conduct) in connection with a New Listing and does not apply to an offering by a listed issuer under MB Rules 3A.32(1)(a)(ii) or 3A.32(1)(b) / GEM Rules 6A.39(1)(a)(ii) or 6A.39(1)(b).

However, in an offering by a listed issuer under MB Rule 3A.32(1)(a)(ii) or 3A.32(1)(b) / GEM Rule 6A.39(1)(a)(ii) or 6A.39(1)(b), it is required to notify the Exchange of the termination of an OC in writing as soon as practicable under MB Rule 3A.41(1) / GEM Rule 6A.46(1).

MB Rules 2.07C(6)(a), 3A.32, 3A.37, 3A.41, 9.08(2) and 12.01C, PN22
GEM Rules 16.19(1), 6A.39, 6A.44, 6A.46, 12.10(2) and 16.01C, PN5
First released: April 2022; last updated: May 2024

4. If market conditions deteriorate in the course of a secondary placing that falls within MB Rule 3A.32 / GEM Rule 6A.39, can the placing agents agree with the issuer to reduce their fees so that the net proceeds from the placing would not be substantially reduced despite that the placing shares are priced below the bottom end of the initial price range?

If a reduction of fee arrangement is permitted, must such reduction of fee arrangement be included in the engagement letter and if not, do the placing agents need to consult the regulators before changes are made to the fee structure?

What disclosure is required in the announcement on the secondary placing in respect of the placing agents' fees?

We understand that it is not a common market practice for placing agents to agree at the time of engagement that they shall reduce their fees in the event that the placing price is set below the indicative price range in a placing. However, in the event that such fee reduction arrangements have been agreed at the time of the engagement, the arrangements should be reflected in the engagement letter.

The placing agents are not required to consult the regulators before changes are made to the fee structure given the tight timeline to complete a secondary placing.

The announcement on the secondary placing should disclose the final rate paid/ payable to the placing agents (after discount) based on the placing price, which should have been determined by the time the relevant announcement is made. Where a placing agent agrees to waive part or all of the fee after the announcement, the issuer is normally expected to update the market on this subsequent fee waiver as a material change in information previously announced.

MB Rules 3A.34 and 3A.36
GEM Rules 6A.41 and 6A.43
First released: April 2022; last updated: May 2024

Guidance on the issue of convertible securities by listed issuers

A. Purpose

1. This letter gives guidance on the Listing Rule requirements relating to issues of convertible securities by listed issuers, including convertible and exchangeable bonds, notes and loans and convertible and exchangeable preference shares (collectively **convertible securities**). These securities are convertible into shares of the issuers (**conversion shares**) which are listed on the Exchange. The conversion shares may be satisfied by issue of new shares or transfer of treasury shares. This guidance does not cover the listing of the convertible securities.

B. Relevant Listing Rules

2. The issue of convertible securities by a listed issuer is subject to shareholders' approval, either pursuant to a special mandate in relation to the convertible securities or as part of a listed issuer's general mandate under Main Board Rule 13.36 (GEM Rules 17.39 to 17.41). Under Main Board Rule 13.36(6) (GEM Rule 17.42C), where the convertible securities are issued pursuant to a general mandate for cash consideration, the initial conversion price must not be lower than the benchmarked price (as defined in Main Board Rule 13.36(5) (GEM Rule 17.42B)) of the issuer's shares at the time of issue.

3. Under Main Board Rules 8.20, 16.01 and 28.01 (GEM Rules 11.30(2), 22.01 and 34.05), if a listed issuer proposes to issue convertible securities, it must, prior to the issue of convertible securities, seek the Exchange's approval for (i) the convertible securities; and (ii) the listing of the shares issuable[1] upon conversion under the terms of the convertible securities, whether the convertible securities themselves are to be listed or not.

4. Under Main Board Rules 16.03 and 28.05 (GEM Rules 22.03 and 34.05), the listed issuer must obtain the Exchange's prior consent for any proposed change in the terms of the convertible securities, unless the change occurs automatically according to the terms of the convertible securities.

5. Listed issuers must also comply with other specific Rule requirements for convertible securities issued by them under Chapters 16 and 28 of the Main Board Rules (Chapters 22 and 34 of the GEM Rules).

[1] The listed issuer is not required to submit a listing application for any transfer of treasury shares upon conversion of the convertible securities.

C. Guidance

(I) Pre-emptive rights

6. Under Main Board Rules 2.03(6) and 13.36 (GEM Rules 2.06(6), 17.39, 17.40 and 17.41), any new issue of shares (including securities convertible into shares) or sale or transfer of treasury shares by an issuer on a non-pre-emptive basis must be approved by shareholders. Shareholder approval may be obtained by either a specific mandate (i.e. an approval of a specific transaction in general meeting) or a general mandate.

Sufficiency of general mandate

7. If an issuer proposes to issue convertible securities under a general mandate, it must have an unused mandate that is sufficient to cover all conversion shares. This should take into account the conversion price and the adjustment mechanism that may affect the number of conversion shares. We set out below two broad categories of terms under convertible securities and our approach in assessing the issue size of the conversion shares:

(i) Conventional convertible securities with a fixed initial conversion price, subject to adjustments that are triggered by events within the issuer's control:

(a) The initial conversion price for the convertible securities is at a fixed dollar amount. It is subject to customary adjustment provisions triggered by corporate actions that are within the issuer's control, including share consolidations or subdivisions, capital distributions, further issues of securities or sales or transfers of treasury shares at less than current market price, etc.

(b) In general it is acceptable for an issuer to issue these convertible securities under a general mandate if, at the time of the issue of the convertible securities, 1) the unutilised portion of the general mandate is sufficient to cover the number of conversion shares based on full conversion of the convertible securities; and 2) where the convertible securities are issued for cash consideration, the initial conversion price is not lower than the benchmarked price of the issuer's shares.

(c) As the events triggering the adjustments of the conversion price are within the issuer's control, the issuer should not take corporate actions that would result in the number of conversion shares exceeding the mandate limit.

(d) The listing approval, if granted by the Exchange, will generally be given in respect of a specific number of conversion shares within the mandate limit. The issuer must adopt appropriate procedures to keep track of the number of conversion shares issued/ transferred and to be issued/ transferred under the terms of the convertible securities. It should take this into account before it takes any actions that would trigger the adjustment provisions.

(e) The issuer's monthly return should appropriately reflect the number of conversion shares which may be issued/ transferred upon full conversion of the amount of convertible securities outstanding as at the close of the month, and that it has sufficient mandate to cover these shares.

(ii) Convertible securities with an automatic price re-set or adjustment mechanism which is not triggered by events within the issuer's control:

(a) An example is a "toxic" convertible where the conversion price is re-set with reference to the future trading price of the issuer's shares.

(b) The issuer must obtain a specific mandate from its shareholders for the issue of the convertible securities if it proposes to issue the convertible securities for cash or it is unable to demonstrate that its general mandate at the time of the issue of the convertible securities is sufficient to cover all conversion shares[2].

Proposed changes to convertible securities

8. As mentioned in paragraph 4 above, an issuer must seek the Exchange's approval before it proposes any change to the terms of convertible securities after issue. If the Exchange considers that an issuer's proposal constitutes a material change to the terms of the convertible securities, it will treat the proposal as if it were a new issue of convertible securities. This means that the issuer must obtain shareholder approval for the proposed new issue, unless it has a sufficient unutilised portion of, and is permitted to use, its general mandate at the time of the proposed new issue to cover the number of conversion shares based on full conversion of the proposed convertible securities. (See also Listing Decision LD54-2013)

(II) Disclosure requirements

Announcement for issue of convertible securities

9. If an issuer issues convertible securities for cash, it must publish an announcement in accordance with Main Board Rule 13.28 (GEM Rule 17.32). The disclosure should include:

(i) all material terms of the convertible securities, including the conversion price and a summary of the provisions for adjustments of the price and/or the number of conversion shares;

(ii) the maximum number of conversion shares upon exercise of the conversion rights; and

(iii) if the convertible securities are to be issued under a general mandate, details of the mandate. The information should demonstrate the mandate is sufficient to cover the conversion shares, such as the date of the general meeting approving the mandate, the number of shares that the issuer is authorised to issue or sell or transfer out of treasury under the mandate and other terms and conditions of the mandate, and the unutilised portion of the mandate available for the proposed issue of convertible securities.

10. The above information should also be disclosed in an announcement for a notifiable transaction under Chapter 14 of the Main Board Rules (Chapter 19 of the GEM Rules) if the consideration for the transaction involves the issue of convertible securities.

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[2] If the issuer has no control over any adjustment of the conversion price after the issue of the convertible securities, it should use the lowest possible conversion price to calculate the maximum number of conversion shares upon full conversion of the convertible securities.

Circular for issue of convertible securities

11. Under Main Board Rule 13.36(8) (GEM Rule 17.42E), where an issuer proposes to issue convertible securities under a specific mandate, the circular to shareholders shall disclose the issuer's intention, if any, to use treasury shares to satisfy its obligation upon conversion of any of such convertible securities.

Announcement for change in terms of convertible securities

12. After an issuer has issued convertible securities, it should timely announce:

    (i) any change in the terms of the convertible securities (including any adjustment of the conversion price according to the terms of the convertible securities); and

    (ii) the effect of the change.

13. Where the convertible securities were issued under a general mandate, the issuer should also confirm that it has sufficient mandate to cover the conversion shares after the change takes effect. (See also paragraphs 7(i)(c), 7(i)(d) and 8 above)

Disclosure in financial reports

14. Issuers are expected to disclose additional information in their annual and interim reports to enable investors to be aware of the dilution impact on the issuers' shares in the event that all outstanding convertible securities were converted as at the relevant year end or period end, including:

    (i) the number of shares that may be issued or transferred out of treasury upon full conversion of the outstanding convertible securities;

    (ii) the dilutive impact on the then number of issued shares (excluding treasury shares) of the issuer and respective shareholdings of the substantial shareholders of the issuer;

    (iii) the dilutive impact on earnings per share;

    (iv) an analysis on the financial and liquidity position of the issuer, discussing its ability to meet its redemption obligations under the convertible securities; and

    (v) an analysis on the issuer's share price at which it would be equally financially advantageous for the securityholders to convert or redeem the convertible securities based on their implied internal rate of return (and therefore the securityholders would be indifferent as to whether the convertible securities are converted or redeemed) at a range of dates in the future.

    In each case, this information should take into account any provisions permitting payment of interest in kind (assuming a worst-case scenario).

(III) Public float

15. The public float requirements under Main Board Rules 8.08 and 13.32 (GEM Rule 11.23(7)) seek to ensure an open market in the securities for which listing is sought. The Exchange would not give listing approval for an issue of conversion shares if it may lead to a breach of the requirement.

16. For example, if an issuer proposes to issue convertible securities to its connected person(s) or a person who would become its substantial shareholder upon conversion of the convertible securities, the issue of the convertible securities may result in the issuer's public float failing to meet the minimum requirement. In these circumstances, the Exchange would not approve the issue of the convertible securities and the listing of the conversion shares issuable unless the issuer has concrete arrangements to ensure the minimum public float is maintained upon conversion of the convertible securities. An example of an acceptable arrangement would be to set out in the terms of the convertible securities a restriction against any conversion of the convertible securities if such conversion would result in the issuer failing to meet the minimum public float. *(See also Listing Decision LD56-2013)*

Whether the Exchange would give consent to a listed issuer under Rule 10.06(3)(a) for share buyback to be conducted concurrently with its convertible bond offering

Facts

1. Company A sought the Exchange's consent under MB Rule 10.06(3)(a) for share buyback to be conducted concurrently with its proposed offering of convertible bonds (**CBs**).

CB offering

2. Company A was a Main Board issuer with a market capitalisation of over HK$100 billion and an average daily turnover volume of over HK$400 million in the preceding six months. It proposed to conduct an offering of CBs in an aggregate principal amount of around US$300 million to professional investors through placing banks. The initial conversion price of the CBs was expected to be set at a substantial premium over the benchmarked price[1] of the shares of Company A in compliance with MB Rule 13.36(6). Upon conversion of the CBs, Company A would deliver shares to the bondholders. The CBs were expected to be issued under the general mandate granted to its directors at the last annual general meeting.

Concurrent share buyback in connection with the CB offering

3. Company A submitted that the subscribers of the CBs would comprise hedge funds and arbitrage investors whose investment strategies involved purchasing the CBs and concurrently short selling a portion of the underlying shares (**delta shares**) to establish an initial hedge against their exposure under the CBs. To facilitate a coordinated short sale by these CB investors, the placing banks would aggregate the delta shares and sell them off-market (**delta placement**) on behalf of the CB investors.

4. It was proposed that, concurrently with the CB offering, the delta shares would be offered to Company A and other investors. The allocation and price of the delta shares would be determined through a bookbuilding among the placing banks and the other investors, which Company A would not be involved. The delta placement price would be determined with reference to the last closing price of the shares of Company A immediately prior to the CB offering, and was expected to be at a small discount to such closing price. Company A would purchase the delta shares at the same delta placement price with part of the CB offering proceeds, and would cancel the purchased delta shares afterwards.

5. The purchase of delta shares by Company A would constitute an off-market share buybacks of Company A (**concurrent share buyback**). Company A considered the concurrent share buyback was part and parcel of the CB offering, which would help facilitate the creation of initial hedge of the CB investors and hence their subscription. It would also mitigate the negative pressure on the share price from their short-selling activities and the potential dilution of the CB offering from the conversion.

[1] As defined in MB Rule 13.36(5).

Announcement of the proposed transactions

6. The CB offering would be launched after market close in Hong Kong and the pricing terms would be determined overnight outside trading hours. Company A would publish an announcement before market open on the next trading day to disclose the terms of the CB offering and the concurrent share buyback.

Relevant Listing Rules

7. MB Rule 10.06(3)(a) provides that an issuer whose primary listing is on the Exchange may not (i) make a new issue of shares, or a sale or transfer of any treasury shares; or (ii) announce a proposed new issue of shares, or a sale or transfer of any treasury shares, for a period of 30 days after any purchase by it of shares, whether on the Exchange or otherwise, without the prior approval of the Exchange. The moratorium does not apply to a new issue of shares or a sale or transfer of any treasury shares under a capitalisation issue or a share scheme, pursuant to the exercise of warrants, share options or similar instruments, which were outstanding prior to the share buyback.

8. MB Rule 10.06(6)(c) provides that for the purpose of MB Rules 10.05, 10.06 and 19.16, "shares" shall mean shares of all classes and securities which carry a right to subscribe or purchase shares.

Analysis

9. MB Rule 10.06(3)(a) restricts an issuer from issuing new shares or convertible securities, or transfer of treasury shares, within 30 days after any share buyback. This is to ensure the issue or transfer of shares does not take place at a price that has been affected by the issuer's previous share buyback.

10. In this case, the proposed CB offering with concurrent share buyback would fall within the scope of MB Rule 10.06(3)(a) because the issuance of the CBs and the share buyback would take place concurrently.

11. Company A sought the Exchange's consent under MB Rule 10.06(3)(a)[2] to conduct the concurrent share buyback at the same time of the CB offering. When assessing Company A's application, the Exchange took into account the following factors:

    (i) The concurrent share buyback was part and parcel of the CB offering to facilitate the CB investors to establish an initial hedge required for their subscription of the CBs, and to mitigate the negative share price impact of such hedging activities and the potential dilution impact of the CB offering. As such, the concurrent share buyback would be beneficial to Company A and its shareholders as a whole.

    (ii) The concurrent share buyback would not artificially inflate the conversion price of the CBs. The CB offering would be launched after market close in Hong Kong, and the conversion price of the CBs and the delta placement price (and hence the repurchase price) would be determined at around the same time with reference to the last closing price of the shares. The delta placement price would be determined through a bookbuilding among the placing banks and the other investors, which Company A would not be involved.

[2] Company A also applied to the SFC for, and was granted, a waiver of, *inter alia*, a similar requirement in the Code on Share Buy-backs (Rule 7) based on the specific circumstances of its case.

Company A would announce the terms of the CBs and the concurrent share buyback before market open on the next trading day. In light of the above, the concurrent share buyback would not pose a material risk of price inflation. Further, Company A confirmed that: (a) save for the proposed concurrent share buyback, it had not conducted any share buybacks within 30 days before the announcement of the CB offering; and (b) it would not make a new issue of shares or a sale or transfer of any treasury shares, or announce a proposed new issue of shares or a sale or transfer of any treasury shares, for a period of 30 days after the concurrent share buyback, whether on the Exchange or otherwise, without the prior consent of the Exchange.

(iii) The shares of Company A were less susceptible to price manipulation given its large market capitalisation and high liquidity.

Conclusion

12. The Exchange gave consent to Company A under MB Rule 10.06(3)(a) to conduct the CB offering with the concurrent share buyback.

Whether the Exchange would grant listing approval for new shares to be issued by a listed issuer upon conversion of convertible notes that could result in the listed issuer's public float falling below the minimum requirement

Parties

- **Company A** – a Main Board issuer
- **Company B** – an investor who agreed to subscribe for new shares and convertible notes to be issued by Company A

Facts

1. Company A proposed to issue certain new shares (**Subscription Shares**) and convertibles notes to Company B under a subscription agreement. The convertible notes would be convertible into new shares of Company A (**Conversion Shares**) after the issue date according to the terms of the notes.

2. The proposed issue was conditional on approval of Company A's shareholders and the Exchange giving listing approval for the Subscription Shares and the Conversion Shares.

3. Upon completion of the subscription agreement, Company B would become a substantial shareholder of Company A, and the public float of Company A's shares would still meet the 25% requirement. However, based on the shareholding structure of Company A at that time, the public float would fall below 25% if Company B exercised its rights to convert some or all of the convertible notes.

4. Company A proposed to undertake to the Exchange that it would take appropriate measures to ensure the compliance with the public float requirement at all times. For example, it would consider placing new shares to independent third parties to maintain a 25% public float as a result of any conversion of the convertible notes, or redeeming some of the convertible notes.

5. Alternatively, Company A proposed to limit the maximum number of Conversion Shares that it might issue to Company B to be 25% of Company A's issued share capital at the time of completion of the subscription agreement.

Relevant Listing Rules

6. Rule 8.08(1)(a) provides that

   "at least 25% of the issuer's total number of issued shares must at all times be held by the public."

7. Rule 13.32(1) states that

   "Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands…"

Analysis

8. The public float requirement seeks to ensure an open market in the securities for which listing is sought. The Exchange would not give listing approval for an issue of new shares which would cause or facilitate a breach of the requirement.

9. In this case, the issue of the convertible notes to Company B could possibly result in the public float of Company A's shares falling below the minimum 25% requirement. The Exchange did not consider that Company A's undertaking to use reasonable endeavours to meet the requirement would adequately address its concern. Without any concrete arrangements to ensure a minimum 25% public float for Company A upon conversion of the convertible notes, the Exchange was not prepared to give listing approval until the issue was addressed.

10. The Exchange also did not consider the alternative proposal acceptable as it only took into account the shareholding structure of Company A at the time of the completion of the subscription agreement and not the conversion of the notes. It would be possible for Company A to issue Conversion Shares resulting in a breach of minimum public float requirement, as a result of changes to Company A's share capital (e.g. share repurchase) after the completion of the subscription agreement.

11. To address the Exchange's concern, Company A and Company B agreed to revise the terms of the convertible notes so that a conversion of the notes could not take place if it would result in Company A failing to meet the minimum public float requirement under the Rules.

Conclusion

12. The Exchange accepted that the action taken by Company A in paragraph 11 above addressed the issue of possible insufficient public float upon completion of the subscription agreement.

Whether the Exchange would approve the proposed changes to the terms of convertible bonds issued by a listed issuer under general mandate

Facts

Background

1. Two years ago, a Main Board issuer (**Company A**) issued certain convertible bonds to an independent third party (the **investor**) under a general mandate (the **original general mandate**). Assuming full conversion of the bonds at the initial conversion price, the conversion shares would represent 10% of the then issued shares of Company A.

2. The original general mandate allowed Company A to issue new shares of not more than 20 per cent. of its issued shares until the conclusion of the next annual general meeting. Except for the issue of the convertible bonds, Company A had not used the mandate to issue any other securities.

Proposals

3. In light of the change in market conditions after the issue of the convertible bonds, Company A and the investor proposed to revise the terms of the bonds:

   (a) the parties proposed to reduce the initial conversion price of the bonds. Based on the revised conversion price, the maximum number of conversion shares would not exceed the number of new shares issuable under the original general mandate.

   (b) alternatively, the parties would extend the conversion period and the maturity date of the bonds for one year. There would not be any change to the conversion price of the bonds and therefore the number of conversion shares issuable by Company A.

4. Company A submitted that the original general mandate would be sufficient to cover the conversion shares issuable under the revised terms of the bonds It sought the Exchange's approval for the proposed changes to the terms of the bond.

Relevant Listing Rules

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

(iii) options, warrants or similar rights to subscribe for any shares or such convertible securities.

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).

(b) …

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

(a) …

(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

…

…

(Rule 13.36 was amended on 11 June 2024. See Note below.)

6. Rule 28.05 states that:

Any alterations in the terms of convertible debt securities after issue must be approved by the Exchange, except where the alterations take effect automatically under the existing terms of such convertible debt securities.

Analysis

7. The Exchange considered that each of the proposals described in paragraph 3 would constitute a material change to the terms of the convertible bonds. They should be regarded as new arrangements for Company A to issue convertible securities to the investor. It could not use the original general mandate for the new arrangements.

8. Accordingly, Company A was required to comply with Rule 13.36 for the proposals. It should obtain a specific mandate for issuing the conversion shares under the revised terms of the bonds unless it had an existing general mandate that was valid and sufficient to cover these conversion shares. If Company A failed to do so, the Exchange would not approve the proposed changes to the terms of the bonds.

Conclusion

9. Company A was required to comply with Rule 13.36 for the proposals.

Subsequent Development

10. Under Rule 13.36(6) (which became effective on 3 July 2018), an issuer may not issue securities convertible into new shares of the issuer for cash consideration pursuant to a general mandate under Rule 13.36(2)(b), unless the initial conversion price is not lower than the benchmarked price (as defined in Rule 13.36(5)) of the shares at the time of the placing.

11. In this case, the convertible bonds were issued to the investor for cash consideration two years ago and Company A was required to comply with Rule 13.36 for the proposals described in paragraph 3. Under the amended Rules, Company A should obtain a specific mandate for issuing the conversion shares under the revised terms of the bonds unless (i) it had an existing general mandate that was valid and sufficient to cover these conversion shares; and (ii) the conversion

price of the bonds as revised was not lower than the benchmarked price of the shares at the time of the proposal.

Note: Rule 13.36 was amended on 11 June 2024 to, among others, (i) apply the existing requirements for an issue of new shares to a resale of treasury shares; and (ii) exclude treasury shares in the calculation of issued shares for the purpose of determining the general mandate limit. The Rule amendments would not change the analysis and conclusion in this case.

Whether an issue of convertible non-voting redeemable preference shares should be treated as an issue of equity or debt instruments

Facts

1. A listed issuer (**Company A**) proposed to issue non-voting redeemable preference shares, convertible into ordinary shares of Company A, to holders of its existing convertible loan notes. The convertible loan notes would then be cancelled and replaced by the convertible non-voting redeemable preference shares.

2. The principal features of the convertible non-voting redeemable preference shares were as follows:-

   - holders would be entitled to fixed cumulative dividends on the outstanding principal amounts due, irrespective of whether or not Company A had profits. It was submitted that such payments were akin to interest payments in debt financing arrangements in that they constituted a guaranteed rate of return;

   - holders ranked in priority to the holders of the ordinary shares; and

   - the convertible non-voting redeemable preference shares were not intended to be listed.

Analysis

3. Chapter 15 of the Listing Rules (options, warrants and similar rights) did not apply as it only applies to those options or notes that are not governed by any other specific chapter of the Listing Rules.

4. As the convertible non-voting redeemable preference shares were convertible into ordinary shares, Chapter 16 of the Listing Rules (convertible equity securities) should apply.

5. Even though the convertible non-voting redeemable preference shares were issued to replace the convertible loan notes, Chapter 28 of the Listing Rules (convertible debt securities) did not apply since preference shares are included in the definition of equity securities under the Listing Rules.

Conclusion

6. As the non-voting redeemable preference shares were equity securities with convertible features, Chapter 16 of the Listing Rules should apply. Moreover, the convertible non-voting redeemable preference shares would constitute securities convertible into shares. The issue was therefore subject to shareholders' approval by virtue of Rule 13.36(1)(a)(ii) unless covered by a general mandate.

Whether the Exchange would grant waiver for a warrant to be issued by a listed issuer in connection with its offering of equity-linked securities

Facts

1. Company A sought a waiver from compliance with MB Rule 13.36(7) so that it could issue the upper strike warrant under the general mandate granted to its directors at the last annual general meeting, and an approval from compliance with MB Rule 15.02(2) so that the upper strike warrant could have a tenor longer than five years to align with that of the equity-linked securities (**ELSs**).

   Offering of cash settled equity-link securities with call spread

2. Company A was a Main Board issuer with a market capitalisation of over HK$60 billion and an average daily turnover volume of over HK$300 million in the preceding six months. It proposed to conduct an offering of cash settled ELSs to professional investors through placing banks with an aggregate principal amount of around US$500 million and a tenor of seven years. The initial exercise price of the ELSs was expected to be set at a substantial premium over the benchmarked price[1] of the shares of Company A. Upon exercise of the conversion rights, holders of ELSs would receive cash based on the market price of the underlying shares of their converted ELSs. No shares would be issued by Company A for the settlement of ELSs.

3. In connection with the ELS offering, Company A would enter into a call spread (**call spread**) with affiliates of the placing banks (**call spread counterparties**), comprising:

   - **Lower strike call**: a call option granted by the call spread counterparties to Company A, which would entitle Company A to receive in cash the surplus of the market price of the shares over the lower strike price (which would be equivalent to the initial exercise price of the ELSs), in respect of the number of shares underlying the lower strike call exercised.

   - **Upper strike warrant**: a call option granted by Company A to the call spread counterparties, which would entitle the call spread counterparties to receive new shares from Company A issued at a pre-determined upper strike price that would be even higher than the initial exercise price of the ELSs.

4. Company A submitted that the call spread was an essential part of the ELS offering. The lower strike call served to offset part of Company A's payment obligation upon conversion of the ELSs, while the upper strike warrant would potentially achieve a higher exercise price for issuance of shares.

[1] As defined in MB Rule 13.36(5)

5. The call spread was intended to mirror and complement the structure of the ELS offering. It would be structured in a way that the timing, size and economics of the exercises under the call spread would match those under the ELSs. In particular, the term and exercise period of the call spread and the ELSs would be the same, and the maximum number of the shares issuable under the upper strike warrant would be equal to the maximum number of the shares underlying the ELSs.

6. Company A would pay an upfront cost for the call spread (being the difference between the premium payable for the lower strike call and the premium receivable for the upper strike warrant), which would be funded by the proceeds of the ELS offering. Company A had also provided the basis of determining the valuation of these call options and the upfront cost.

Waiver / approval sought

7. Company A sought a waiver from compliance with MB Rule 13.36(7) so that it could issue the upper strike warrant using the general mandate granted to its directors at the last annual general meeting. Company A submitted that the upper strike warrant was part and parcel of the ELS offering, which would in effect enable the company to raise funds in a way similar to an issue of convertible debt securities with a higher conversion price. Accordingly, Company A should be permitted to use the general mandate in line with an issue of convertible securities under MB Rule 13.36(6). It would be unduly burdensome to convene a general meeting to approve the upper strike warrant as the launch of the ELS offering would be time-sensitive in nature and subject to fast-changing market conditions.

8. Company A also sought an approval under MB Rule 15.02(2) so that the upper strike warrant could have a tenor longer than five years to align with that of the ELSs.

Relevant Listing Rules

9. Under MB Rule 13.36(7), listed issuers may not issue warrants, options or similar rights to subscribe for any new shares or securities convertible into new shares of the listed issuer for cash consideration pursuant to a general mandate.

10. MB Rule 13.36(6) provides that where convertible securities are issued pursuant to a general mandate for cash consideration, the initial conversion price must not be lower than the benchmarked price (as defined in MB Rule 13.36(5)) of the issuer's shares at the time of issue.

11. Under MB Rule 15.02(2), warrants, options or similar rights to subscribe or purchase equity securities of an issuer must expire not less than one year and not more than five years from the date of issue or grant.

Analysis

12. MB Rule 13.36(7) was introduced as part of the Listing Rules amendments relating to capital raisings by listed issuers in 2018. As set out in the consultation paper, the rule was introduced to prevent abuse of general mandate by some listed issuers for placing warrants at a nominal price that lacked commercial rationale. It is not intended to unduly restrict ordinary capital raising activities.

13. In this case, the upper strike warrant was not a standalone transaction to dilute the existing shareholders' interest in Company A. Company A would issue the upper strike warrant to the call spread counterparties at the same time of the ELS offering to potentially achieve a higher exercise price for issuance of shares. The overall structure would enable Company A to raise funds in a form similar to issue of convertible debt securities and the effective conversion price (being the initial exercise price of the ELS deducting the upfront cost payable by Company A for the call spread) would still be higher than the benchmarked price in compliance with MB Rule 13.36(6). Granting of the waiver would be unlikely to result in undue risks to its shareholders. Further, the call spread was intended to mirror and complement the structure of the ELSs. It would be reasonable for the upper strike warrant to have a tenor matching that of the ELSs.

Conclusion

14. The Exchange granted a waiver to Company A for its proposed issue of upper strike warrant in connection with the ELS offering under general mandate, and an approval for a tenor longer than five years to align with that of the ELSs.

In respect of a proposed rights issue of shares with bonus warrants, whether the Exchange would waive the requirements on the number and spread of warrantholders at the time of listing of the warrants

Facts

1. A Main Board issuer (**Company A**) proposed a rights issue on the basis of one rights share for every 10 existing shares held, with 2 bonus warrants for each rights share subscribed. The rights issue would be fully underwritten by independent underwriters.

2. Company A would apply for listing of the warrants on the Exchange.

3. For a class of securities new to listing, Rules 8.08(2) and 8.08(3) require that at the time of listing, there must be at least 300 holders of the securities to be listed, and not more than 50% of the securities in public hands can be beneficially owned by the three largest public shareholders. The Rules provide an exemption for listing of warrants that are offered to the issuer's existing shareholders by way of bonus issue, subject to certain conditions.

4. The exemption for bonus issue of warrants was not applicable in this case as the warrants were offered only to shareholders who would subscribe for the rights shares. The number and spread of warrantholders at the time of listing would depend on the results of the rights issue. Company A therefore sought a waiver from Rules 8.08(2) and (3).

5. Company A submitted that there were over 600 registered shareholders and 300 CCASS participants holding its shares based on its register of members and the CCASS shareholding information. Further, about 70% of its shares were held in public hands, and there was no information indicating a high concentration of shareholdings. Given a wide spread of shareholders, a lack of open market in the warrants was unlikely to occur at the time of listing.

Relevant Listing Rules

6. Rule 8.08 states that

   "There must be an open market in the securities for which listing is sought. This will normally mean that:

   (1) (a) at least 25% of the issuer's total issued share capital must at all times be held by the public;

   …

(2) for a class of securities new to listing, at the time of listing there must be an adequate spread of holders of the securities to be listed, except where: (a) they are options, warrants or similar rights to subscribe for or purchase shares; (b) they are offered to existing holders of a listed issuer's shares by way of bonus issue; and (c) in the 5 years before the date of the announcement of the proposed bonus issue, there are no circumstances to indicate that the issuer's shares may be concentrated in the hands of a few shareholders. The number will depend on the size and nature of the issue, but in all cases there must be at least 300 shareholders; and

(3) not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders, save where: (a) the securities to be listed are options, warrants or similar rights to subscribe or purchase shares; (b) such securities are offered to existing holders of a listed issuer's shares by way of bonus issue; and (c) in the 5 years preceding the date of the announcement on the proposed bonus issue, there are no circumstances to indicate that the shares of the issuer may be concentrated in the hands of a few shareholders."

(Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

Analysis

7. Rules 8.08(2) and (3) seek to ensure a broad base of holders of a new class of securities at the time of listing to support their secondary market liquidity.

8. When assessing this waiver application, the Exchange noted that:

- The warrants were to be offered to Company A's existing shareholders under a rights issue. As Company A had a wide spread of shareholders, it was likely to have an open market in the warrants at the time of listing.
- Listing the warrants would provide a market for the shareholders to trade the warrants taken up by them.
- There was less concern on liquidity in the case of warrants as they could be exercised and converted into listed shares of Company A.

9. The Exchange considered it acceptable to waive the requirements on the number and spread of warrantholders at the time of listing of the warrants. However, if there were only a small number of warrantholders upon completion of the rights issue, the Exchange had the right to request Company A and the underwriters to explore the opportunity for placing some warrants to independent placees to increase the number of warrantholders at the time of listing.

Conclusion

10. The Exchange granted the waiver to Company A.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether Chapter 15 applies to unlisted warrants

Facts

1. A listed issuer (**Company A**) proposed to enter into a transaction involving the issue of warrants for which it did not propose to apply for a listing on the Exchange.

2. The terms of the warrants did not comply with the requirements of Rule 15.02 of the Listing Rules which provides, among other things, that: (i) the securities to be issued on exercise of the warrants must not, when aggregated with all other equity securities which remain to be issued on exercise of any other subscription rights, if all such rights were immediately exercised, whether or not such exercise is permissible, exceed 20% of the issued equity capital of the issuer at the time such warrants are issued; and (ii) such warrants must expire not less than one and not more than five years from the date of issue or grant.

3. Company A submitted that Chapter 15 did not apply to unlisted warrants.

Analysis

4. Rule 15.01 provides that Chapter 15 "applies to both options, warrants and similar rights to subscribe or purchase equity securities of an issuer which are issued or granted on their own by that issuer or any of its subsidiaries ("warrants") and to warrants which are attached to other securities but does not apply to any options which are granted under an employee or executive share scheme which complies with Chapter 17."

5. The rationale behind the placing of restrictions on warrants is to reduce the degree of uncertainty to which a listed issuer's share capital may be subject as a result of their potential dilution effect. In this regard, unlisted warrants could potentially create the same kind of uncertainty as listed warrants. Hence, no distinction is drawn in Chapter 15 between listed and unlisted warrants and, indeed, no such distinction should be drawn.

Conclusion

6. Company A decided to restructure the transaction so that the warrants would comply with the requirements of Chapter 15.

Whether a listed issuer could issue convertible debentures with warrants while it had used up the 20 percent limit at the date of the agreement for the issue

Facts

1. A listed issuer (**Company A**) entered into an agreement for the issue of two tranches of convertible debentures with warrants.

2. Tranche 1 of the convertible debentures would be issued within a month. If the Tranche 2 conditions were fulfilled within the next two months, Company A could at any time during a specified period require holders of the convertible debentures to subscribe for Tranche 2 of the convertible debentures.

3. On subscription of the convertible debentures, holders of the convertible debentures would be entitled to be issued, by way of bonus, warrants carrying rights to subscribe an amount equal to 10% of the principal amount of the convertible debentures for two years commencing from the date of the Tranche 1 issue.

4. Company A had outstanding warrants, the shares to be issued upon exercise of which amounted to 20% of Company A's then issued share capital.

5. Company A submitted that the issue of the new warrants would not exceed the 20% limit prescribed under Rule 15.02(1) as:

   - the convertible debentures would be subscribed in two stages. Company A might have sufficient time to repurchase an equivalent amount of the existing warrants before the issue of the new warrants, thereby preventing the 20% limit from being exceeded; and

   - if the repurchase of the existing warrants was precluded by the relevant dealing restrictions, the existing warrant holders could surrender the existing warrants to Company A to ensure compliance with the 20% limit.

Analysis

6. The shares to be issued upon exercise of the new warrants, when aggregated with the shares to be issued upon exercise of the existing warrants, must not exceed 20% of Company A's issued share capital as at the date of the agreement.

7. The proposal for surrender of the existing warrants was not acceptable since it was viewed as a means to circumvent the 20% limit.

Conclusion

8. Company A could not issue the new warrants since, at the date of the agreement relating to the issue, it had used up the 20% limit under Rule 15.02(1).

9. Company A subsequently entered into a supplemental agreement to cancel the bonus issue of warrants.

Issue of warrants

1. Is a listed issuer required to seek shareholders' approval for a proposed bonus issue of warrants to its existing shareholders on a pro-rata basis?

Yes. While MB Rule 13.36(2)(a) / GEM Rule 17.41(1) exempts an offer of securities to existing shareholders on a pro-rata basis, a bonus issue of warrants must be approved by shareholders in general meeting unless they are issued under a general mandate according to MB Rule 15.02 / GEM Rule 21.02.

MB Rules 13.36(2)(a) and 15.02
GEM Rules 17.41(1) and 21.02
First released: November 2008; last updated: May 2024

Guidance on bonus issues of shares

I. Purpose

1. This letter provides guidance on the Exchange's approach in handling bonus issues of shares by listed companies.

II. Relevant Listing Rules

2. Main Board Rule 2.03 (GEM Rule 2.06) states that:

   "The Listing Rules reflect currently acceptable standards in the market place and are designed to ensure that investors have and can maintain confidence in the market and in particular that: -

   …

   (2) the issue and marketing of securities is conducted in a fair and orderly manner … "

3. Main Board Rule 2.06 (GEM Rule 2.09) states that:

   "Suitability for listing depends on many factors. Applicants for listing should appreciate that compliance with the Exchange Listing Rules may not of itself ensure an applicant's suitability for listing. The Exchange retains a discretion to accept or reject applications and in reaching their decision will pay particular regard to the general principles outlined in rule 2.03 [GEM rule 2.06]. …"

4. Main Board Rule 8.20 (GEM Rule 11.30(2)) states that"

   "Listing must be sought for all further issues of securities of a class already listed prior to the issue of the securities."

III. Guidance

5. A bonus issue of shares involves a listed company issuing new shares and/or transferring treasury shares to its existing shareholders, credited as fully paid out of its reserves or profits, in proportion to their shareholdings[1].

[1] When a company issues bonus shares under the "no-par" regime, such shares will have no nominal value, meaning the company is no longer required to transfer an amount to share capital if it issues shares for no consideration, unless it elects to do so (for example, by capitalising profits). Therefore, a company may allot and issue bonus shares either with or without increasing its share capital.

6. In addition to the specific Rule requirements on this type of issues, listed companies must also comply with the general principle of the Listing Rules to ensure that their bonus issues of shares are conducted in a fair and orderly manner. Listed companies should observe the following guidance which is not meant to be exhaustive. The references to an allotment or issue of shares shall include a transfer of treasury shares.

Size of bonus issues

7. Under the current trading arrangements, there is a time interval between the ex-entitlement date for a bonus issue (the **ex-date**)[2] and the date of allotment of the bonus shares (the **allotment date**). The previous closing share price is adjusted downward on the ex-date but the bonus shares would not be available for trading until the allotment date, causing a squeeze in the availability of shares and significant price fluctuations during the ex-entitlement period. The Exchange noted untoward price fluctuations in a number of cases where listed companies conducted bonus issues of shares with a large distribution ratio.

8. Generally, the reason given by companies for conducting bonus issues of shares[3] is to increase the liquidity of their shares in the market. This could also be achieved by effecting a share subdivision. Both bonus issues and share subdivisions serve to increase the number of shares outstanding and reduce the share price.

9. It is the responsibility of listed companies to ensure that their issues of bonus shares are conducted in a fair and orderly manner. The Exchange may not grant listing approval for large scale bonus issues of shares where there is reasonable likelihood of disorderly trading during the ex-entitlement period. In these circumstances, the Exchange will normally expect listed companies to adopt share subdivisions. This would avoid disorderly trading during the ex-entitlement period of bonus issues of shares. Generally, the Exchange is likely to raise concern about the operation of an orderly market when a company proposes a bonus issue of shares of 200% or more of existing issued shares (excluding treasury shares). This is despite that the Exchange may raise the same concern even if the bonus issue proposed by a company is of a smaller scale after considering the relevant facts and circumstances.

10. The Exchange will grant listing approval for large scale bonus issue of shares only in exceptional circumstances. For example, if there are regulatory restrictions for the company to effect a share subdivision under the laws in the place of its incorporation or the requirements of other stock exchange where it is dually listed. In these circumstances, the company must demonstrate that its proposed issue is not likely to give rise to disorderly trading during the ex-entitlement period.

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[2] Under the T+2 settlement cycle, shares will be traded ex-entitlements to the bonus issue on the trading day immediately before the record date (or the last registration date where there is a book closure). Share price will be adjusted downward on the ex-date in accordance with the distribution ratio. A portion of the shareholders' holdings in the company will not be tradeable until the bonus shares are issued or transferred to the shareholders.

[3] As highlighted in the Securities and Futures Commission's Corporate Regulation Newsletter of March 2016, it could be misleading or inaccurate if a company discloses its bonus issue of shares as "a reward" to shareholders or a means to widen its capital base.

Timetable for bonus issues

11. Listed companies should also follow the guidance set out in the "Guide on distribution of dividend and other entitlements" when planning their bonus issues. In particular, they should keep the time interval between the ex-date and the allotment date as short as practicable. Where a bonus issue is subject to condition(s), the company must clearly disclose the condition(s) in the bonus issue announcement.

Restrictions

12. Under Main Board Rule 13.64A (GEM Rule 17.76A), a listed company must not undertake a subdivision or bonus issue of shares if its share price adjusted for the subdivision or bonus issue is less than HK$1 based on the lowest daily closing price of the shares during the six-month period before the announcement of the subdivision or bonus issue.

Whether the Exchange would approve the proposed share subdivision and increase in board lot size shortly after the listed issuer completed a rights issue and a share consolidation

Facts

Background

1. About 6 months ago, a Main Board issuer (**Company A**) announced a rights issue of shares at a discount to the market price. As the theoretical ex-right price would drop to about HK$0.1 based on the then share price, Company A also announced a 10 into 1 share consolidation to bring the theoretical price up proportionally with a view to ensuring compliance with Rule 13.64.

2. About 5 months later after the announcement, the rights issue and share consolidation were completed. Between the announcement date and the completion date, Company A's shares were trading in the price range of HK$0.09 to HK$0.19 (or HK$0.9 to HK$1.9 after the price adjustments for the rights issue and share consolidation).

Proposal

3. One month after the completion of the share consolidation, Company A proposed a 1 into 5 share subdivision, and a change in trading board lot size from 2,000 shares to 8,000 shares. Its shares were then trading at prices of about HK$1.7 to HK$2.

4. Company A was of the view that the liquidity in its shares was low due to the high trading price in its shares and board lot value when compared with those of other similar listed companies. Based on the then share price, after the proposed share subdivision, the adjusted share price would be reduced to HK$0.32 and the adjusted board lot value would exceed HK$3,200.

5. Under Rule 13.52B(1), Company A consulted the Exchange on its proposed share subdivision and the related trading arrangements.

Relevant Listing Rules

6. Rule 2.03 states that:

"The Listing Rules reflect currently acceptable standards in the market place and are designed to ensure that investors have and can maintain confidence in the market and in particular that:—

(1) …;

(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; and

(6) ….

In these last four respects, the rules seek to secure for holders of securities, other than controlling interests, certain assurances and equality of treatment which their legal position might not otherwise provide."

7. Rule 13.64 states that:

"Where the market price of the securities of the issuer approaches the extremities of HK$0.01 or HK$9,995.00, the Exchange reserves the right to require the issuer either to change the trading method or to proceed with a consolidation or splitting of its securities."

8. As set out in the Exchange's Guide on Trading Arrangements for Selected Types of Corporate Actions, for the purpose of Rule 13.64, the Exchange considers any trading price less than HK$0.1 to be approaching the extremity.

9. Rule 13.52B(1) states that:

"Where the subject matter of the document may involve a change in or relate to or affect arrangements regarding trading in the issuer's listed securities …, the issuer must consult the Exchange before the document is issued. The document must not include any reference to a specific date or specific timetable in respect of such matter which has not been agreed in advance with the Exchange."

Analysis

10. Issuers may effect share consolidation or subdivision to change the numbers of their shares in issue, resulting in a corresponding increase or decrease in the market price per share. These changes may serve to facilitate trading activities and improve market efficiency. As these corporate actions affect the arrangements for trading shares on the Exchange, issuers must seek the Exchange's prior approval.

11. While share consolidation or subdivision itself do not change shareholders' proportionate interests in an issuer, such corporate actions involve costs and they would result in existing shareholders holding odd lots or fractional shares, which are usually traded at prices lower than those in complete board lots. While some issuers would arrange for intermediaries to offer matching services, this could not eliminate the negative effect of such corporate actions for the shareholders, particularly for smaller shareholders holding one or a few board lots.

12. In light of this, prior to proceeding with share consolidation or subdivision, directors should consider all the relevant factors and take reasonable steps to demonstrate that the proposal can serve its intended purpose and is in the best interest of the issuer and its shareholders. Factors that directors should take into account, which are not exhaustive:

- whether the proposed action is justifiable in light of the potential costs and negative impact arising from creation of odd lots to shareholders;
- that the frequency of any share consolidation or subdivision be kept to a reasonable level to minimize the costs arising from odd lots as a result of unnecessary repeated actions;
- whether a proposed share consolidation or subdivision may have an effect of offsetting the intention of any prior, or other simultaneous corporate action (e.g. share consolidation followed by share subdivision within a relatively short time span, or share subdivision made in conjunction with an increase in board lot size);
- whether there is a sufficient demonstration period to support that the share trading price is not temporary and a proposed share consolidation or subdivision is justified (e.g. a reasonable period of high trading price to justify a proposed share subdivision); and
- whether there is any other available alternative methods (e.g. change in board lot size instead of share subdivision).

13. When considering the case of Company A, the Exchange noted that:

- Company A submitted that the purpose of the proposed 1 into 5 share subdivision was to increase trading liquidity. However, its proposal also involved an increase in board lot size by 4 times, and the adjusted board lot value would only be slightly below the current value. The combined effects of these corporate actions might not entirely support the purported reason for proposing the actions. Company A failed to justify the proposal and why it would be in the best interest of the shareholders as a whole, particularly taking into account the potential odd lots creation.
- While there was recent increase in Company A's share price to above HK$2, its shares were trading at most time during the last 6 months at the price of around HK$0.9 to HK$1 only (after the adjustment for share consolidation). Company A was unable to demonstrate that its shares were trading at fairly high prices over a reasonable period to justify its proposed share subdivision.
- The proposed share subdivision was put forward shortly after completion of the share consolidation. It is not clear how the two actions could be justified within a short period.
- Company A failed to consider other alternatives (e.g. reducing the board lot size to bring down the value each board lot for its intended purpose of increasing trading liquidity).

14. In light of the above, the Exchange considered that Company A had not provided sufficient reasons to support its proposal at this time.

Conclusion

15. The Exchange did not approve the proposed share subdivision and increase in board lot size.

Subsequent development

16. Under Rule 13.64A (which became effective on 3 July 2018), an issuer must not undertake a subdivision (or bonus issue) of shares if its share price adjusted for the subdivision (or bonus issue) is less than HK$1 based on the lowest daily closing price of the shares during the six-month period before the announcement of the share subdivision (or bonus issue). Without prejudice to the requirements of Rule 13.64A, listed issuers proposing share subdivision or consolidation should continue to follow the Exchange's guidance set out in this Listing Decision.

HKEX Guidance Letter
HKEX-GL118-23

December 2023 (Updated in January 2024)

Guidance on the electronic submission of prospectus and accompanying documents to the Exchange and the Companies Registry for authorisation and registration

Purpose

1. This letter provides guidance on the manner in which documents must be electronically delivered to the Exchange for an application for authorisation of the registration of a prospectus in accordance with the Listing Rules and the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32) (**C(WUMP)O**) (*subject to the effective date and transitional arrangements set out in paragraphs 15 to 17 below*).[1]

2. Listed issuers issuing prospectuses and their advisers are strongly advised to review the requirements as listed out in this guidance letter and in the relevant laws and regulations and ensure that the application for authorisation for registration of the prospectus, the prospectus, its related application forms and other accompanying documents delivered to the Exchange for authorisation of registration are duly prepared in accordance with those requirements.

Relevant Listing Rules and legislation

3. In respect of listed issuers, Main Board Rule 9.22(2) (GEM Rule 12.26E(2)) provides that in cases where a listing document constitutes a prospectus under the C(WUMP)O, the following documents must be submitted to the Exchange by 11 a.m. on the intended date of authorisation of registration of prospectus:

   (a) an application for authorisation for registration of the prospectus under section 38D(3) or section 342C(3) of the C(WUMP)O (as the case may be);

   (b) two copies of the prospectus, duly signed[2] in accordance with section 38D(3) or section 342C(3) of the C(WUMP)O and having endorsed thereon or annexed thereto the documents required under the relevant section;

   (c) in respect of every Chinese translation of the prospectus,

      (i) a certificate issued by the translator certifying that the Chinese translation of the English version of the prospectus is true and accurate; and

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1 For the avoidance of doubt, this includes listing documents relating to debt securities which must be registered in accordance with the C(WUMP)O and, pursuant to Main Board Rules 24.15 and 25.01 (GEM Rule 28.17 and 29.01), are subject to the procedures for authorisation for registration set out in Chapter 11A (GEM Rules Chapter 15) and Main Board Rule 9.11(33) (GEM Rule 28.15).

2 For the purpose of this guidance letter, the term "signed" in respect of the "signing" of a prospectus refers to, as the case may be: (i) the act of signing by every director or proposed director of the company or by his agent authorised in writing under section 38D(3) of the C(WUMP)O; or (ii) the act of certifying by two members of the governing body of the company or by their agents authorised in writing, as envisaged under section 342C(3) of the C(WUMP)O. See further information in paragraph 5.

(ii) a certificate issued by the issuer certifying that the translator is competent to have given the above certificate; and

(d) any power of attorney, or other authority under which the prospectus is signed.

4. Note to Main Board Rule 2.07(3A) (GEM Rule 2.21) states that, in respect of documents submitted to the Exchange for the purpose of the authorisation of the registration of a prospectus, they must be submitted in the manner and via the means prescribed by the C(WUMP)O and any related guidance materials published from time to time.

5. Under the C(WUMP)O[3], a prospectus to be submitted for the purpose of seeking authorisation of the registration of a prospectus must be an *original* copy signed by such persons as required under section 38D(3) or section 342C(3) of the C(WUMP)O[2] (as the case may be) (**Designated Signatories**), while other documents (**Accompanying Documents**) to be endorsed on or attached to the prospectus to be registered may be *originals* or *certified* copies (certified as true copies by persons recognised under section 39C(b) or section 342CC(b) of the C(WUMP)O (as the case may be) (**Approved Certifier**)[4]).

6. The Electronic Transactions Ordinance (Cap. 553) (**ETO**) establishes a framework under Hong Kong law for the recognition of electronic records[5] and signatures, giving them the same legal status as their paper counterparts. Under the ETO[6], where a rule of law requires the signature of a person on a document, an electronic signature or, in the case where a Government entity is involved, a digital signature (as defined in the ETO) of that person satisfies such requirement.

Guidance

7. A prospectus, its related application forms and its Accompanying Documents[7] to be submitted for the purpose of seeking authorisation of the registration of a prospectus pursuant to the C(WUMP)O must be submitted to the Exchange in electronic form.

8. Digital signatures must be used for: (a) signing[2] the original copies of the prospectus, its related application forms, and any Accompanying Documents[7] (if the original Accompanying Document is submitted); and (b) certifying a copy of any Accompanying Document as a true copy[8] (if a certified copy of the Accompanying Document is submitted).

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3 Sections 38D and 342C of the C(WUMP)O.

4 The persons recognised under sections 39C(b) and 342CC(b) of the C(WUMP)O are: (i) a director (or a member of the governing body of the company) or the company secretary of the company or an agent of the director (or a member of the governing body of the company) or the company secretary authorised in writing for the purpose by the director (or such member) or company secretary; (ii) a solicitor within the meaning of section 2(1) of the Legal Practitioners Ordinance (Cap 159) or a certified public accountant within the meaning of section 2 of the Professional Accountants Ordinance (Cap 50); and (iii) a notary public within the meaning of section 2(1) of the Legal Practitioners Ordinance (Cap 159).

5 An "electronic record" is defined under the ETO to mean a record generated in digital form by an information system, which can be (a) transmitted within an information system or from one information system to another; and (b) stored in an information system or other medium.

6 Section 6 of the ETO.

7 These documents include items 2 to 8 set out in Appendix I. Pursuant to section 3 of and Schedule 1 to the ETO, powers of attorney are excluded from the application of the relevant sections of the ETO. Accordingly, powers of attorney cannot be executed by digital signature and shall be executed following appropriate wet ink procedures in accordance with applicable laws. Thus, no original power of attorney may be delivered in electronic form but copies of powers of attorney certified as true copies by Approved Certifiers' personal Recognised Digital Signatures may be delivered in electronic form for seeking authorisation and registration.

8 A scanned copy of a physical record bearing a physical signature will not be accepted nor will an electronic record bearing just an electronic signature that does not meet the requirements of this guidance letter.

9. A digital signature must be supported by a recognised certificate, generated within the validity of that certificate and used in accordance with the terms of that certificate (**Recognised Digital Signature**). The terms "*recognised certificate*" and "*within the validity of that certificate*" shall have the meanings ascribed to them under the ETO. The following certification authorities in Hong Kong are recognised for issuing digital certificates:

   (a) The Postmaster General (Hongkong Post Certification Authority) issues recognised digital certificates under the brand name of "e-Cert"[9];

   (b) Digi-Sign Certification Services Limited issues digital certificates with the brand name of "ID-Cert"[10].

10. To apply for the authorisation of the registration of prospectus, a listed issuer (or its adviser) must submit, by email,[11] to the Exchange by 11 a.m. on the intended date of authorisation of the prospectus:[12]

   (i) an original copy of the prospectus, together with originals of its related application forms, signed[2] by the Designated Signatories using their Recognised Digital Signatures;

   (ii) original Accompanying Documents[7] signed by the relevant authorised signatories using their Recognised Digital Signatures, **or** copies of the Accompanying Documents certified as true copies by Approved Certifiers with their Recognised Digital Signatures; and

   (iii) where a prospectus or a related application form is signed by an authorised person by virtue of a power of attorney or any other authority:

      (a) a copy of each power of attorney certified as true copy by an Approved Certifier with his Recognised Digital Signature; or

      (b) each original authority signed by the relevant signing party with Recognised Digital Signature or a copy thereof certified as true copy by an Approved Certifier with his Recognised Digital Signature;

   provided that in case only a certified copy of any document has been submitted as aforesaid, the listed issuer (or its adviser) must, upon demand by the Exchange if it thinks fit, produce the original to the Exchange for inspection.

11. To grant an authorisation for registration of a prospectus, the Exchange will send the listed issuer (or its adviser), by email, a certificate of authorisation, the prospectus and its related application forms each signed by the Exchange with its own Recognised Digital Signature together with the Accompanying Documents authorised by the Exchange.

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9 See Hongkong Post e-Cert - Types of e-Cert for further details.

10 See Digi-Sign Certification Services Limited (dg-sign.com) for further details.

11 The email(s) should be sent to the relevant team email of the Listing Regulation and Enforcement Department of the Exchange. The subject of the email(s) should contain the relevant information set out as follows: *"[COMPANY NAME] (Stock Code: [CODE]) - ([CASE NUMBER]) | Prospectus Registration Documents*". Each email should not exceed a message size of 25MB and, if necessary, multiple emails may be used to send in the document bundle.

12 All documents submitted to the Exchange for application of authorisation of registration of prospectus must be submitted in PDF, in a searchable and printable format; and in a file type, mode and setting that enables the Exchange to verify the digital signatures on the document and (in respect of a prospectus and its related application forms) apply the Exchange's digital signature to the document. Each digital signature must have a text statement inserted adjacent to the signature block which sets out the name and capacity of the signatory as follows: "*[D]igitally signed by [FULL NAME OF THE SIGNATORY AS PER GOVERNMENT ISSUED IDENTIFICATION DOCUMENT], [CAPACITY e.g. director, or authorised agent / attorney of [name of the person authorising or the donor of power]]*". If certification wording in respect of a certification by a signatory is required to be set out in a document, such certification wording should be inserted as a text statement adjacent to the signature block of the related digital signature.

12. The listed issuer (or its adviser) should forward the email(s) and the attachments it receives from the Exchange (as set out in paragraph 11 above), by email, to the Companies Registry for registration together with: (a) evidence of payment of the required registration fee; and (b) a statement confirming to the Companies Registry that documents attached to the email(s) so forwarded to the Companies Registry are documents issued or authorised by the Exchange for registration of prospectus and they have not been altered, substituted or otherwise modified subsequent to the Exchange's authorisation.

13. **Appendix I** to this letter sets out documentary requirements in full. **Appendix II** contains a diagram illustrating the prospectus authorisation and registration workflow.

14. Under section 32 of the Companies Ordinance, the Registrar of Companies may, in relation to any document required or authorised to be delivered to the Registrar of Companies under the C(WUMP)O, specify the requirements as to the authentication of the document or the manner of delivery of the document. Market participants are encouraged to also refer to the latest Gazette notice and circular published by the Registrar of Companies from time to time for details of the latest requirements in relation to the delivery of prospectus and Accompanying Documents to the Companies Registry for registration as specified by the Registrar of Companies.

Effective date and transitional period

15. From 1 January 2024, listed issuers (and their advisers) may start submitting documents electronically for application for authorisation of registration of a prospectus by following the guidance set out in this letter.

16. From 1 July 2024, the Exchange will no longer accept documents sent to it for the purpose of the authorisation of registration of a prospectus that do not meet the requirements of this guidance letter.

17. During the transitional period from 1 January to 30 June 2024, listed issuers (or their advisers) must submit to the Exchange and the Companies Registry all the relevant documents either wholly in electronic form by email or wholly in hard copy form.

Appendix I – Documentary requirements for prospectus authorisation and registration[13]

	Action	Relevant documents	Signing party	Digital signature requirements
Prospectus Authorisation				
1.	Listed issuer (or its adviser) to submit the documents for authorisation of registration of prospectus by email to the Exchange	Prospectus and related application forms	Designated Signatories	Signed by Designated Signatories using their personal Recognised Digital Signatures
2.		Power of Attorney Other authority (i.e. any authority other than a power of attorney)	Donor of the power Signing parties of the authority	In the case of originals *(only for an authority other than a power of attorney)*: • Signed by the relevant signing parties using their organisational/personal (as the case may be) Recognised Digital Signatures In the case of certified copies *(for both power of attorney and other authority)*: • Certified by an Approved Certifier[14] using personal Recognised Digital Signature of the Approved Certifier
3.		Translator Certificate	Translator	In the case of originals: • Signed by the relevant signing parties using their organisational/personal (as the case may be) Recognised Digital Signatures In the case of certified copies: • Certified by an Approved Certifier using personal Recognised Digital Signature of the Approved Certifier
4.		Translator Competency Certificate	Listed issuer	
5.		Expert consent letters[15]	Experts	

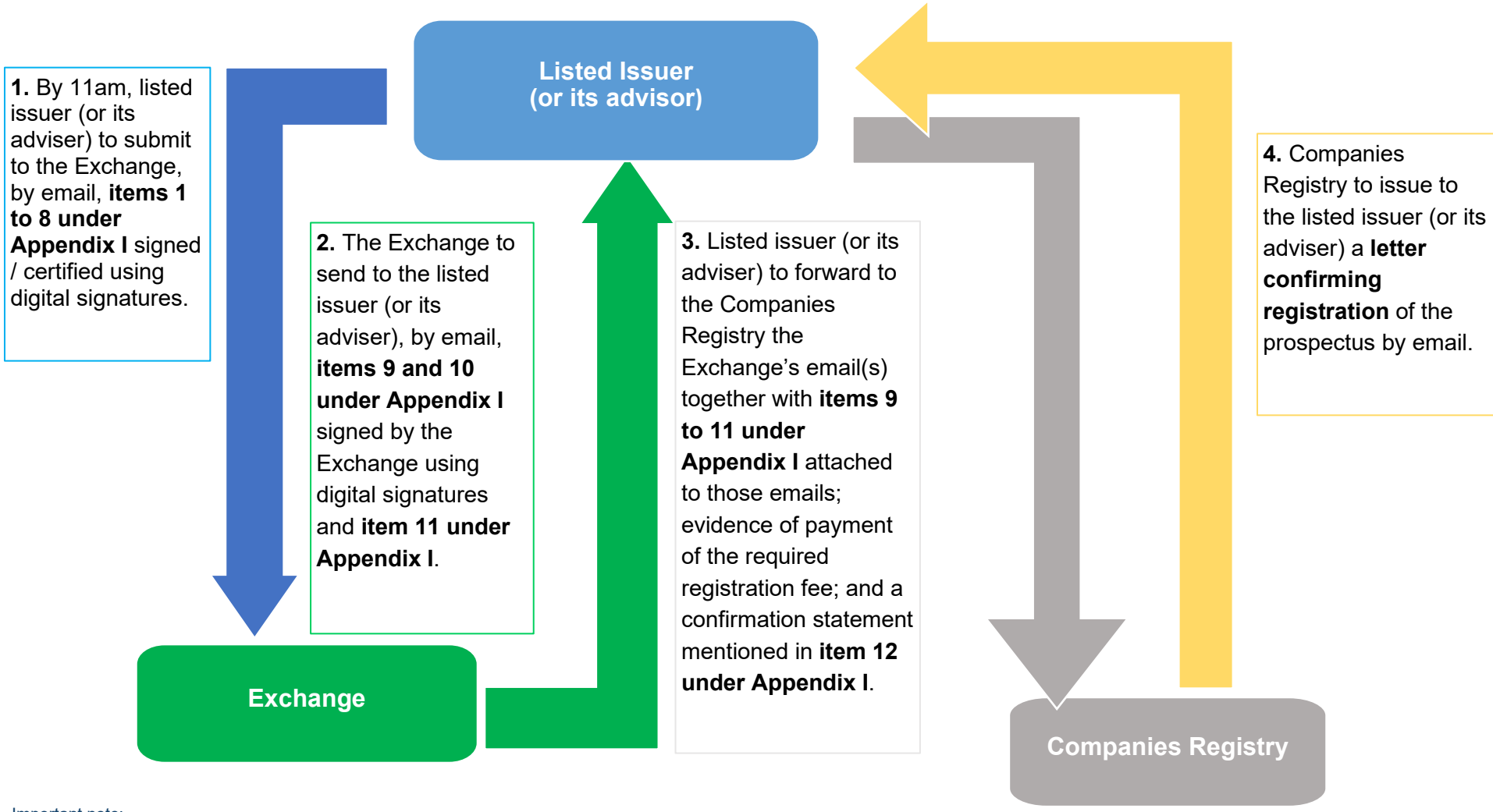
[13] Please refer to the C(WUMP)O for further details on requirements on prospectus authorisation and registration.
[14] The Approved Certifier certifying a copy of a power of attorney or an authority as a true copy should not be the donee of that power of attorney or the authorised agent under that authority.
[15] Section 38D(3)(a) / section 342C(3)(a) of the C(WUMP)O

	Action	Relevant documents	Signing party	Digital signature requirements
6.		Material contracts[16]	Signing parties of the material contracts	
7.		A list of the name(s), description(s) and address(es) of the vendor(s) of the sale shares[17], if any	N/A[18]	
8.		Statement of adjustments made by the reporting accountant,[19] if any	Reporting accountant	
Authorisation of Registration and Registration of Prospectus				
9.	The Exchange to send email(s) attaching the authorised documents and certificate of authorisation to the listed issuer (or its adviser)	Certificate of Authorisation	The Exchange	Signed by the Exchange using the Exchange's organisational Recognised Digital Signature
10.		Prospectus and related application forms	The Exchange	Signed by the Exchange using the Exchange's organisational Recognised Digital Signature

16 Section 38D(3)(b)(i) / section 342C(3)(b)(i) of the C(WUMP)O
17 Section 38D(3)(b)(ii) / section 342C(3)(b)(ii) of the C(WUMP)O
18 No signature requirement for this document.
19 Section 38D(3)(b)(iii) / section 342C(3)(b)(iii) of the C(WUMP)O

	Action	Relevant documents	Signing party	Digital signature requirements
11.		Accompanying Documents	N/A	N/A
12.	Listed issuer (or its adviser) to forward to the Companies Registry the email(s) (with the documents attached) from the Exchange together with evidence of payment of the required registration fee and a confirmation statement as set out in paragraph 12 of the guidance letter	N/A	N/A	N/A
13.	Companies Registry to send to the listed issuer (or its adviser) by email a letter confirming registration of the prospectus	Confirmation letter	Registrar of Companies	N/A

Appendix II –
Workflow for electronic submission of prospectus and accompanying documents for authorisation and registration



Conversion of PRC issuers' unlisted shares into H shares for listing on the Exchange

1. For a listed issuer incorporated in the PRC, under what circumstances can its unlisted shares be converted into H shares for listing on the Exchange?

The conversion of unlisted shares into H shares is governed by the PRC regulations and the PRC issuer's articles of association. Where the PRC issuer proposes to convert all or part of its unlisted shares held by domestic/foreign shareholders into H shares, it should ensure that the conversion process is clearly disclosed and explained to the public. This would include, among others, the filing and approval requirements of the relevant PRC regulatory authorities and any requisite internal approval process under its articles of association.

The PRC issuer must seek the Exchange's approval for the listing of such H shares before conversion. In general, the Exchange would approve the issuer's listing application, subject to its compliance with the relevant requirements under the PRC regulations and its articles of association.

The PRC issuer should announce the effective date of the conversion after receiving all necessary approvals and filing notification and disclose the changes in its unlisted shares and H shares in issue as a result of the conversion in its next day disclosure return and monthly return.

MB Rules 2.03, 2.13 and 13.09
GEM Rules 2.06, 17.10 and 17.56
First released: December 2023

7

Public float

In a reverse takeover where the listed issuer was deemed to be a new listing applicant, whether the minimum public float requirement could be satisfied by placing of new shares and/or existing shares by the listed issuer and/or its controlling shareholder prior to the completion of the transaction

Facts

1. A Main Board listed issuer and a deemed new listing applicant under Listing Rule 8.21C (**Company A**) entered into an agreement with its controlling shareholder (**Parentco**) for the acquisition of certain target companies held by Parentco (**asset injection transaction**). As the asset injection transaction constituted a very substantial acquisition involving a change in control of Company A, it was treated as a reverse takeover transaction under the Listing Rules. Consequently, the asset injection transaction was deemed a new listing of Company A's shares pursuant to Listing Rule 8.21C. It follows that the asset injection transaction required the issue to shareholders of Company A a circular in the form of a listing document and the transaction required the approval of independent shareholders of Company A in a special general meeting.

2. In order to maintain the minimum public float requirement upon completion of the asset injection transaction, Company A and Parentco proposed the following three options:-

   Option 1 – Parentco placing existing shares;

   Option 2 – Company A placing new shares;

   Option 3 – A combination of placing existing and new shares by Parentco and Company A.

Relevant Listing Rules

3. Listing Rule 7.11 provides that:

   '*The Exchange may be prepared to allow preliminary arrangements and placings to be made to dispose of securities before the start of dealings where necessary to comply with the requirement in rule 8.08(1) that a minimum prescribed percentage of any class of listed securities must at all times be held by the public.*'

4. Listing Rule 8.08(1) provides that:

'*There must be an open market in the securities for which listing is sought. This will normally mean that: –*

(1) (a) at least 25% of the issuer's total issued share capital must at all times be held by the public…'

(Listing Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

5. Listing Rule 8.21C provides that:

'Without prejudice to the generality of other applicable provisions of the Exchange Listing Rules, a listed issuer that is treated as if it were a new applicant must meet all the basis conditions set out in this Chapter 8, unless otherwise waived by the Exchange. In particular, where there are assets to be injected into or acquired by the listed issuer, the assets to be injected or acquired or the enlarged group must meet the requirements under rule 8.05, and the enlarged group must meet all the other basic conditions set out in this Chapter 8. In cases of doubt, issuers and advisers should consult the Exchange at an early stage.'

6. Listing Rule 10.07(1)(a) provides 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 dispose of shares in the issuer '*in the period commencing on the date by reference to which disclosure of the shareholding of the controlling shareholders is made in the listing document and ending on the date which is 6 months form the date on which dealings in the securities of a new applicant commence on the Exchange*'.

Analysis

Public float requirement under Listing Rule 8.08

7. The Exchange stated in paragraph 118 of the *Consultation Conclusions on Proposed Amendments to the Listing Rules relating to Initial Listing and Continuing Listing Eligibility* issued in January 2004 (**Consultation Conclusions**) that with regard to the treatment of new listing applications arising from reverse takeover transactions, and in particular, with regard to asset injections, the same set of initial listing eligibility criteria should be consistently and fairly applied in order to ensure a level playing field for all listing applicants seeking a listing on the Exchange.

8. The Exchange concluded in paragraph 123 of the Consultation Conclusions that the Main Board Listing Rules should be amended such that in a case of "reverse takeover" transaction including asset injection in a rescue situation, the enlarged group (or where appropriate, the NewCo, or assets to be injected) would be required to comply with the initial listing eligibility criteria. This would mean that the enlarged group of the existing issuer, or the NewCo, must meet the public float requirements and the spread of shareholders requirements under Listing Rule 8.08.

9. Pursuant to the Consultation Conclusions, Listing Rule 8.21C was adopted and took effect on 31 March 2004.

10. In light of its recent statements in the Consultation Conclusions, the Exchange ordinarily will not entertain a proposal to waive the requirements of Rule 8.08 to allow time for the restoration of public float after the completion of a deemed new listing transaction. Accordingly, the Exchange required strict compliance with Listing Rule 8.08 in this case. The Exchange would regard the date of completion of the asset injection transaction as the date of the deemed new listing of the shares of Company A. Consequently, Company A was required to demonstrate to the Exchange that the requirements under Listing Rule 8.08 would be satisfied on or before the completion of the asset injection transaction.

Consequential waiver of Listing Rule 10.07

11. In the event of placings under proposed Option 1 and Option 3 mentioned in paragraph 2 above, Listing Rule 10.07(1) would operate to prohibit Parentco from disposing of Company A's shares within the prescribed restricted period. Therefore, the Exchange was asked to consider a waiver of Listing Rule 10.07(1) to afford Company A greater flexibility when acting to comply with Listing Rule 8.08.

12. Listing Rule 7.11 provides that the Exchange may be prepared to allow preliminary arrangements and placings to be made to dispose of shares of an issuer before the start of dealings where necessary to comply with the requirements of Listing Rule 8.08(1). The Exchange noted that the proposed placing arrangements were consistent with the spirit of Listing Rule 7.11. However, the Exchange also noted that one of the purposes of Listing Rule 10.07 is intended to ensure that controlling shareholders are committed to an issuer during its initial stage of listing, as a means to ensure the protection of investors.

13. In the present case, the Exchange noted that the proposed placings formed part of the asset injection transaction. This conferred sufficient protection on the shareholders of Company A as the asset injection transaction would be subject to approval by independent shareholders. The proposed placing arrangements would also be disclosed in Company A's circular to the shareholders prior to the special general meeting. In view of the above safeguards, the Exchange concluded that it was appropriate to grant a waiver of Listing Rule 10.07 for the purpose of facilitating the placings by Parentco under the above proposed Option 1 or Option 3.

Conclusion

14. Based on the above facts and circumstances and the Exchange's analysis of the Listing Rules, the Exchange determined that:-

    a. the proposed placing arrangements by the Company and/or Parentco to maintain the minimum public float under Listing Rule 8.08 before completion of the asset injection were arrangements acceptable to the Exchange;

    b. the Exchange would grant a waiver of Listing Rule 10.07 so that Parentco, a controlling shareholder, would be able to place down its shares as contemplated under the proposed placing arrangements within the restricted period.

Note: Listing Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Listing Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would allow a listed issuer to resume trading in its shares when it had restored its public float to 15 per cent

Parties

- **Company A** – a Main Board issuer
- **Company B** – Company A's controlling shareholder

Facts

1. Company B made a general offer for Company A's shares under the Takeovers Code after it had acquired a controlling interest in Company A.

2. When the offer closed, the percentage of Company A's shares in public hands fell to 13 per cent. There was a lack of open market for the shares. As a result, trading in the shares was suspended.

3. Company A noted from the Rules that the Exchange will normally require suspension of trading in an issuer's securities when its public float falls below 15 per cent. It asked whether trading in its shares could resume when it had restored the public float to 15 per cent.

Relevant Listing Rules

4. Rule 8.08(1) states that:

   There must be an open market in the securities for which listing is sought. This will normally mean that:

   (a) at least 25 per cent of the issuer's total number of issued shares must at all times be held by the public.

   …

   (Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

5. Rule 13.32 states that:

   (1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …

   …

(3) If the percentage falls below the minimum, the Exchange reserves the right to require suspension of trading in an issuer's securities until appropriate steps have been taken to restore the minimum percentage of securities in public hands. In this connection, the Exchange will normally require suspension of trading in an issuer's securities where the percentage of its public float falls below 15 per cent...

Analysis

6. Rules 8.08 and 13.32 seek to ensure an open market for trading in listed securities and require at least 25 per cent of the securities be held by the public.

7. Therefore, when the issuer's public float falls below 25 per cent, trading will be suspended if it is necessary to avoid a disorderly market. The Exchange will allow resumption of trading when appropriate steps have been taken to restore a 25 per cent public float.

8. The Rules also provide guidance that the Exchange would normally consider a public float of less than 15 per cent be too small to maintain an orderly market and require a suspension of trading in this situation. This does not mean that the Exchange would accept a public float of 15 per cent for resumption of trading.

Conclusion

9. Company A was required to restore its public float to at least 25 per cent before resumption of trading.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would cancel the listing of a listed issuer whose shares had been suspended from trading for a prolonged period due to insufficient public float

Facts[1]

1. Trading in shares of a Main Board issuer (**Company A**) had been suspended pending restoration of its public float.

2. At the time of trading suspension, Company A had two major shareholders (each holding about 45% of Company A's issued shares) and its public float was below 10%. After the suspension, there were certain takeover related matters involving a possible general offer of Company A's shares which might have affected Company A's plans to resolve the public float issue.

3. About eight months ago, Company A noted that those takeover related matters were resolved and there was no general offer of Company A's shares. Company A announced its intention to issue new shares to independent placees to restore the public float to at least 25%.

4. Since then, Company A had some discussions with its financial advisers but there was no material development on the proposed placing. It also submitted an alternative proposal to the Exchange but the proposal could not satisfactorily address the public float issue and did not proceed. In response to the Exchange's concern about the prolonged suspension of Company A's shares, Company A requested for an extension of time to resolve the public float issue until the market conditions had improved. However, no concrete plan or timetable was provided.

[1] Time reference is the time to date of the decision.

Relevant Listing Rules

5. Rule 6.01 provides that:

"Listing is always granted subject to the condition that where the Exchange considers it necessary for the protection of the investor or the maintenance of an orderly market, it may at any time direct a trading halt or suspend dealings in any securities or cancel the listing of any securities in such circumstances and subject to such conditions as it thinks fit, whether requested by the issuer or not. The Exchange may also do so where:— …

…

(2) the Exchange considers there are insufficient securities in the hands of the public …

…"

6. Rule 6.04 provides that:

"Where dealings have been halted or suspended, the procedure for lifting the trading halt or suspension will depend on the circumstances and the Exchange reserves the right to impose such conditions as it considers appropriate. The issuer will normally be required to announce the reason for the trading halt or suspension and, where appropriate, the anticipated timing of the lifting of the trading halt or suspension…The continuation of a suspension for a prolonged period without the issuer taking adequate action to obtain restoration of listing may lead to the Exchange cancelling the listing."

7. Rule 6.10 provides that:

"There may be cases where a listing is cancelled without a suspension intervening. Where the Exchange considers that any circumstances set out in rule 6.01 arise, it may:

(1) publish an announcement naming the issuer and specifying the period within which the issuer must have remedied those matters which have given rise to such circumstances. Where appropriate the Exchange will suspend dealings in the issuer's securities. If the issuer fails to remedy those matters within the specified period, the Exchange will cancel the listing. The Exchange may treat any proposals to remedy those matters as if they were an application for listing from a new applicant for all purposes, in which case, the issuer must comply with the requirements for new listing applications as set out in the Listing Rules; or

… "

8. Rule 8.08 provides that:

"There must be an open market in the securities for which listing is sought. This will normally mean that:

(1) (a) at least 25 % of the issuer's total number of issued shares must at all times be held by the public.

…"

(Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

9. Rule 13.32 provides that:

> *"(1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …*
>
> *(2) Once the issuer becomes aware that the number of listed securities in the hands of the public has fallen below the relevant prescribed minimum percentage the issuer shall take steps to ensure compliance at the earliest possible moment.*
>
> *…*
>
> *(3) If the percentage falls below the minimum, the Exchange reserves the right to require suspension of trading in an issuer's securities until appropriate steps have been taken to restore the minimum percentage of securities in public hands. In this connection, the Exchange will normally require suspension of trading in an issuer's securities where the percentage of its public float falls below 15%...*
>
> *…"*

Analysis

10. Rule 6.01 provides that where the Exchange considers it necessary for the protection of the investor or the maintenance of an orderly market, it may suspend trading or cancel the listing of any securities. The Rule also specifies certain circumstances under which the Exchange may suspend trading or cancel a listing, which include insufficient public float.

11. The continuation of a suspension for a prolonged period is detrimental to maintaining order or confidence in the market. It deprives shareholders' right from trading their shares or realising their investments in the market; and is not in the interest of the investing public. Rule 6.04 sets out the general principle that the continuation of a suspension for a prolonged period without the issuer taking adequate action to obtain restoration of listing may lead to the Exchange cancelling the listing.

12. For delisting under any of the circumstances set out in Rule 6.01, the Exchange may under Rule 6.10 specify a remedial period for the issuer to address the matter that gives rise to the trading suspension before delisting. The length of the remedial period will depend on the nature and complexity of the matter which the Exchange requires the issuer to rectify. Where trading is suspended due to insufficient public float, the Exchange will expect the issuer to address the matter within a reasonably short period of time.

13. In this case, trading in Company A's shares had been suspended for a prolonged period due to insufficient public float. Whilst Company A had announced its intention to restore the public float through placing of new shares, there was no material development over a period of eight months. In its latest submission, Company A was still unable to put forward any concrete plan or timetable to address the public float issue. The Exchange considered that Company A had not taken adequate actions to address the public float issue for resumption of trading.

14. Having considered the facts and circumstances of this case, the Exchange decided to commence the delisting process and gave Company A a six-month period to address the public float issue.

Conclusion

15. The Exchange served a notice to Company A on the commencement of the delisting process under Rules 6.01(2) and 6.10 on the ground that Company A had insufficient public float for a prolonged period. If Company A failed to address the public float issue within six months, the Exchange would proceed with cancellation of Company A's listing.

Subsequent development

16. Company A's public float had been restored to 25% within the six-month period as a result of the issue of new shares by Company A and the sale of existing shares by its controlling shareholder to independent placees. As a result, trading in Company A's shares had resumed.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether (i) a listed issuer could proceed with a share repurchase offer which might result in a lack of open market in its shares; and (ii) the Exchange would give consent to the listed issuer for issuing new shares within 30 days after completion of such offer to meet the public float requirement

Facts

1. A Main Board issuer (**Company A**) was dually listed on the Exchange and an overseas stock exchange. It proposed to withdraw its listing in the overseas stock exchange by making a share repurchase offer to all existing public shareholders in Hong Kong and the overseas market (**Offer**).

2. It intended to maintain a listing on the Exchange. For any shareholders in the overseas market who did not accept the Offer, their shares would be transferred to the Hong Kong branch register.

3. It would also issue new shares to certain independent institutional investors (**Investors**) for cash to finance part of the funding requirement for the Offer.

4. To ensure a minimum of 25% public float immediately after the Offer, Company A had obtained undertaking from the Investors and certain public shareholders not to accept the Offer.

5. However, if there was a very high take up of the Offer, Company A's shares would be held by a small number of shareholders and there might not be an open market for trading in the shares in Hong Kong upon completion of the Offer. To address the concern, Company A submitted that:

   a. it had a wide spread of shareholders with over 2,000 shareholders in the overseas market and over 60 shareholders in Hong Kong including nominee companies. More than 60% of the overseas shareholders were institutional investors;

   b. the subscription of new shares in Company A by the Investors and the business cooperation with them would enhance the value of Company A. Company A did not expect a high uptake of the Offer; and

   c. in the event that there was a concern about the lack of an open market in Company A's shares after the offer, it would place new shares to independent placees (**Possible Placing**) to ensure compliance with the public float requirement.

6. Company A asked whether the Exchange would allow it to proceed with the proposed Offer. It also sought the Exchange's consent to conduct the Possible Placing within 30 days after the Offer under Rule 10.06(3).

Relevant Listing Rules

7. Rule 8.08 states that:

"There must be an open market in the securities for which listing is sought. This will normally mean that:-

(1) (a) at least 25% of the issuer's total number of issued shares must at all times be held by the public;

…

(2) for a class of securities new to listing, at the time of listing there must be an adequate spread of holders of the securities to be listed, …. The number will depend on the size and nature of the issue, but in all cases there must be at least 300 shareholders; and

(3) not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders, …."

(Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

8. Rule 13.32 states that:

"(1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …

(2) Once the issuer becomes aware that the number of listed securities in the hands of the public has fallen below the relevant prescribed minimum percentage the issuer shall take steps to ensure compliance at the earliest possible moment…

(3) If the percentage falls below the minimum, the Exchange reserves the right to require suspension of trading in an issuer's securities until appropriate steps have been taken to restore the minimum percentage of securities in public hands. In this connection, the Exchange will normally require suspension of trading in an issuer's securities where the percentage of its public float falls below 15% (or 10% in the case of an issuer that has been granted a lower percentage of public float under rule 8.08(1)(d) at the time of listing).

(4) Where the percentage has fallen below the minimum, the Exchange may refrain from suspension if the Exchange is satisfied that there remains an open market in the securities…

…"

9. Rule 10.06(3) states that:

> "An issuer whose primary listing is on the Exchange may not make a new issue of shares or announce a proposed new issue of shares for a period of 30 days after any purchase by it of shares, whether on the Exchange or otherwise (other than an issue of securities pursuant to the exercise of warrants, share options or similar instruments requiring the issuer to issue securities, which were outstanding prior to that purchase of its own securities), without the prior approval of the Exchange."
>
> (Rule 10.06(3) was amended on 11 June 2024. See Note below.)

Analysis

Public float requirements

10. The public float requirement seeks to ensure an open market for trading in listed securities and require at least 25% of the securities be held by the public at all times. Where there are insufficient securities in the hands of the public, trading will be suspended if it is necessary to avoid a disorderly market.

11. Company A proposed a withdrawal of listing in the overseas stock exchange by making a share repurchase offer to all existing shareholders. In the extreme case where all public shareholders accepted the Offer (other than those undertaken to Company A not to do so), Company A's shares would be held by a small number of shareholders and there might not be an open market in the shares in Hong Kong upon completion of the Offer. It was not in the interest of Company A's shareholders if trading suspension continued for a prolonged period due to the lack of an open market in the shares.

12. The Exchange would allow Company A to proceed with the proposal taking into account the following:

    a. the purpose of the Offer was to facilitate the withdrawal of listing of Company A's shares from the overseas stock exchange. Company A intended to maintain a listing of its shares on the Exchange;

    b. Company A had a wide spread of shareholders, and a number of shareholders undertook not to accept the Offer. The concern about a lack of open market in its shares would arise only if there was a very high take up of the Offer; and

    c. Company A proposed to place new shares to independent placees to ensure an open market for trading its shares in Hong Kong upon completion of the Offer.

Possible Placing after the share repurchase offer

13. Rule 10.06(3) requires that an issuer seeks the Exchange's consent before issuing new shares or announcing a new issue of shares within 30 days after the purchase of its own shares. This is to ensure that the issuer does not affect the price of the new shares to be issued by the repurchase of its own shares.

14. In this case, the purpose of the Possible Placing was to ensure an adequate spread of shareholders in Hong Kong after the Offer. In Company A's announcement for the proposed Offer, there would be disclosure to inform the market of the Possible Placing after the Offer. The proposal did not raise concern on market manipulation.

Conclusion

15. The Exchange allowed Company A to proceed with the proposed Offer and gave consent for conducting the Possible Placing within 30 days after the Offer.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. Rule 10.06(3) was amended on 11 June 2024 to (i) apply the existing moratorium period requirement for an issue of new shares to a resale of treasury shares and (ii) extend the carve-out provision to include the grant of share awards or options under a share scheme that complies with Chapter 17, or a new issue of shares or a sale or transfer of treasury shares under a capitalisation issue, upon vesting or exercise of share awards or options under the share scheme that complies with Chapter 17 or pursuant to the exercise of outstanding warrants, share options or similar instruments. The Rule amendments would not change the analysis and conclusion in this case.

Whether a listed issuer was required to include convertible preference shares as part of its total issued shares in calculating the public float of its listed shares

Facts

1. The ordinary shares of a listed issuer (**Company A**) were listed on the Exchange. It proposed to issue convertible preference shares (**CPS**) to settle part of the consideration for its acquisition of assets from a connected person.

2. Under the terms of the CPS, they would be non-redeemable. Each CPS would be convertible into one ordinary share of Company A subject to adjustments. Holders of the CPS would be entitled to dividends, if any, that would be paid with respect to the ordinary shares on an "as converted" basis. They would have no voting rights at Company A's general meetings, except for a resolution to vary the rights of the holders of the CPS or to wind up Company A.

3. The CPS would not be listed. Company A would apply to the Exchange for a listing of the ordinary shares to be issued upon conversion of any CPS.

4. Holders of the CPS could not convert the CPS if it would result in the public float of the listed shares falling below the minimum level required in the Listing Rules.

5. The public float of Company A's listed shares exceeded 25% of its total issued share capital before the proposed transaction. However, it would fall below 25% if the CPS were to be included as part of the total issued share capital.

Relevant Listing Rules

6. Rule 8.08(1) states that:

   "There must be an open market in the securities for which listing is sought. This will normally mean that:

   (a) at least 25% of the issuer's total number of issued shares must at all times be held by the public.

   …"

   (Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

Analysis

7. Rule 8.08 seeks to ensure that a sufficient amount of listed shares are in public hands at all times in order to maintain an open market for trading in the securities.

8. The Rule states that its purpose is *normally* achieved when the public float of listed shares represents at least 25% of the issuer's total issued share capital.

9. In this case, Company A's total issued share capital would include two classes of shares, i.e. the listed shares and the CPS. Having considered the terms of the CPS, they were similar to debt securities. The Exchange was satisfied that the public float would not be affected as a result of the issue of the CPS. It allowed Company A to exclude the CPS when calculating the public float of its listed shares.

Conclusion

10. It was not necessary for Company A to include the CPS as part of its total issued share capital for the purpose of calculating the public float of its listed shares.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would allow a listed issuer to reduce its minimum public float to 24 per cent as a result of a proposed issue of new shares to a strategic investor

Parties

- **Company A** – a Main Board issuer
- **Investor** – Company A's strategic partner

Facts

1. Company A was owned as to 70% by its controlling shareholder and as to 30% by public shareholders. Since its listing a year ago, it had had the minimum public float of 25% under Rule 8.08(1)(a). There was a PRC regulatory requirement imposed at the time of listing that the controlling shareholder had to own at least a 51% interest in Company A.

2. The Investor was one of the world's leading manufacturers of the same products as those produced by Company A. Company A and the Investor proposed to form a long term strategic partnership (**Proposed Transaction**). The Investor would inject funds and introduce advanced technologies to Company A to develop new products and cooperate in sales and distribution of the products globally.

3. As a condition of the Proposed Transaction, the Investor required to acquire a 25% plus one share equity interest in Company A, through subscribing for new shares and/or acquiring existing shares from the controlling shareholder. This effectively gave the Investor veto rights over any special resolution which required support from shareholders holding at least a 75% interest under the applicable laws.

4. After the Proposed Transaction, the controlling shareholder and the Investor would hold a 51% and a 25% plus one share equity interest in Company A respectively, and the public float would be 24% minus one share.

5. Company A sought a waiver from the public float requirement under Rule 8.08(1)(a) because:

   a. Despite the 1% plus one share public float shortfall, the absolute number of shares in public hands would remain unchanged and there remained an open and highly liquid market in Company A's shares which were widely distributed among a large number of shareholders. Company A had approximately 480,000 shareholders immediately upon completion of its IPO. Its total market capitalisation was over $10 billion and the average daily trading volume of its shares since listing was approximately 7 million shares.

   b. The Proposed Transaction would be beneficial to Company A and its shareholders as a whole since it would bring to Company A new funds, experience and advanced technologies, and enhance its global competitiveness and earning capacity.

c. Given the PRC regulatory requirement and the Investor's requirement, a public float representing 24% minus one share would be the highest achievable level of public float. Compliance with Rule 8.08(1)(a) would be unduly burdensome and impractical to Company A.

d. At the time of listing, Company A, with a market capitalisation of over HK$29 billion, would have qualified for a waiver under Rule 8.08(1)(d) had it applied for it. No waiver was sought at that time because the Proposed Transaction had not been contemplated.

Relevant Listing Rules

6. Rule 8.08(1) states that:

There must be an open market in the securities for which listing is sought. This will normally mean that:

(a) at least 25% of the issuer's total number of issued shares must at all times be held by the public.

…

(d) The Exchange may, at its discretion, accept a lower percentage of between 15% and 25% in the case of issuers with an expected market capitalization at the time of listing of over HK$10,000,000,000, where it is satisfied that the number of securities concerned and the extent of their distribution would enable the market to operate properly with a lower percentage …. Additionally, a sufficient portion (to be agreed in advance with the Exchange) of any securities intended to be marketed contemporaneously within and outside Hong Kong must normally be offered in Hong Kong.

7. Rule 13.32 states that:

(1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …

Notes: (1) …

(2) The lower percentage of securities in public hands that the Exchange may at its discretion grant to eligible issuers under Rule 8.08(1)(d) may only be granted at the time of listing and will not be open for application post listing notwithstanding an issuer may after listing attain a market capitalisation of over HK$10,000,000,000.

Analysis

8. The public float requirement seeks to ensure an open market in the securities for which listing is sought. To provide an open, fair and orderly market for the trading in the securities, it is essential to have available a minimum number of shares for trading.

9. At the time of listing, the Exchange may accept a public float of between 15% and 25% if issuers have an expected market capitalisation of over HK$10 billion. Note 2 of Rule 13.32(2) clarifies that the Exchange may only allow the lower percentage under Rule 8.08(1)(d) to eligible issuers at the time of (and not after) listing. The Exchange will not accept an issuer's request to lower the minimum public float percentage threshold after listing simply because of its large market capitalisation.

10. In this case, Company A sought to reduce the minimum public float requirement because of the Proposed Transaction.

11. The Exchange noted the rationale for the Proposed Transaction submitted by Company A. When assessing Company A's waiver application, it considered the following factors:

    a. With the Investor's requirement to hold 25% plus one share in Company A, Company A and its controlling shareholder had shown their best endeavours to comply with the Rules by reducing the latter's interest to 51%, the minimum PRC regulatory requirement. The highest achievable public float for Company A would be 24% minus one share.

    b. The public float shortfall would be about 1%. The number of Company A's shares in the public hands would remain unchanged. The shortfall would unlikely affect the provision of an open, fair and orderly market for Company A's shares, having regard to (i) the large shareholder base and high liquidity of the shares; and (ii) the public market capitalisation which had been over HK$10 billion since listing.

    c. Had the Proposed Transaction been in place at the time of listing, Company A would have qualified for a public float waiver under Rule 8.08(1)(d).

Conclusion

12. The Exchange waived the public float requirement for Company A.

Whether the Exchange would grant listing approval for new shares to be issued by a listed issuer to an investor that could result in the listed issuer's public float falling below the minimum requirement

Parties

- **Company A** – a Main Board issuer
- **Investor** – a party independent of Company A

Facts

1. Company A had financial difficulties. It proposed:

   a. to issue new shares to the Investor (**Subscription Shares**) under a subscription agreement; and

   b. a rights issue, fully underwritten by the Investor.

2. These transactions were conditional on approval of Company A's shareholders and the Exchange giving listing approval for the new shares.

3. The Investor would be Company A's controlling shareholder upon completion of the subscription. If no shareholder took up the rights shares and the Investor fulfilled its underwriting obligation, the public float of Company A's shares would fall below the 25% requirement under Rules 8.08(1)(a) and 13.32(1).

4. Company A stated in its announcement regarding the proposal that it would undertake to the Exchange that it would use reasonable endeavours to meet the minimum public float requirement upon completion of the transaction. However, no arrangement was put in place to ensure compliance with the requirement.

Relevant Listing Rules

5. Rule 8.08(1)(a) states that:

   There must be an open market in the securities for which listing is sought. This will normally mean that:

   (a) at least 25% of the issuer's total number of issued shares must at all times be held by the public.

   …

   (Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

6. Rule 13.32 states that:

   (1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …

Analysis

7. The public float requirement seeks to ensure an open market in the securities for which listing is sought. The Exchange would not give listing approval for an issue of new shares which would cause or facilitate a breach of a requirement under the Rule. It is the Exchange's practice to require the issuer to put in place adequate arrangements to prevent a breach of the Rules, for example, by entering into an irrevocable arrangement to place a sufficient number of shares to meet the minimum public float requirement.

8. Here, the Investor's subscription and underwriting obligations could possibly result in the public float of Company A's shares being below the minimum public float requirement. The Exchange did not consider that Company A's undertaking to use reasonable endeavours to meet the requirement would adequately address its concern. Without any concrete arrangements to ensure a minimum 25% public float for Company A upon completion of the proposal, the Exchange was not prepared to give listing approval until the issue was addressed.

9. To address the Exchange's concern, the parties took the following measures:

   a. The Investor and Company A agreed to limit the Investor's underwriting obligation so that it would not cause Company A to breach the requirement.

   b. Professional underwriters would underwrite the rights shares not underwritten by the Investor to avoid the issue of insufficient public float.

Conclusion

10. The Exchange accepted that the measures in paragraph 9 above addressed the issue of possible insufficient public float upon completion of the proposal.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would grant listing approval for new shares to be issued by a listed issuer upon conversion of convertible notes that could result in the listed issuer's public float falling below the minimum requirement

Parties

- **Company A** – a Main Board issuer
- **Company B** – an investor who agreed to subscribe for new shares and convertible notes to be issued by Company A

Facts

1. Company A proposed to issue certain new shares (**Subscription Shares**) and convertibles notes to Company B under a subscription agreement. The convertible notes would be convertible into new shares of Company A (**Conversion Shares**) after the issue date according to the terms of the notes.

2. The proposed issue was conditional on approval of Company A's shareholders and the Exchange giving listing approval for the Subscription Shares and the Conversion Shares.

3. Upon completion of the subscription agreement, Company B would become a substantial shareholder of Company A, and the public float of Company A's shares would still meet the 25% requirement. However, based on the shareholding structure of Company A at that time, the public float would fall below 25% if Company B exercised its rights to convert some or all of the convertible notes.

4. Company A proposed to undertake to the Exchange that it would take appropriate measures to ensure the compliance with the public float requirement at all times. For example, it would consider placing new shares to independent third parties to maintain a 25% public float as a result of any conversion of the convertible notes, or redeeming some of the convertible notes.

5. Alternatively, Company A proposed to limit the maximum number of Conversion Shares that it might issue to Company B to be 25% of Company A's issued share capital at the time of completion of the subscription agreement.

Relevant Listing Rules

6. Rule 8.08(1)(a) provides that

   "at least 25% of the issuer's total number of issued shares must at all times be held by the public."

   (Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

7. Rule 13.32(1) states that

   "Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands…"

Analysis

8. The public float requirement seeks to ensure an open market in the securities for which listing is sought. The Exchange would not give listing approval for an issue of new shares which would cause or facilitate a breach of the requirement.

9. In this case, the issue of the convertible notes to Company B could possibly result in the public float of Company A's shares falling below the minimum 25% requirement. The Exchange did not consider that Company A's undertaking to use reasonable endeavours to meet the requirement would adequately address its concern. Without any concrete arrangements to ensure a minimum 25% public float for Company A upon conversion of the convertible notes, the Exchange was not prepared to give listing approval until the issue was addressed.

10. The Exchange also did not consider the alternative proposal acceptable as it only took into account the shareholding structure of Company A at the time of the completion of the subscription agreement and not the conversion of the notes. It would be possible for Company A to issue Conversion Shares resulting in a breach of minimum public float requirement, as a result of changes to Company A's share capital (e.g. share repurchase) after the completion of the subscription agreement.

11. To address the Exchange's concern, Company A and Company B agreed to revise the terms of the convertible notes so that a conversion of the notes could not take place if it would result in Company A failing to meet the minimum public float requirement under the Rules.

Conclusion

12. The Exchange accepted that the action taken by Company A in paragraph 11 above addressed the issue of possible insufficient public float upon completion of the subscription agreement.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would allow a listed issuer to reduce its minimum public float to 15 per cent based on its market capitalisation after listing

Facts

1. An issuer (**Company A**) was listed on the Main Board. Under Rules 8.08(1) and 13.32(1), at least 25% of its total issued share capital must at all times be held by the public (see Note below).

2. After listing, Company A requested the Exchange to exercise its discretion under Rule 8.08(1)(d) to allow it to maintain a minimum public float of 15%. At the time of application, Company A's market capitalisation was approximately HK$12 billion.

3. Company A submitted that:

   - Given the number of securities concerned and their widespread distribution, the market for Company A's shares would still be able to operate properly after relaxation of the minimum public float from 25% to 15%.

   - It expected that its public float percentage would likely be reduced to 15% because: (i) it proposed to repurchase its own shares; and (ii) its existing shareholders, including institutional investors, might increase their shareholdings where circumstances permitted.

   - As at the time of listing, Company A had a market capitalisation of approximately HK$20 billion. While Note (2) to Rule 13.32(2) provided that the relaxation of the public float requirement under Rule 8.08(1)(d) would not be open for application after listing, Company A was of the view that the Note was only intended to apply to an issuer who was unable to meet the market capitalisation threshold of HK$10 billion at the time of listing, but not an issuer, Company A, who had met that threshold at the time of listing.

Relevant Listing Rules

4. Rule 8.08(1)(d) provides that:

   The Exchange may, at its discretion, accept a lower percentage of between 15% and 25% in the case of issuers with an expected market capitalisation at the time of listing of over HK$10,000,000,000, where it is satisfied that the number of securities concerned and the extent of their distribution would enable the market to operate properly with a lower percentage, …

5. Note (2) of Rule 13.32(2) provides that:

> The lower percentage of securities in public hands that the Exchange may at its discretion grant to eligible issuers under rule 8.08(1)(d) may only be granted at the time of listing and will not be open for application post listing notwithstanding an issuer may after listing attain a market capitalisation over HK$10,000,000,000.

Analysis

6. Rule 8.08(1)(d) describes the conditions upon which the Exchange may exercise discretion to accept a lower percentage of public float of between 15% to 25% at the time of listing. Note (2) to Rule 13.32(2) further reinforces the timing at which the Exchange may exercise such discretion by providing that *"… the lower percentage of securities in public hands that the Exchange may at its discretion grant to eligible issuers under Rule 8.08(1)(d) may only be granted at the time of listing and will not be open for application post listing notwithstanding an issuer may after listing attain a market capitalization of over HK$10,000,000,000."*

7. It is clear that the prescribed minimum public float, once determined at the time of listing, is not subject to further relaxation after listing merely on the basis of market capitalisation. This position recognises the fact that the fluctuations of the share price, and hence market capitalisation, of listed issuers after listing would make it difficult to monitor compliance and create market uncertainty if the minimum public float is allowed to be reviewed and adjusted merely because of such fluctuations.

8. The Exchange did not agree that Note (2) to Rule 13.32(2) was only intended to apply to an issuer who was unable to meet the market capitalisation threshold of HK$10 billion at the time of listing, but not to an issuer who had met that threshold at the time of listing. The Exchange's administrative practice in considering a public float waiver request at the time of listing is to allow the minimum public float to be the higher of the prescribed minimum according to the Listing Rules and that held by the public immediately after completion of the offering and upon exercise of the over-allotment option. Accordingly, had Company A who was able to meet the minimum 25% public float requirement, applied for a waiver at the time of listing, no waiver would have been granted.

Conclusion

9. The Exchange declined Company A's request for the Exchange to exercise its discretion under Rule 8.08(1)(d) to allow Company A to maintain a minimum public float of 15%.

Note: Rule 8.08(1) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would regard shares in a listed issuer held by a trust as being "in public hands" if the trustee was a connected person of the listed issuer

Parties

- **Company A** – a listed company
- **Mr X** – a director of Company A

Facts

1. Mr X was a director and therefore a connected person of Company A. He was also the trustee of a charitable trust which held certain shares in the issued share capital of Company A.

2. An issue arose as to whether the shares held by the trust could be regarded as being "in public hands" for the purpose of Rule 8.24 of the Listing Rules.

Analysis

3. Rule 8.24 provides that, among other things, the Exchange will not regard shares held by a connected person as being “in public hands”.

4. Despite the charitable nature of the trust in question, Mr X, as trustee, exercised control over its assets of which the shares formed part. Such control extended to the voting rights attaching to such shares. In view of his control over the voting rights, the shares should be considered as being held by him for the purpose of determining whether they could be regarded as being "in public hands".

Conclusion

5. The shares in question could not be regarded as being "in public hands" for the purpose of Rule 8.24.

Whether a fund manager was a core connected person or connected person of the listed issuer when the manager held shares in a listed issuer on behalf of its clients

Parties

- **Company A** – a Main Board issuer

- **Manager** – an international asset management group and a shareholder of Company A

Facts

1. The Manager managed funds and assets for institutional and private clients around the world. It held about 12 per cent of Company A's shares (the **Shares**) for two categories of clients:

    - 8 per cent were held under certain funds managed by the Manager (collectively, the **Pooled Funds**). These funds had defined investment objectives and mandates to invest in a wide range of companies. Investors of the funds were required to effectively delegate, without recourse, the investment decisions and voting powers of the Shares to the Manager.

    - 4 per cent were held on behalf of a number of clients under segregated investment accounts and closed-end funds (collectively, the **Segregated Funds**). These clients retained the power to instruct the Manager on how to handle their investments, including investment decisions and voting powers of the underlying securities.

      The mandate given by each client to the Manager contained a proxy arrangement under which the Manager was authorised to vote on behalf of the client according to the client's instruction, and in the absence of a specific voting instruction, the Manager might exercise the voting rights in accordance with its proxy voting policy endorsed by the client. The policy sought to assure that proxies were voted in the best interest of each client.

2. The Manager had no other connection with Company A. It did not have any board seats in Company A or special rights to influence its management.

3. Company A submitted the 4 per cent Shares held under the Segregated Funds should be excluded when assessing whether the Manager was a substantial shareholder of Company A because the voting rights of these Shares rested with the clients. It sought the Exchange's confirmation that the Manager was not Company A's core connected person or connected person.

Relevant Listing Rules

4. Rule 1.01 defines a "substantial shareholder" in relation to a company as:

   a person who is entitled to exercise, or control the exercise of, 10 per cent or more of the voting power at any general meeting of the company.

5. Rule 1.01 states that a "core connected person" in relation to a company includes:

   … a director, chief executive or substantial shareholder of the company …

6. Rule 14A.07 states that a "connected person" includes:

   (1) a director, chief executive or substantial shareholder of the listed issuer…
   …

7. Rule 8.24 states that:

   The Exchange will not regard any core connected person of the issuer as a member of the "public" or shares held by a core connected person as being "in public hands". …

Analysis

8. Under the Rules, a core connected person or connected person includes an issuer's substantial shareholder for the purpose of the public float and connected transaction requirements. These requirements seek to (i) ensure a sufficient amount of listed securities in public hands to maintain an open market for trading; and (ii) safeguard against connected persons taking advantage of their positions to the detriment of the issuer's minority shareholders.

9. In this case, the Exchange noted that:

   - The Manager had control over 8 per cent of the Shares which were held under the Pooled Funds.
   - The 4 per cent of the Shares held under the Segregated Funds could be distinguished from other Shares held by the Manager:
     - The clients of the Segregated Funds were the beneficial owners of the underlying Shares. They had control over the investment portfolios including the purchase and sale of these Shares.
     - The exercise of the voting rights attached to the Shares held under the Segregated Funds was always subject to the clients' specific instructions. Although the Manager could exercise the voting rights in the absence of any specific instructions, it must vote in the best interest of the clients, and not itself, under the proxy voting policy endorsed by the clients.

10. As the Manager did not have control over 10 per cent or more of the shares, it was not a substantial shareholder of Company A.

Conclusion

11. The Manager was not Company A's core connected person or connected person.

Public float

1. In the case of a PRC issuer whose domestic shares are quoted on NEEQ, will the domestic shares held by public shareholders be counted towards the PRC issuer's public float under the Listing Rules?

No. Only listed H-shares held by members of the public are counted towards the PRC issuer's public float under the Listing Rules. For the avoidance of doubt, when calculating the percentage of public float, the total number of issued shares (excluding treasury shares) of the PRC issuer (i.e. denominator) refers to all shares in issue including H shares and domestic shares but excluding treasury shares.

MB Rules 8.08, 13.32 and 19A.13A
GEM Rules 11.23(7) and 25.07A
First released: September 2019; last updated: June 2024

8

Transfer of listing from GEM to Main Board

Transfer of listing from GEM to Main Board

Qualifications for transfer

1. When can a GEM issuer submit a transfer application under MB Chapters 9A and 9B?

A GEM issuer applying for transfer under:

(i) MB Chapter 9A must have published its annual report for the first full financial year after its initial listing; and

(ii) MB Chapter 9B must have published its annual reports for the three full financial years following its initial listing.

For example, below is the earliest timeline for a GEM issuer with a December year end to submit a transfer application:

Applicable MB Chapter	Year end	Initial GEM listing	Earliest time to submit a transfer application
MB Chapter 9A	December	November 2022	After 2023 annual report has been published and distributed to its shareholders.
MB Chapter 9B	December	November 2022	After 2025 annual report has been published and distributed to its shareholders.

MB Rules 9A.02(2) and 9B.03(1)
First released: May 2008; last updated: May 2024

2. How would the Exchange assess whether a GEM issuer meets the minimum market capitalisation requirement under MB Chapter 8 (Market Cap Requirement)?

Under MB Rule 9A.02(1), a GEM issuer must meet all qualifications for listing on the Main Board, including the Market Cap Requirement. For this purpose, the market capitalisation should be calculated using the share price on the date of listing on the Main Board. In practice, the Exchange will calculate the market capitalisation using the closing share price on the trading day immediately before the first day of the proposed transfer.

The Exchange will also examine the GEM issuer's share price movement and assess whether the Market Cap Requirement was met during the trading record period. If the GEM issuer failed to meet the Market Cap Requirement for a prolonged period of time during the trading record period and had unusual share price movement (especially for any increase close to the day of transfer), the Exchange may:

(i) Not approve the transfer application until a reasonable and satisfactory explanation is provided by the GEM issuer and its sponsor; and

(ii) Require the GEM issuer to make prominent disclosure in its transfer announcement or listing document on the volatile share price and/or trading volume.

MB Rules 9A.02(1) and 9B.03(2)
GEM Rule 9.24
First released: May 2008; last updated: May 2024

3. How should a GEM issuer calculate the volume weighted average market capitalisation requirement under MB Rule 9B.03(2)?

(i) List the daily market capitalisation (determined by the number of total issued shares (excluding treasury shares) and the intraday volume weighted average price) and daily number of shares traded over the 250 trading days immediately preceding the relevant transfer application and until the commencement of dealings in the GEM issuer's securities on the Main Board (the **Reference Period**). *(Columns A, B and C of the table below)*

(ii) If there was any corporate action during the period, calculate the adjusted number of shares traded (e.g. two-for-one share sub-division results in an adjustment factor of 2, one-for-five share consolidation results in an adjustment factor of 0.2). *(Column D)*

(iii) Calculate the total adjusted number of shares traded over the Reference Period and derive the weight for each trading day. *(Columns D and E)*

(iv) Calculate the volume weighted average market capitalisation (i.e. the weighted sum of the market capitalisation on each trading day). For example, in the table, the weighted sum would be HK$500 million x 0.40% + HK$550 million x 0.48% + … + HK$650 x 0.32% + … (*Column F*)

Reference Period	Market Capitalisation (HK$ million)	Number of Shares Traded	Adjusted Number of Shares Traded	Weight	Volume weighted average market capitalisation (HK$ million)
(A)	*(B)*	*(C)*	*(D) = (C)*adjusted factor*	*(E) = (D)/Sum of (D)*	*(F) = (B) x (E)*
1	500	1,000	2,000	0.40%	2.0
2	550	1,200	2,400	0.48%	2.6
…	…	…	…	…	…
99	600	1,500	3,000	0.60%	3.6
100 (effective date of share sub-division)	**650**	**1,600**	**1,600**	**0.32%**	**2.1**
101	700	1,700	1,700	0.34%	2.4
…	…	…	…	…	…
250	750	1,800	1,800	0.36%	2.7
		TOTAL	**500,000**	**100%**	**≥ 500**

Table - illustrative example of a two-for-one share sub-division effective from 100th day

MB Rules 8.05(2)(d), 8.05(3)(d), 8.09(2), 9A.02(1) and 9B.03(2)
GEM Rule 9.24
First released: May 2008; last updated: June 2024

4. How can a GEM issuer confirm (for the purpose of meeting the requirement of MB Rule 9A.02(3)) if there is an open Exchange investigation into its compliance, before it submits a transfer application?

The Exchange will, upon the request of a GEM issuer, provide the GEM issuer with a written confirmation on whether it fulfills the requirement under MB Rule 9A.02(3) as at the date of such confirmation.

If additional information that alters such confirmation comes to light within two months of the letter, the Exchange will notify the GEM issuer in writing.

MB Rule 9A.02(3)
First released: May 2008; last updated: May 2024

5. What factors would the Exchange take into consideration in assessing whether a breach of the Listing Rules by a GEM issuer is "serious" for the purpose of assessing its eligibility for a transfer to the Main Board?

The Exchange normally considers the following factors:

(i) The nature, extent, duration and frequency of the breach (e.g. whether it involves any prejudice or risk of prejudice to investors such as failure to obtain prior shareholder approval for connected transactions, or failure to make disclosure under GEM Rule 17.10); and

(ii) Whether there is evidence that the breach involves fraud, deceit or dishonesty, is intentional or due to recklessness, or reveals material or systemic weaknesses in the issuer's internal control procedures.

MB Rule 9A.02(3)
GEM Rule 17.10
First released: May 2008; last updated: May 2024

6. Can a GEM issuer fulfil the compliance record requirement of MB Rule 9A.02(3) if it was held to have committed a serious breach of the Listing Rules that was subsequently overturned by the GEM Listing Review Committee / Listing Review Committee?

Yes.

In addition, a GEM issuer may apply for a transfer under MB Chapters 9A and 9B in each of the following scenarios: (i) if investigations by the Exchange are not leading or have not led to any disciplinary proceedings; or (ii) upon conclusion of the disciplinary proceedings where there is no finding of any serious breach of the Listing Rules.

MB Rule 9A.02(3)
First released: January 2024; last updated: May 2024

Transfer process

7. Will the Exchange allow existing shares to be traded on GEM, while new shares (issued on or before the transfer of listing) being traded on the Main Board (i.e. parallel trading)?

No. Parallel trading of securities of the same issuer on both boards is not allowed. There should be a clear-cut date for cessation of trading on GEM and commencement of trading on the Main Board.

MB Rules 9A.11 and 9B.02
First released: May 2008; last updated: May 2024

8. Will trading in the shares of a GEM issuer be halted or suspended at any time during the transfer process?

GEM issuers are required to observe the trading halt or suspension policy and the general disclosure obligations under the GEM Rules as long as they are still listed on GEM. A GEM issuer must assess whether the information relating to the transfer process would require disclosure under GEM Rule 17.10, having considered its particular circumstances. A trading halt or suspension would be necessary in any of the circumstances described in GEM Rules 17.11A(1) to (3) where an announcement cannot be made promptly.

MB Rules 9B.08 and 11.04
GEM Rules 9.26, 17.10, 17.11A(1) to (3)
First released: May 2008; last updated: May 2024

After transfer to the Main Board

9. Where a GEM issuer has successfully transferred its listing to the Main Board, will it still be held accountable for breaches of the Listing Rules committed when it was listed on GEM?

Yes.

GEM Rule 3.10
First released: May 2008; last updated: May 2024

9

Repurchase of securities and treasury shares

9.1 Repurchase of securities

Guidance letter – Guidance on automatic share buy-back programs conducted on behalf of listed issuers	GL117-23	9.1 – 1
Listing decision – Whether the Exchange would give consent to a listed issuer under Rule 10.06(3)(a) for share buyback to be conducted concurrently with its convertible bond offering	LD139-2025	9.1 – 6
Listing decision – (i) Whether a listed issuer could proceed with a share repurchase offer which might result in a lack of open market in its shares; and (ii) whether the Exchange would give consent to the listed issuer for issuing new shares within 30 days after completion of such offer to meet the public float requirement	LD82-2014	9.1 – 9
Listing decision – Whether the Exchange would approve a listed issuer's proposed issue of new shares after its redemption of convertible bonds	LD99-1	9.1 – 13

9.2 Treasury shares

Guidance letter – Guidance on arrangements for listed issuers to hold or deposit treasury shares in CCASS (Effective from 11 June 2024)	GL119-24	9.2 – 1
Frequently asked questions – Treasury shares	FAQ9.2 – No.1-9	9.2 – 5

HKEX Guidance Letter
HKEX-GL117-23

October 2023 (Updated in June 2024)

Guidance on automatic share buy-back programs conducted on behalf of listed issuers

I. Background and purpose

1. A listed issuer may, from time to time, buy back its own shares on the Exchange. This could be conducted to enhance its earnings per share, to return capital to its shareholders, to adjust its debt-to-equity ratio, or to signal to the market that its shares are undervalued and that the management have confidence in the prospects of the listed issuer.

Regulatory framework for repurchase of shares

2. On-market share repurchases may create conditions for market manipulation and insider trading as an issuer may influence its share price through share repurchases and insiders may trade in the shares to benefit from non-public information about share repurchases.

3. In Hong Kong, Parts XIII and XIV of the Securities and Futures Ordinance (**SFO**) contain provisions against price manipulations and prohibit insiders from unfairly using inside information to deal in securities. Additionally, the Listing Rules impose certain dealing restrictions[1] for share repurchases on the Exchange to guard against price manipulations and to prohibit a listed issuer from unfairly using inside information to deal in its shares. These include prohibiting an issuer from share repurchases on the Exchange while in possession of undisclosed inside information and during the 30 days prior to the release of financial results (the **Restricted Period**)[2].

4. Other markets including the UK and the US also have provisions to prohibit price manipulations and trading on the basis of material non-public information and/or during closed periods[3]. At the same time, these markets also provide exemptions or safe harbours for trading programs conducted during the restricted period, provided that there is sufficient safeguard to ensure that share repurchases are carried out independently and the issuer has no influence over the share repurchases.

1 Main Board Rule 10.06(2) (GEM Rule 13.11)
2 Main Board Rule 10.06(2)(e) (GEM Rule 13.11(4))
3 The US does not impose a closed period. The UK imposes a closed period of 30 days.

Waivers granted for dually listed issuers

5. We have granted waivers allowing issuers to conduct automatic share buy-back programs on the Exchange and to continue these programs throughout the Restricted Period, provided that the terms of the programs were determined outside the Restricted Period (the **Waivers**). These issuers are dually listed on the Exchange and the London Stock Exchange (**LSE**) or the New York Stock Exchange (**NYSE**), and the programs are similar to the share buy-back programs adopted by these issuers for their share buy-backs on LSE or NYSE under the exemption from the Market Abuse Regulation of the UK (**MAR**)[4] or the "safe harbour" under the Securities Exchange Act of the US (**SEA**)[5].

6. Generally, these programs are established before an issuer is in possession of material non-public information and are lead-managed by a single broker which makes its trading decisions independently of the issuer, subject to pre-determined parameters. The share repurchases must also comply with the limits on purchase price and daily trading volume, and restrictions on trading during the opening/closing sessions. The issuers are also required to disclose details of their share repurchases under the programs.

Purpose of this guidance letter

7. The Exchange will consider granting a Waiver for automatic share buy-back programs of individual issuers (regardless of whether they are solely or dually listed on the Exchange) provided that the automatic share buy-back programs are structured in a manner to mitigate the risks of abuse of undisclosed inside information and price manipulation. The issuer must also demonstrate that strict compliance with the Restricted Period is unduly burdensome.

8. This letter provides guidance to listed issuers on conducting automatic share buy-back programs on the Exchange, and the framework for the Exchange's assessment of the issuer's share buy-back program in considering a Waiver application.

II. Relevant Listing Rules

9. Main Board Rule 10.06 (GEM Rule 13.11(4)) states that:

"…

(2) Dealing Restrictions

…

(e) an issuer shall not purchase its shares on the Exchange at any time after inside information has come to its knowledge until the information is made publicly available. In particular, during the period of 30 days immediately preceding the earlier of:

(i) the date of the board meeting (as such date is first notified to the Exchange in accordance with the Listing Rules) for the approval of the issuer's results for any year, half-year, quarterly or any other interim period (whether or not required under the Listing Rules); and

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4 In the UK, Article 5 of the MAR exempts issuers' buy-back programs from Articles 14 (dealing with inside information) and 15 (market manipulation).

5 In the US, s240.10b5-1 and s240.10b-18 of the SEA provide a "safe harbour" from liabilities for trading on the basis of material non-public information and manipulation for an issuer's repurchase of shares on the market.

(ii) the deadline for the issuer to announce its results for any year or half-year under the Listing Rules, or quarterly or any other interim period (whether or not required under the Listing Rules),

and ending on the date of the results announcement, the issuer may not purchase its shares on the Exchange, unless the circumstances are exceptional;

…"

III. Guidance

10. The Exchange will consider granting a Waiver to allow an automatic share buy-back program to continue throughout the Restricted Period if the risk of abuse of undisclosed inside information and price manipulation is low. The Exchange will apply the following criteria (which is not meant to be exhaustive) in assessing the share buy-back program of an issuer and its application for Waiver.

(A) Safeguards against trading with undisclosed inside information

Irrevocable non-discretionary arrangement with a single independent broker

11. An automatic program should be established outside the Restricted Period and cannot be modified or terminated (unless required by applicable laws) during the Restricted Period. There should also be restrictions on the appointed broker to safeguard against dealing with inside information:

(i) **Irrevocable non-discretionary arrangement** – The listed issuer should enter into a binding contract with a broker with parameters for share buy-backs (i.e. fixed trading parameters including price, volume and dates, or formula or algorithm for determining the price, volume and dates) set prior to the commencement of the automatic program. The contract should be entered into outside the Restricted Period, and modification or termination (unless required by applicable laws) of the program would not be permitted during the Restricted Period.

(ii) **Independent broker** – The listed issuer should appoint a broker independent of the listed issuer and its connected persons. The issuer and its broker must have in place appropriate systems and controls with Chinese Walls to ensure that (i) there is no influence by the issuer or any of its connected persons over the automatic program after its commencement date and that all investment decisions under the automatic program are made independently from the listed issuer and its connected persons; and (ii) no non-public information of the issuer and its connected persons is given directly or indirectly to, or received by any personnel of the broker involved with the establishment or execution of the automatic program until a reasonable time after its completion or termination. The broker must also conduct the buy-backs in accordance with the pre-determined trading parameters set out in the binding contract and in compliance with the applicable rules or laws.

(iii) **Single broker** – Share buy-backs should be effected through only one broker. This is to avoid the perception of widespread interest in the listed issuer's shares should many brokers are appointed to repurchase the shares.

Terms of the buy-back program

12. The terms of the buy-back program should not be structured to circumvent the dealing restrictions under the Rules and to avoid the perception of abuse of inside information by the listed issuer. For example, if a listed issuer enters into a program shortly before the blackout period and terminate the program shortly after the release of results, it may raise a concern on whether the program was established to circumvent the blackout period under the Listing Rules.

    (i) **Duration of program –** While the Exchange does not propose to set a fixed minimum period for a share buy-back program, the program should be of sufficient duration. A listed issuer should justify the reasonableness of the duration of the program, for example, by reference to the proposed size of the program and parameters agreed with the broker, including the expected price and timing of buy-backs. A program of short duration may raise a concern that the program is established to avoid the blackout period.

    (ii) **Cooling-off period –** As best practice, there should be a time gap between the commencement of the share buy-back under the program and the Restricted Period. Commencing a program shortly before the Restricted Period may give rise to a perception that a listed issuer may benefit from any material non-public information of which it may have been aware at the time of adopting the program. Further, management may be in possession of confidential information which even if not material (i.e. not an inside information), may nevertheless be relevant to the market assessment of the price of its securities.

    The terms of a specific program may determine whether both a cooling-off period and a long duration is required. For example, where a program is to be entered into shortly after release of the results, it may not be necessary to impose a cooling-off period.

(B) Safeguards against potential price manipulations

13. The Exchange will take into account the specific circumstances of an issuer (such as its market capitalisation and sufficient liquidity) in assessing the risk of price manipulations.

Issuer's size and liquidity of its shares

14. Share repurchases may reduce the liquidity of an issuer's shares and raise the risk that the share buy-back program may materially affect the market price of its shares. This is especially the case for listed securities which are thinly traded on the Exchange. Also, a large scale share repurchases may have a disproportionate impact on the share price.

15. Therefore, the Exchange considers that a Waiver may be granted to issuers with a large market capitalisation and sufficient liquidity, as their securities would be less susceptible to price manipulation through a buy-back program. As a reference, the Exchange would consider (i) market capitalisation of at least HK$10 billion[6]; and (ii) an average daily turnover volume (ADTV) of at least HK$10 million[7] in the six months immediately prior to the adoption of the buy-back program, as a benchmark for eligibility for the Waiver.

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6 With reference to new listing applicants eligible for a reduced public float under Main Board Rule 8.08(1)(d).

7 With reference to one of the criteria for designated securities eligible for short selling in Hong Kong under Regulation (18)(f) in the Eleventh Schedule to the Rules and Regulations of the Exchange and the Options Trading Rules, which requires the designated security to have a market capitalisation of at least HK$3 billion and an aggregate turnover during the preceding 12 months to market capitalisation ratio of not less than 60% (i.e. ADTV of about HK$7 million).

Dealing restrictions

16. The Exchange considers that a share buy-back program allowing dealing within a Restricted Period should be subject to additional dealing restrictions to limit the impact on share prices, so as to mitigate the risks of price manipulation.

    (i) **Trading volume limit** – Trading under a share buy-back program should be limited to 25% of the average daily trading volume over the immediately preceding 20 trading days as a condition for the Waiver so as to limit the impact of the share repurchases on the liquidity of the shares and hence the share prices.

    (ii) **Intra-day limit** – Participation in opening and/or closing auctions/ periods should be restricted as market activities at such times are considered to be a significant indicator of the direction of trading, the strength of demand and the current market value of the securities. This condition for the Waiver aims to prevent an issuer from creating or sustaining a high bid or transaction price at or near the close of trading.

17. Apart from the above dealing restrictions, trading under a share buy-back program is subject to the price restriction imposed under the Listing Rules for all share repurchases[8].

(C) General conditions

18. The Exchange obtained the SFC's consent for granting Waivers for automatic share buy-back programs of issuers by applying the framework criteria as set out in this letter.

19. Listed issuers may refer to the Guide on Applications for Waivers and Modifications of the Listing Rules for guidance on the criteria in assessing the Waiver applications, including whether compliance with the Rules would be unduly burdensome, and whether it would result in undue risks to shareholders.

20. Issuers should disclose details of their automatic share buy-back programs by way of announcements and any share repurchases conducted thereunder by way of next day disclosure returns[9]. These disclosures not only ensure transparency of share repurchases conducted under the programs, they also facilitate oversight of the issuers to prevent non-compliance.

21. In addition, issuers must ensure their compliance with the SFO, in particular the provisions relating to market manipulation and insider dealing, in relation to their adoption of automatic share buy-back program and the share repurchases conducted thereunder.

8 Main Board Rule 10.06(2)(a) (GEM Rule 13.11(6)) prohibits share repurchases on the Exchange at a purchase price higher by 5% or more than the average closing price for the 5 preceding trading days on which the shares were traded on the Exchange.

9 Main Board Rule 13.25A (GEM Rule 17.27A)

Whether the Exchange would give consent to a listed issuer under Rule 10.06(3)(a) for share buyback to be conducted concurrently with its convertible bond offering

Facts

1. Company A sought the Exchange's consent under MB Rule 10.06(3)(a) for share buyback to be conducted concurrently with its proposed offering of convertible bonds (**CBs**).

CB offering

2. Company A was a Main Board issuer with a market capitalisation of over HK$100 billion and an average daily turnover volume of over HK$400 million in the preceding six months. It proposed to conduct an offering of CBs in an aggregate principal amount of around US$300 million to professional investors through placing banks. The initial conversion price of the CBs was expected to be set at a substantial premium over the benchmarked price[1] of the shares of Company A in compliance with MB Rule 13.36(6). Upon conversion of the CBs, Company A would deliver shares to the bondholders. The CBs were expected to be issued under the general mandate granted to its directors at the last annual general meeting.

Concurrent share buyback in connection with the CB offering

3. Company A submitted that the subscribers of the CBs would comprise hedge funds and arbitrage investors whose investment strategies involved purchasing the CBs and concurrently short selling a portion of the underlying shares (**delta shares**) to establish an initial hedge against their exposure under the CBs. To facilitate a coordinated short sale by these CB investors, the placing banks would aggregate the delta shares and sell them off-market (**delta placement**) on behalf of the CB investors.

4. It was proposed that, concurrently with the CB offering, the delta shares would be offered to Company A and other investors. The allocation and price of the delta shares would be determined through a bookbuilding among the placing banks and the other investors, which Company A would not be involved. The delta placement price would be determined with reference to the last closing price of the shares of Company A immediately prior to the CB offering, and was expected to be at a small discount to such closing price. Company A would purchase the delta shares at the same delta placement price with part of the CB offering proceeds, and would cancel the purchased delta shares afterwards.

5. The purchase of delta shares by Company A would constitute an off-market share buybacks of Company A (**concurrent share buyback**). Company A considered the concurrent share buyback was part and parcel of the CB offering, which would help facilitate the creation of initial hedge of the CB investors and hence their subscription. It would also mitigate the negative pressure on the share price from their short-selling activities and the potential dilution of the CB offering from the conversion.

[1] As defined in MB Rule 13.36(5).

Announcement of the proposed transactions

6. The CB offering would be launched after market close in Hong Kong and the pricing terms would be determined overnight outside trading hours. Company A would publish an announcement before market open on the next trading day to disclose the terms of the CB offering and the concurrent share buyback.

Relevant Listing Rules

7. MB Rule 10.06(3)(a) provides that an issuer whose primary listing is on the Exchange may not (i) make a new issue of shares, or a sale or transfer of any treasury shares; or (ii) announce a proposed new issue of shares, or a sale or transfer of any treasury shares, for a period of 30 days after any purchase by it of shares, whether on the Exchange or otherwise, without the prior approval of the Exchange. The moratorium does not apply to a new issue of shares or a sale or transfer of any treasury shares under a capitalisation issue or a share scheme, pursuant to the exercise of warrants, share options or similar instruments, which were outstanding prior to the share buyback.

8. MB Rule 10.06(6)(c) provides that for the purpose of MB Rules 10.05, 10.06 and 19.16, "shares" shall mean shares of all classes and securities which carry a right to subscribe or purchase shares.

Analysis

9. MB Rule 10.06(3)(a) restricts an issuer from issuing new shares or convertible securities, or transfer of treasury shares, within 30 days after any share buyback. This is to ensure the issue or transfer of shares does not take place at a price that has been affected by the issuer's previous share buyback.

10. In this case, the proposed CB offering with concurrent share buyback would fall within the scope of MB Rule 10.06(3)(a) because the issuance of the CBs and the share buyback would take place concurrently.

11. Company A sought the Exchange's consent under MB Rule 10.06(3)(a)[2] to conduct the concurrent share buyback at the same time of the CB offering. When assessing Company A's application, the Exchange took into account the following factors:

    (i) The concurrent share buyback was part and parcel of the CB offering to facilitate the CB investors to establish an initial hedge required for their subscription of the CBs, and to mitigate the negative share price impact of such hedging activities and the potential dilution impact of the CB offering. As such, the concurrent share buyback would be beneficial to Company A and its shareholders as a whole.

    (ii) The concurrent share buyback would not artificially inflate the conversion price of the CBs. The CB offering would be launched after market close in Hong Kong, and the conversion price of the CBs and the delta placement price (and hence the repurchase price) would be determined at around the same time with reference to the last closing price of the shares. The delta placement price would be determined through a bookbuilding among the placing banks and the other investors, which Company A would not be involved.

[2] Company A also applied to the SFC for, and was granted, a waiver of, *inter alia*, a similar requirement in the Code on Share Buy-backs (Rule 7) based on the specific circumstances of its case.

Company A would announce the terms of the CBs and the concurrent share buyback before market open on the next trading day. In light of the above, the concurrent share buyback would not pose a material risk of price inflation. Further, Company A confirmed that: (a) save for the proposed concurrent share buyback, it had not conducted any share buybacks within 30 days before the announcement of the CB offering; and (b) it would not make a new issue of shares or a sale or transfer of any treasury shares, or announce a proposed new issue of shares or a sale or transfer of any treasury shares, for a period of 30 days after the concurrent share buyback, whether on the Exchange or otherwise, without the prior consent of the Exchange.

(iii) The shares of Company A were less susceptible to price manipulation given its large market capitalisation and high liquidity.

Conclusion

12. The Exchange gave consent to Company A under MB Rule 10.06(3)(a) to conduct the CB offering with the concurrent share buyback.

Whether (i) a listed issuer could proceed with a share repurchase offer which might result in a lack of open market in its shares; and (ii) the Exchange would give consent to the listed issuer for issuing new shares within 30 days after completion of such offer to meet the public float requirement

Facts

1. A Main Board issuer (**Company A**) was dually listed on the Exchange and an overseas stock exchange. It proposed to withdraw its listing in the overseas stock exchange by making a share repurchase offer to all existing public shareholders in Hong Kong and the overseas market (**Offer**).

2. It intended to maintain a listing on the Exchange. For any shareholders in the overseas market who did not accept the Offer, their shares would be transferred to the Hong Kong branch register.

3. It would also issue new shares to certain independent institutional investors (**Investors**) for cash to finance part of the funding requirement for the Offer.

4. To ensure a minimum of 25% public float immediately after the Offer, Company A had obtained undertaking from the Investors and certain public shareholders not to accept the Offer.

5. However, if there was a very high take up of the Offer, Company A's shares would be held by a small number of shareholders and there might not be an open market for trading in the shares in Hong Kong upon completion of the Offer. To address the concern, Company A submitted that:

   a. it had a wide spread of shareholders with over 2,000 shareholders in the overseas market and over 60 shareholders in Hong Kong including nominee companies. More than 60% of the overseas shareholders were institutional investors;

   b. the subscription of new shares in Company A by the Investors and the business cooperation with them would enhance the value of Company A. Company A did not expect a high uptake of the Offer; and

   c. in the event that there was a concern about the lack of an open market in Company A's shares after the offer, it would place new shares to independent placees (**Possible Placing**) to ensure compliance with the public float requirement.

6. Company A asked whether the Exchange would allow it to proceed with the proposed Offer. It also sought the Exchange's consent to conduct the Possible Placing within 30 days after the Offer under Rule 10.06(3).

Relevant Listing Rules

7. Rule 8.08 states that:

"There must be an open market in the securities for which listing is sought. This will normally mean that:-

(1) (a) at least 25% of the issuer's total number of issued shares must at all times be held by the public;

…

(2) for a class of securities new to listing, at the time of listing there must be an adequate spread of holders of the securities to be listed, …. The number will depend on the size and nature of the issue, but in all cases there must be at least 300 shareholders; and

(3) not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders, …."

(Rule 8.08(1)(a) was amended on 11 June 2024. See Note below.)

8. Rule 13.32 states that:

"(1) Issuers shall maintain the minimum percentage of listed securities as prescribed by rule 8.08 at all times in public hands. …

(2) Once the issuer becomes aware that the number of listed securities in the hands of the public has fallen below the relevant prescribed minimum percentage the issuer shall take steps to ensure compliance at the earliest possible moment…

(3) If the percentage falls below the minimum, the Exchange reserves the right to require suspension of trading in an issuer's securities until appropriate steps have been taken to restore the minimum percentage of securities in public hands. In this connection, the Exchange will normally require suspension of trading in an issuer's securities where the percentage of its public float falls below 15% (or 10% in the case of an issuer that has been granted a lower percentage of public float under rule 8.08(1)(d) at the time of listing).

(4) Where the percentage has fallen below the minimum, the Exchange may refrain from suspension if the Exchange is satisfied that there remains an open market in the securities…

…"

9. Rule 10.06(3) states that:

"An issuer whose primary listing is on the Exchange may not make a new issue of shares or announce a proposed new issue of shares for a period of 30 days after any purchase by it of shares, whether on the Exchange or otherwise (other than an issue of securities pursuant to the exercise of warrants, share options or similar instruments requiring the issuer to issue securities, which were outstanding prior to that purchase of its own securities), without the prior approval of the Exchange."

(Rule 10.06(3) was amended on 11 June 2024. See Note below.)

Analysis

Public float requirements

10. The public float requirement seeks to ensure an open market for trading in listed securities and require at least 25% of the securities be held by the public at all times. Where there are insufficient securities in the hands of the public, trading will be suspended if it is necessary to avoid a disorderly market.

11. Company A proposed a withdrawal of listing in the overseas stock exchange by making a share repurchase offer to all existing shareholders. In the extreme case where all public shareholders accepted the Offer (other than those undertaken to Company A not to do so), Company A's shares would be held by a small number of shareholders and there might not be an open market in the shares in Hong Kong upon completion of the Offer. It was not in the interest of Company A's shareholders if trading suspension continued for a prolonged period due to the lack of an open market in the shares.

12. The Exchange would allow Company A to proceed with the proposal taking into account the following:

a. the purpose of the Offer was to facilitate the withdrawal of listing of Company A's shares from the overseas stock exchange. Company A intended to maintain a listing of its shares on the Exchange;

b. Company A had a wide spread of shareholders, and a number of shareholders undertook not to accept the Offer. The concern about a lack of open market in its shares would arise only if there was a very high take up of the Offer; and

c. Company A proposed to place new shares to independent placees to ensure an open market for trading its shares in Hong Kong upon completion of the Offer.

Possible Placing after the share repurchase offer

13. Rule 10.06(3) requires that an issuer seeks the Exchange's consent before issuing new shares or announcing a new issue of shares within 30 days after the purchase of its own shares. This is to ensure that the issuer does not affect the price of the new shares to be issued by the repurchase of its own shares.

14. In this case, the purpose of the Possible Placing was to ensure an adequate spread of shareholders in Hong Kong after the Offer. In Company A's announcement for the proposed Offer, there would be disclosure to inform the market of the Possible Placing after the Offer. The proposal did not raise concern on market manipulation.

Conclusion

15. The Exchange allowed Company A to proceed with the proposed Offer and gave consent for conducting the Possible Placing within 30 days after the Offer.

Note: Rule 8.08(1)(a) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the public float of the issuer. Rule 10.06(3) was amended on 11 June 2024 to (i) apply the existing moratorium period requirement for an issue of new shares to a resale of treasury shares and (ii) extend the carve-out provision to include the grant of share awards or options under a share scheme that complies with Chapter 17, or a new issue of shares or a sale or transfer of treasury shares under a capitalisation issue, upon vesting or exercise of share awards or options under the share scheme that complies with Chapter 17 or pursuant to the exercise of outstanding warrants, share options or similar instruments. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would approve a listed issuer's proposed issue of new shares after its redemption of convertible bonds

Facts

1. A Main Board issuer (**Company X**) exercised its option to redeem early all outstanding convertible bonds issued by it three years ago (**Early Redemption**).

2. It considered the Early Redemption to be in its interest and the interest of its shareholders as it would otherwise have had to pay 10% more to redeem the bonds on maturity a few months later.

3. It proposed to enter into an agreement within 30 days of the Early Redemption to place new shares to independent third parties. The purpose was to raise funds to repay loans due within one year and for general working capital. It sought the Exchange's approval of the proposal under Rule 10.06(3).

Relevant Listing Rules

4. Rule 10.05 states that:

   Subject to the provisions of the Code on Share Repurchases, an issuer may purchase its shares on the Exchange or on another stock exchange recognised for this purpose by the Commission and the Exchange. All such purchases must be made in accordance with rule 10.06. Rules 10.06(1), 10.06(2)(f) and 10.06(3) apply only to issuers whose primary listing is on the Exchange while the rest of rule 10.06(2) and rules 10.06(4), (5) and (6) apply to all issuers. The Code on Share Repurchases must be complied with by an issuer and its directors and any breach thereof by an issuer will be a deemed breach of the Exchange Listing Rules and the Exchange may in its absolute discretion take such action to penalise any breach of this paragraph or the listing agreement as it shall think appropriate. It is for the issuer to satisfy itself that a proposed purchase of shares does not contravene the Code on Share Repurchases.

5. Rule 10.06(3) states that:

> An issuer whose primary listing is on the Exchange may not make a new issue of shares or announce a proposed new issue of shares for a period of 30 days after any purchase by it of shares, whether on the Exchange or otherwise (other than an issue of securities pursuant to the exercise of warrants, share options or similar instruments requiring the issuer to issue securities, which were outstanding prior to that purchase of its own securities), without the prior approval of the Exchange.
>
> (Rule 10.06(3) was amended on 11 June 2024. See Note below.)

6. Rule 10.06(6)(c) states that

> for the purposes of rules 10.05, 10.06, 19.16 and 19.43 "shares" shall mean shares of all classes and securities which carry a right to subscribe or purchase shares, of the issuer provided that the Exchange may waive the requirements of those rules in respect of any fixed participation shares which are, in the opinion of the Exchange, more analogous to debt securities than equity securities. References to purchases of shares include purchases by agents or nominees on behalf of the issuer or subsidiary of the issuer, as the case may be.

Analysis

7. Rule 10.06(3) requires an issuer to seek the Exchange's approval before issuing new shares or announcing a new issue of shares within 30 days after its purchase of its own shares. This is to ensure that the issue of new shares does not take place at a market price that has been affected by the issuer's previous repurchase of its own shares.

8. Here, the convertible bonds fell within the definition of "shares" under Rule 10.06(6)(c) and the redemption fell within the meaning of "purchase of shares" under Rule 10.06(3). Therefore, Company X had to obtain the Exchange's approval under Rule 10.06(3) for its proposed issue of new shares under the placing agreement and publication of the related announcement.

9. The Exchange noted that the purpose of the Early Redemption and the proposed placing was to reduce Company X's debts. It was satisfied that the concern mentioned in paragraph 7 above did not arise.

Conclusion

10. Company X's proposed issue of new shares was acceptable under Rule 10.06(3).

Note: Rule 10.06(3) was amended on 11 June 2024 to (i) apply the existing moratorium period requirement for an issue of new shares to a resale of treasury shares and (ii) extend the carve-out provision to include the grant of share awards or options under a share scheme that complies with Chapter 17, or a new issue of shares or a sale or transfer of treasury shares under a capitalisation issue, upon vesting or exercise of share awards or options under the share scheme that complies with Chapter 17 or pursuant to the exercise of outstanding warrants, share options or similar instruments. The Rule amendments would not change the analysis and conclusion in this case.

HKEX Guidance Letter
HKEX-GL119-24

April 2024 *(Effective from 11 June 2024)*

Guidance on arrangements for listed issuers to hold or deposit treasury shares in CCASS

I. Background and purpose

1. Under the Listing Rules, a listed issuer may hold repurchased shares in treasury for future resale if it is permitted under the laws of the issuer's place of incorporation and its articles of association or equivalent constitutional documents. As the shareholders' rights (such as voting, dividend and distribution) attached to treasury shares are normally suspended by laws[1], the issuer shall ensure that treasury shares are appropriately identified and segregated.

2. In this regard, a listed issuer should have procedures in place to ensure that any movement of its issued shares and treasury shares are promptly and appropriately tracked and disclosed through next day disclosure returns and monthly returns. The issuer should provide appropriate instructions to the relevant parties, including its share registrar and broker, to ensure that a proper record of treasury shares is maintained (including any treasury shares held or deposited with Central Clearing and Settlement System (**CCASS**)).

3. This letter provides guidance to assist listed issuers in meeting their obligations to appropriately identify and segregate their treasury shares in CCASS (see section III.A).

4. This letter also provides guidance on the arrangements for shares repurchased by listed issuers for cancellation (see section III.B).

5. In this letter, references to dividends or distributions include other corporate events with entitlements (e.g. rights issues or open offers), and references to record date shall mean the last registration date if there is a book closure period.

II. Relevant Listing Rules

6. Main Board Rule 1.01 (GEM Rule 1.01) defines treasury shares as:

   "shares repurchased and held by an issuer in treasury, as authorised by the laws of the issuer's place of incorporation and its articles of association or equivalent constitutional documents which, for the purpose of the Rules, include shares repurchased by an issuer and held or deposited in CCASS for sale on the Exchange

   …"

[1] The exception is that under the company laws of some jurisdictions (e.g. Bermuda, the Cayman Islands, Singapore and the United Kingdom), treasury shares are entitled to distribution of bonus shares.

7. Main Board Rule 10.06(5) (GEM Rule 13.14) states that:

"Status of Purchased Shares

The shares repurchased by an issuer shall be held as treasury shares or cancelled. The listing of all shares which are held as treasury shares shall be retained. The issuer shall ensure that treasury shares are appropriately identified and segregated.

…"

III. Guidance

A. Treasury shares held for resale on the Exchange

8. A listed issuer intending to resell any treasury shares on the Exchange may hold or deposit such shares with CCASS registered under the name of HKSCC Nominees Limited (**HKSCCN**) as a common nominee. To facilitate the identification of treasury shares when they are held with CCASS, the issuer is expected to hold or deposit its treasury shares in a segregated account[2] in CCASS. It should also instruct the relevant broker to maintain a proper record of such treasury shares.

(1) Arrangements to hold or deposit treasury shares in CCASS

(a) Jurisdictions requiring treasury shares to be held in issuers' own names

9. If the laws of an issuer's place of incorporation (e.g. Bermuda and the Cayman Islands) require repurchased shares to be held in the issuer's own name in order to be classified as treasury shares, the issuer should, upon completion of the share repurchase, withdraw the repurchased shares from CCASS and register the repurchased shares in the issuer's register of members in its own name as treasury shares.

10. The issuer may re-deposit its treasury shares into CCASS only if it has an imminent plan to resell them on the Exchange, and it should complete the resale as soon as possible.

11. Although the repurchased shares would cease to be classified as treasury shares under the relevant laws when the legal titles of the shares are transferred to HKSCCN upon deposit with CCASS[3], such repurchased shares would continue to be treated in the same way as treasury shares registered in the issuer's own name under the Rules as they are beneficially owned by the issuer[4]. The issuer should, upon depositing any treasury shares in CCASS, give clear written instructions to its broker and share registrar that such repurchased shares would be treated as treasury shares under the Rules.

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2 A segregated account may be opened by a broker or custodian (which is a CCASS participant) for the issuer to hold its treasury shares separately from the securities belonging to other clients of such broker or custodian. In such case, references to a broker in this guidance letter shall mean a broker or custodian through which the issuer's treasury shares are held in CCASS. The issuer may also consider other options available for holding treasury shares separately in CCASS.

3 The withdrawal or re-depositing process of the treasury shares from/into CCASS (as the case may be) would not be treated as a share repurchase or a transfer of shares out of treasury under the Rules if the issuer complies with the Rules and this guidance letter.

4 Under Main Board Rule 1.01 / GEM Rule 1.01, treasury shares include, for the purpose of the Rules, shares repurchased by an issuer and held or deposited in CCASS for sale on the Exchange.

12. For any treasury shares deposited with CCASS pending resale on the Exchange, the issuer should have appropriate measures to ensure that it would not exercise any shareholders' rights or receive any entitlements which would otherwise be suspended under the relevant laws if those shares were registered in the issuer's own name as treasury shares. These measures include, for example, an approval by the issuer's board of directors that:

    (i) the issuer should procure its broker not to give any instructions to Hong Kong Securities Clearing Company Limited (**HKSCC**) to vote at general meetings for the treasury shares deposited with CCASS; and

    (ii) in the case of dividends or distributions, the issuer should withdraw the treasury shares from CCASS, and either re-register them in its own name as treasury shares or cancel them, in each case before the record date for the dividends or distributions.

13. The issuer should disclose the interim measures referred to in paragraph 12 in its explanatory statement for share repurchase mandate if it may hold treasury shares in CCASS for resale on the Exchange.

(b) Jurisdictions which allow treasury shares to be held by nominees on behalf of issuers

14. On the other hand, where the laws of a listed issuer's place of incorporation (e.g. the PRC) do not require treasury shares to be held in the issuer's name, shareholders' rights attached to the shares will be suspended under the laws once the shares are repurchased by the issuer, irrespective of whether they are held in the name of the issuer or its nominee. In such case, the issuer may continue to hold the repurchased shares as treasury shares in a segregated account in CCASS. The issuer shall, upon completion of the share repurchase, give clear written instructions to its share registrar and the relevant broker to update the record to clearly identify those repurchased shares held in CCASS as treasury shares.

(2) Disclosure

(a) Voting at general meetings

15. The issuer should disclose in the poll results announcement[5] the number of treasury shares held by the issuer (including any treasury shares held or deposited with CCASS), and that such treasury shares were excluded from the total number of issued shares entitled to attend and vote on the resolution(s) proposed at the general meeting. The issuer should also confirm in the announcement that it has not exercised the voting rights of the treasury shares at the general meeting.

(b) Dividends or distributions

16. The issuer should disclose in the announcement relating to the declaration of dividends or distributions (i) the number of treasury shares held by the issuer (including any treasury shares held or deposited with CCASS); and (ii) that such treasury shares would not receive the dividends or distributions[6].

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5 Main Board Rule 13.39(5)(a) / GEM Rule 17.47(5)(a)

6 In circumstances (such as distributions of bonus shares) where treasury shares are entitled to the distributions under the relevant laws (see footnote 1), the issuer should include a clarification in the announcement.

17. Where the issuer is incorporated in a jurisdiction requiring treasury shares to be held in its own name, it should also disclose in the announcement that it will withdraw all repurchased shares (if any) from CCASS, and either re-register them in its own name as treasury shares or cancel such repurchased shares, in each case before the record date for the dividends or distributions.

(3) Notification to HKSCC

18. If there remains any treasury shares held with CCASS which are not entitled to the dividends or distributions on the record date, the issuer should give clear written instructions to its share registrar to exclude such treasury shares in determining HKSCCN's entitlements to the dividends or distributions. The issuer and its broker should also promptly notify HKSCC the number of treasury shares held with CCASS, details of the broker and other information HKSCC may prescribe from time to time. HKSCC will exclude such treasury shares based on the notifications in allocating the dividends or distributions among the CCASS participants.

B. Repurchased shares pending cancellation

19. Main Board Rule 10.06(5) (GEM Rule 13.14) provides that the listing of any shares repurchased by an issuer but not held as treasury shares shall be automatically cancelled upon repurchase. The documents of title for the repurchased shares shall be cancelled and destroyed as soon as reasonably practicable following settlement of any such repurchase.

20. Accordingly, an issuer should promptly instruct its broker to withdraw the repurchased shares from CCASS so as to complete the cancellation process with its share registrar. It should not exercise any shareholders' rights to attend and/or vote at the general meetings, or receive any dividend or distribution for the repurchased shares pending cancellation. The disclosure guidance on announcements relating to poll results and dividends or distributions in paragraphs 15 and 16 also applies to repurchased shares pending cancellation (if any).

21. If an issuer repurchased shares before the ex-date for any dividend or distribution but has not withdrawn the shares from CCASS for cancellation on or before the record date, the issuer should instruct its share registrar to exclude such repurchased shares in determining HKSCCN's entitlements. The issuer and the relevant broker should promptly notify HKSCC the number of such repurchased shares held in CCASS, details of the broker and other information HKSCC may prescribe from time to time.

Treasury shares

Shareholders' mandate for resale of treasury shares

1. For a dual primary listed issuer having a listing on the Exchange and an overseas stock exchange:

(a) Does the shareholders' approval requirement under MB Rule 13.36 / GEM Rules 17.39 to 17.41 apply to its resales of treasury shares on the overseas stock exchange?

Yes, because the issuer's treasury shares are listed on both the Exchange and the overseas stock exchange.

(b) Whether the benchmarked price in MB Rules 13.36(5) and 13.36(5A) / GEM Rules 17.42B and 17.42BB should be determined with reference to the closing prices of the issuer's shares traded on the Exchange or any other stock exchange?

The benchmarked price should be determined with reference to the closing prices of the issuer's shares traded on the Exchange (whether the resale is made on the Exchange or otherwise).

MB Rules 13.36(1A), 13.36(5) and 13.36(5A)
GEM Rules 17.39A, 17.42B and 17.42BB
First released: April 2024

2. For an A+H issuer, does the shareholders' approval requirement under MB Rule 13.36 / GEM Rules 17.39 to 17.41 apply to its resales of treasury A shares listed on a PRC stock exchange?

No. Resales of treasury A shares are carved out from the shareholders' approval requirement as they are not listed on the Exchange and are not fungible.

MB Rule 13.36(1A)
GEM Rule 17.39A
First released: April 2024

Moratorium period for new issues of shares or resales of treasury shares after a share repurchase

3. MB Rule 10.06(3)(a) / GEM Rule 13.12 provides that the moratorium period will not apply to an issue of new shares or a transfer of treasury shares pursuant to the exercise of warrants, share options or similar instruments requiring the issuer to issue or transfer shares, which were outstanding prior to the share repurchase. Does this carve-out provision apply to a new issue of shares or a transfer of treasury shares upon conversion of convertible securities?

This carve-out provision also applies to an issue of new shares or a transfer of treasury shares upon conversion of convertible securities, provided that the convertible securities were issued with subscription monies fully settled prior to the share repurchase.

MB Rule 10.06(3)(a)
GEM Rule 13.12
First released: April 2024

Intention statement regarding repurchased shares

4. What should a listed issuer disclose in its explanatory statement if it does not have a firm intention on the treatment of repurchased shares when seeking shareholders' approval for the repurchase mandate?

It is acceptable for a listed issuer to disclose in its explanatory statement that it may cancel any shares it repurchased and/or hold them as treasury shares subject to, for example, market conditions and its capital management needs at the relevant time of the repurchases.

However, when the listed issuer reports any repurchase of shares in the next day disclosure return, it must clearly identify the number of repurchased shares that are cancelled or held as treasury shares, and where applicable, disclose the reasons for any deviation from the intention statement previously disclosed in the explanatory statement.

MB Rule 10.06(1)(b)(xii)
GEM Rule 13.08(12)
First released: April 2024

Implementation of the amended Rules

5. The amended Rules relating to treasury shares will become effective on 11 June 2024 (the Effective Date). Can a listed issuer seek shareholders' approval for the amendments to its constitutional documents before the Effective Date to allow the issuer to hold and use treasury shares to the extent permitted under all applicable laws, rules and regulations?

Yes.

MB Rule 13.51(1)
GEM Rule 17.50(1)
First released: April 2024

6. Under the amended Rules, a listed issuer may use a general mandate approved by its shareholders to issue new shares or resell treasury shares.

(a) Does the general mandate need to specifically authorise the resale of treasury shares in order for the listed issuer to use such general mandate for its resale of treasury shares?

Yes.

(b) If so, can a listed issuer seek such a general mandate from its shareholders before the Effective Date?

Yes, provided that the listed issuer shall specify that it may use such general mandate for its resale of treasury shares only after the Rule amendments has come into effect.

MB Rule 13.36(2)(b)
GEM Rule 17.41(2)
First released: April 2024

7. Does a listed issuer need to amend the rules of its existing share scheme in order for it to satisfy share grants using treasury shares, and if so, will such amendments to the scheme rules be regarded as material amendments requiring shareholders' approval under MB Rule 17.03(18) / GEM Rule 23.03(18)?

Under the amended Rules, the scheme rules should be amended to allow the use of treasury shares to satisfy share grants. However, the Exchange would normally not regard such amendments as a material alteration to the scheme rules under MB Rule 17.03(18) / GEM Rule 23.03(18).

MB Rule 17.03(18)
GEM Rule 23.03(18)
First released: April 2024

8. A listed issuer has obtained a repurchase mandate from its shareholders before the Effective Date in accordance with the existing MB Rule 10.06 / GEM Rules 13.08 and 13.09.

(a) Can the issuer hold any shares repurchased under such mandate on or after the Effective Date as treasury shares under the amended Rules?

Yes, provided that it is permitted by the laws of the issuer's place of incorporation and its constitutional documents, and the resolution granting the repurchase mandate does not restrict the issuer from holding repurchased shares in treasury.

(b) If the issuer has repurchased shares before the Effective Date which are yet to be withdrawn from CCASS for cancellation, can the issuer continue to hold such repurchased shares in CCASS after the Effective Date and treat them as treasury shares under the amended Rules?

No. The listing of all shares repurchased by the issuer before the Effective Date is automatically cancelled upon repurchase. The issuer must promptly withdraw any such repurchased shares from CCASS to complete the cancellation process with its share registrar.

MB Rule 10.06
GEM Rules 13.08 and 13.09
First released: April 2024

9. Under the amended Rules, the restricted period for on-Exchange share repurchases and grants of options or awards under share schemes will be adjusted from one month to 30 days immediately before the date of board meeting for the approval of the issuer's financial results. The amended Rules also impose a 30-day restricted period on resales of treasury shares on the Exchange.

Should a listed issuer follow one-month or 30-day restricted period if its board meeting is scheduled on or after the Effective Date while the restricted period commences before the Effective Date?

The 30-day restricted period under the amended Rules will apply if the board meeting is scheduled on or after the Effective Date based on the issuer's first notification to the Exchange.

MB Rules 10.06(2)(e), 10.06A(3) and 17.05
GEM Rules 13.11(4), 13.14A(3) and 23.05
First released: April 2024

10

Continuing obligations

Guide on Preparation of Annual Report

May 2025

Table of Contents

Introduction

Annual report is an important corporate communication tool for a listed issuer to present material and relevant information on its financial results and operational performance for investors' assessment.

The Listing Rules set out the minimum information an issuer must include in its annual report. As part of our monitoring activities, we undertake an on-going programme to review issuers' annual reports and publish, on an annual basis, findings of our reviews and recommendations to enhance issuers' disclosure and approach to internal controls. Some of these recommendations have been subsequently codified into the Listing Rules.

Under the programme:

- We assess issuers' compliance with the disclosure requirements under the Listing Rules and, based on their disclosure, identify and follow up on potential material non-compliances with the Listing Rules and other misconduct.

- We also adopt a thematic approach, selecting specific areas for review based on results of previous years' reviews and matters considered to be of higher regulatory risks. We consider whether material information was disclosed to allow shareholders to properly assess the matters reported on and whether proper internal controls were maintained.

- To enhance quality of financial disclosure, we also assess issuers' compliance with specific accounting standards in their financial statements.

This Guide on Preparation of Annual Report (**Guide**) summarises the relevant Listing Rule requirements and our recommendations to facilitate issuers in preparing annual reports. It will be updated as and when necessary.

This Guide has three sections:

- Section 1 provides all the disclosure requirements for annual report under the Listing Rules and related guidance materials published by the Exchange.

- Section 2 contains prevailing recommended disclosure in specific areas from our thematic review.

- Section 3 summarises our guidance for financial disclosure under prevailing requirements (including specific accounting standards).

In addition to the disclosure requirements presented in this Guide, issuers should ensure that their annual reports fully comply with all other relevant laws, rules and regulations and industry guidelines, as applicable.

1. Mandatory disclosure requirements under the Rules

1. The disclosure requirements for annual report under the Rules[1] are set out in Appendix D2 to the MB Rules (GEM Chapter 18) and other Chapters, as supplemented by guidance materials[2] published by the Exchange on certain specific matters.

2. Issuers should ensure their annual reports fully disclose the below required information, where applicable:

Subject matter	Issuer must include in its annual report	
Directors, senior management and shareholders	*Directors and senior management*	
	▪ Brief biographical details, competing business, service contract, permitted indemnity provision of directors and/or senior management, and any public sanctions made against them by statutory or regulatory authorities	*MB Rules 2A.10A(1), 8.10(2)(b) and (c), 13.51B(1), and para. 6.3(a), 6.3(h), 12, 14, and 28(2)(a) to (c) and (e) of App. D2 / GEM Rules 3.11A, 11.04, 17.50A(1), note 4(f) to 18.07, 18.07A(2)(a) to (c) and (e), 18.24, 18.39, 18.44(1) and 18.45*
	▪ Disclosure of interests information of directors and chief executives	*Para. 6.3(m), 13 and 28(2)(e) of App. D2, and Practice Note 5 to MB Rules / GEM Rules 18.07A(2)(e), 18.15 to 18.17 and 18.17A*
	▪ Emolument information, including directors', past directors', and five highest paid individuals' emoluments, remuneration payable to senior management by band, emolument policy and arrangement to waive directors' emoluments (if any)	*Code provision E.1.5 of App. C1, and para. 6.3(n), 24 to 25, and 28(1)(a) and (c) of App. D2 to MB Rules / GEM Rules note 4(j) to 18.07, 18.07A(1)(a) and (c), 18.28 to 18.30 and code provision E.1.5 of App. C1*
	▪ Details of significant transaction, arrangement or contract that a director or a connected entity was materially interested	*Para. 15 and 28(2)(e) of App. D2 to MB Rules / GEM Rules 18.07A(2)(e) and 18.25*
	▪ Confirmation of newly appointed director's understanding on his/her obligations and date of relevant legal advice obtained by director	*MB Rule note 2 to 3.09D / GEM Rule note 2 to 5.02D*
	▪ Annual independence confirmation of independent non-executive director (**INED**), and an explanation on why an INED is considered to be independent if he/she cannot meet any of independence guidelines under the Rules	*MB Rules 3.13, 3.14, and para. 12A and 12B of App. D2 / GEM Rules 5.09, 5.10, 18.39A and 18.39B*
	Shareholders	
	▪ Details of loan requiring shares pledged by controlling shareholder and loan agreements with covenants on controlling shareholder's specific performance	*MB Rules 13.21, and para. 6.3(d) and 6.3(e) of App. D2 / GEM Rules 17.23, and notes 4(b) and 4(c) to 18.07 / Guide for New Listing Applicants, Ch. 3.8, para. 4(i)*
	▪ Details of any significant contract between the issuer's group and the controlling shareholder's group	*Para. 16 of App. D2 to MB Rules / GEM Rules 18.26 and 18.27 / Guide for New Listing Applicants, Ch. 3.8, para. 4(ii)*
	▪ Disclosure of interests information of substantial shareholders and other persons pursuant to Part XV of the Securities and Futures Ordinance	*Para. 6.3(m) and 13 of App. D2, and Practice Note 5 to MB Rules / GEM Rules 18.15 to 18.17, 18.17B and 18.17C*
	▪ Details of arrangement to waive shareholders' dividends (if any)	*Para. 17 of App. D2 to MB Rules / GEM Rule 18.31*

1 In this Guide, "Rules" refer to both Main Board (**MB**) Rules and GEM Rules.
2 They include guidance letters, FAQs and Guide for New Listing Applicants.

Subject matter	Issuer must include in its annual report	
Financial reporting, accounting and auditing matters	*Financial reporting and accounting*	
	▪ Audited financial statements, basic financial information, including profit/loss on sale of properties, ageing analysis of accounts receivable and payable, rates of dividend paid/proposed and amounts absorbed, reserves available for distribution, and a five-year financial summary	*MB Rules 13.46, para. 2 to 4, 19, 28(1)(b)(ii) and (2)(e), and 29 of App. D2 / GEM Rules 18.03, 18.07A(1)(b)(ii) and (2)(e), 18.33, 18.37, 18.46, 18.47 and 18.50B*
	▪ Minimum required information where an issuer receives a modified audit opinion[3] ***(See also section 2.1)***	*Para. 3.1 of App. D2 to MB Rules / GEM Rule note to 18.47*
	▪ Principal activities, a discussion and analysis of the group's performance during the financial year and the material factors underlying its results and financial position, and recommended additional commentary ***(See also sections 2.2 and 2.3)***	*Code provision A.1.2 of App. C1, and para. 6.3(n), 28(2)(a) and (d), 32 and 52 of App. D2 to MB Rules / GEM Rules note 4(j) to 18.07, 18.07A(2)(a) and (d), 18.41, 18.83 and code provision A.1.2 of App. C1*
	▪ An analysis of loans and borrowings, information on breach of significant loan agreement by issuer, details of advance to entity, and financial assistance and guarantees to affiliated companies, and a combined balance sheet of affiliated companies ***(See also section 2.4)***	*MB Rules 13.20 to 13.22, and para. 6.3(c), 6.3(f), 6.3(g), 22 and 28(1)(b)(i) of App. D2 / GEM Rules 17.22 to 17.24, notes 4(a), 4(d) and 4(e) to 18.07, 18.07A(1)(b)(i) and 18.21*
	▪ Information on subsidiaries, pension scheme, largest and five largest customers and suppliers, and properties held for development and/or sale or for investment purposes where any percentage ratios exceed 5%	*Para. 9, 23, 26, 28(1)(b)(iii) and 31 of App. D2 to MB Rules / GEM Rules 18.07A(1)(b)(iii), 18.10, 18.23, 18.34 and 18.40*
	▪ Body of accounting standards followed, reasons for any change and/or significant departure from accounting standard adopted, and nature and amount of material changes in accounting estimates	*Notes 2.2 and 2.5 to para. 2, and para. 5 of App. D2 to MB Rules / GEM Rules note to 18.04, 18.06, note 3 to 18.07, 18.19 and 18.20*
	▪ Explanation for any material differences between the net income shown in the financial statements and published profit forecast	*Para. 18 of App. D2 to MB Rules / GEM Rule 18.18*
	Auditing	
	▪ Details of change in auditors in preceding three years	*Para. 30 of App. D2 to MB Rules / GEM Rule 18.42*
	▪ Remuneration of auditor	*Para. 28(1)(b)(iv) of App. D2 to MB Rules / GEM Rule 18.07A(1)(b)(iv)*
Issue of securities or resale of treasury shares and related matters	*Issue of securities or resale of treasury shares*	
	▪ Details of current year's equity fundraisings or sale of treasury shares for cash, and amount of proceeds brought forward from previous years' equity fundraising and sale of treasury shares, and details of use of proceeds	*Para. 10(4), 11, 11A, 28(2)(e) and 50(1) of App. D2 to MB Rules / GEM Rules 18.07A(2)(e), 18.14, 18.32, 18.32A and 18.81(1)*
	▪ A monthly breakdown of on-market sales of treasury shares during the financial year, reference in directors' report on on-market sales of treasury shares, reasons for sales, and total funds raised with details of use of proceeds	*MB Rules 10.06B(3) and para. 6.3(b) of App. D2 / GEM Rules 13.14B(3) and note 4(k) to 18.07*
	Convertible securities, options, warrants or similar rights	
	▪ Details of any convertible securities, options, warrants or similar rights issued/granted, redeemable securities, exercise of any conversion or subscription rights, and purchase, sale, redemption or cancellation by issuer during the financial year	*Para. 10 of App. D2 to MB Rules / GEM Rules 18.11 to 18.13*
	▪ Details of outstanding redeemable securities and convertible securities, and the dilutive impact	*Para. 10(3) of App. D2 to MB Rules / GEM Rule 18.13 / GL80-15, para. 14*
Public float	▪ A statement of sufficiency of public float	*MB Rules 13.35 and para. 34A of App. D2 / GEM Rules 17.38A and 18.08B*

[3] The requirement will apply to annual reports in respect of financial years commencing on or after 1 July 2025.

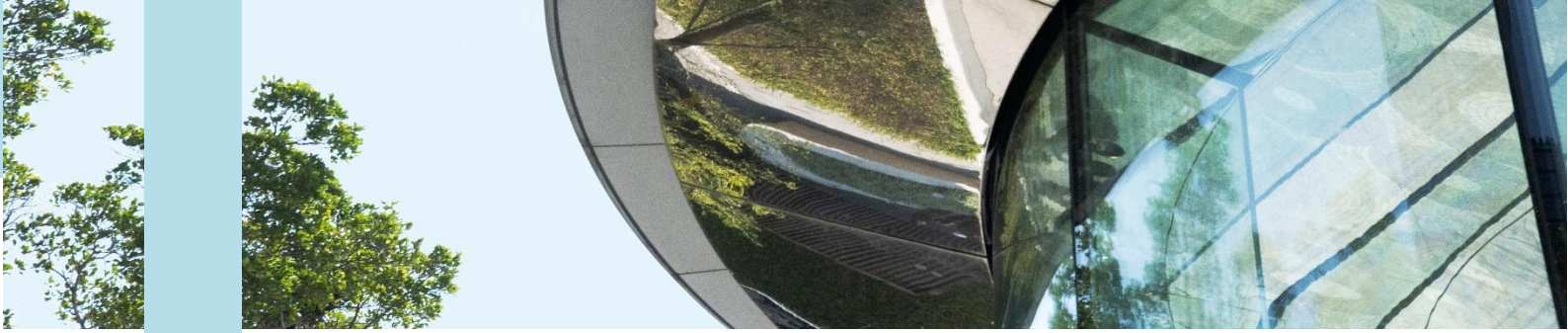
Subject matter	Issuer must include in its annual report	
Repurchase of securities and treasury shares	▪ A monthly breakdown of purchases of shares during the financial year, reference in directors' report on purchases of shares, and reasons for purchases	*MB Rules 10.06(4)(b) and para. 6.3(b) of App. D2 / GEM Rules 13.13(2) and note 4(k) to 18.07*
	▪ Details of purchase or redemption of listed securities during the financial year, and number of treasury shares (if any) held as at year end date and their intended use	*Para. 10(4) and 50(1) of App. D2 to MB Rules / GEM Rules 18.14 and 18.81(1)*
Notifiable transactions	*Performance guarantees* ▪ Whether the actual performance of the company or business acquired meets the guarantee ***(See also section 2.5)***	*MB Rules 14.36B(3), 14A.63(3) and para. 6.3(i) of App. D2 / GEM Rules note 4(h) to 18.07, 19.36B(3) and 20.61(3)*
	Acquisition, disposal and lease of aircraft ▪ Where a waiver is granted on disclosure requirement of actual consideration for aircraft acquisition, aggregate number, breakdown by aircraft model, aggregate net book value and/or commitment amounts of aircraft owned and/or committed to purchase	*MB Rule note (b) to 14.58(4) / GEM Rule note (b) to 19.58(5)*
	▪ Where a Qualified Aircraft Leasing Activity[4] is exempt from notifiable transactions requirements, aggregate number, breakdown by aircraft model, aggregate net book value, commitment amounts, aggregate net gain or loss on aircraft disposal of aircraft owned, committed to purchase and/or sold, and average lease rental yield of aircraft leasing	*MB Rule 14.33D(2) / GEM Rule 19.33D(2)*
Connected transactions	▪ Terms of connected transactions (including continuing connected transactions (**CCTs**))	*MB Rules 14A.49, 14A.71(1) to (5) and para. 8(1) of App. D2 / GEM Rules 18.09(1), 20.47 and 20.69(1) to (5)*
	▪ Auditors' and INEDs' review findings and confirmation on CCTs during the financial year	*MB Rules 14A.71(6) and para. 8(1) of App. D2 / GEM Rules 18.09(1) and 20.69(6)*
	▪ A confirmation statement on whether any related party transaction was connected transaction and whether such transaction complied with connected transaction requirements	*MB Rules 14A.72 and para. 8(2) of App. D2 / GEM Rules 18.09(2) and 20.70*
	▪ A confirmation statement on whether issuer has followed its pricing policies when determining the price and terms of CCTs conducted during the financial year	*GL73-14, para. 11*
	▪ Where an IPO waiver is granted on monetary annual cap requirement, basis of transaction amount calculation and related amounts of CCTs	*Guide for New Listing Applicants, Ch. 3.9, para. 6(i)*
Share schemes	▪ Terms, movement, scheme mandate limit and material matters reviewed and/or approved by remuneration committee of share schemes funded by new shares, treasury shares and existing shares	*MB Rules 17.07, 17.07A, 17.09, 17.12(1) and para. 6.3(j) of App. D2 / GEM Rules note 4(i) to 18.07, 23.07, 23.07A, 23.09 and 23.12(1)*

[4] As defined in MB Rule 14.04(10D) / GEM Rule 19.04(10D)

Subject matter	Issuer must include in its annual report	
Newly listed issuers	▪ Progress of rectification of non-compliance disclosed in the prospectus that can only be rectified shortly after listing and explanation for any delay	*Guide for New Listing Applicants, Ch. 1.2D, para. 7*
	▪ Where issuer and/or its shareholders undertook to the Exchange at the time of listing on disclosure of sanctioned activity, details, status and plans of any new and/or existing sanctioned activity, and efforts in monitoring its business exposure to sanctions risks	*Guide for New Listing Applicants, Ch. 4.4, para. 6(iii)*
	▪ Decisions on matters reviewed by INEDs on corporate governance measures to resolve actual/potential conflicts of interests between issuer and its controlling shareholders (including why business opportunities referred to issuer by its controlling shareholders were not taken up)	*Guide for New Listing Applicants, Ch. 3.8, para. 3*
	▪ Valuation amount and additional depreciation (if any) of property interests valued under MB Chapter 5 / GEM Chapter 8 or other tangible assets valued where such valuation was included in the prospectus and those assets are not stated at valuation in the first annual financial statements published after listing	*Para. 27 of App. D2 to MB Rules / GEM Rule 18.35*
	(See also section 2.6)	
Issuers listed under special listing regimes or other listing structures	*Overseas issuers / PRC issuers*	
	▪ (including also secondary listed issuers) Information in the auditors' report, including audit opinion, applicable act, ordinance or other legislation, authority / body of auditing standards, and where a body of financial reporting standards other than HKFRS or IFRS is adopted, a reconciliation statement setting out the financial effect of material differences (if any) from HKFRS or IFRS	*MB Rules 19.22, 19.23, 19.25, 19.25A, 19A.33, 19A.34, 19A.37, 19C.18, 19C.19, 19C.22 and 19C.23 / GEM Rules 24.15, 24.16, 24.18, 24.18A, 25.27, 25.28 and 25.30 / GL111-22, para. 31, Guide for New Listing Applicants, Ch. 2.1, para. 31, Ch. 3.11, para. 5*
	▪ Whether the auditors or reporting accountants for a PIE Engagement[5] are the Registered or Recognised PIE Auditors[5]	*FAQ3.3 – No.5*
	▪ A statement that no pre-emptive rights exist in the jurisdiction that the issuer is incorporated or otherwise established (where applicable)	*Para. 20 of App. D2 to MB Rules*
	▪ Necessary information to enable shareholders to obtain taxation relief	*Para. 21 of App. D2 to MB Rules / GEM Rules 24.19 and 25.31*
	Mineral companies / Issuers publicly disclosed resources and/or reserves	
	▪ Details of exploration, development and mining production activities, a summary of expenditure incurred on these activities during the financial year, and annual updates on the resources and reserves (including mining assets that have been waived from reporting in the competent person's report at time of IPO)	*MB Rules 18.14, 18.16, 18.17, and para. 6.3(k) of App. D2 / GEM Rules note 4(g) to 18.07, 18A.14, 18A.16, 18A.17 / GL47-13, para. 7 to 11, Guide for New Listing Applicants, Ch. 2.6, para. 7*
	▪ Where an issuer (which is not a mineral company defined under MB Chapter 18 / GEM Chapter 18A) publicly disclosed details of resources and/or reserves, an update of those resources and/or reserves	*MB Rules 18.15 and para. 6.3(k) of App. D2 / GEM Rules note 4(g) to 18.07 and 18A.15*
	Investment companies	
	▪ Details of all investments with a value greater than 5% of the investment company's gross assets and at least the 10 largest investments	*MB Rules 21.12(1)(a) and para. 6.3(l) of App. D2*
	▪ An analysis of any provision for diminution in investment value, and realised and unrealised surpluses	*MB Rule 21.12(1)(b) and (c), and para. 6.3(l) of App. D2*

[5] As defined in MB Rule 1.01 / GEM Rule 1.01

Subject matter	Issuer must include in its annual report	
Issuers listed under special listing regimes or other listing structures (cont'd)	*Weighted voting rights (**WVR**)*	
	▪ Identities of beneficiaries of WVR, impact of potential conversion and all circumstances in which the WVR attached to the share will cease	*MB Rules 8A.39 to 8A.41*
	▪ A warning statement to inform prospective investors of potential risks of investing in an issuer with a WVR structure	*MB Rules 8A.37 and 8A.38*
	Biotech companies	
	▪ Details of research and development activities, and a summary of corresponding expenses during the financial year	*MB Rules 18A.08(1) and (2)*
	▪ A warning statement that a core product(s) may not be successfully developed and marketed	*MB Rule 18A.08(3)*
	(See also section 2.7)	
	Specialist technology companies	
	▪ Total number of securities in issuer held by each person that is subject to lock-up requirements	*MB Rule 18C.18 / Guide for New Listing Applicants, Ch. 2.5, para. 66 and 67*
	▪ Details of research and development, and a summary of corresponding expenses during the financial year	*MB Rules 18C.19(1) and (4)*
	▪ Timeframe for, and any progress made towards, achieving the revenue requirement, and updates on any revenue, profit and other business and financial estimates provided in the listing document, and any subsequent updates published by the issuer	*MB Rules 18C.19(2) and (3)*
	▪ A warning statement that the issuer may not achieve the revenue requirement	*MB Rule 18C.19(5)*
	*Special purpose acquisition companies (**SPACs**)*	
	▪ Significant accounting policies and judgements for SPAC transactions, and material events that occurred subsequent to the balance sheet date	*GL113-22, para. 13, Guide for New Listing Applicants, Ch. 2.4, para. 13*
	Issuers that adopted contractual arrangements	
	▪ Details of material contractual arrangements, including particulars of operating entity and its registered owners, major terms, reasons for adoption, any material changes, associated risks, actions taken to mitigate the risks, and any termination during the financial year	*GL77-14, para. 19*
	Issuers with stapled securities	
	▪ Details of stapled structure	*Guide for New Listing Applicants, Ch. 5.4, para. 14*
Corporate governance / environmental, social and governance	▪ Information required under the Corporate Governance Code and the Environmental, Social and Governance Reporting Guide ***(see also our "Analysis of 2022 Corporate Governance Practice Disclosure" and "2024 Analysis of ESG Practice Disclosure")***	*MB Rules 13.89, 13.91, App. C1, App. C2, and para. 6.4, 34 and 50(2) of App. D2 / GEM Rules 17.101, 17.103, note 5 to 18.07, 18.44(2), 18.81(2), App. C1 and App. C2*
Others	▪ Stock code of the issuer	*MB Rule 13.51A / GEM Rule 17.52A*
	▪ GEM characteristics statements for GEM issuers	*GEM Rules 2.20 and note 2 to 18.07*



2. Recommended disclosure in specific areas from thematic review

2.1 Financial statements with auditors' modified opinions

1. An issuer is obliged to present financial statements that give a true and fair view of its state of affairs, operation results and cashflows. If an issuer receives a modified audit opinion [6], it must, as a minimum, disclose in its annual report (i) details of the modifications and financial impact; (ii) management's position and basis on major judgmental areas; (iii) audit committee's view; and (iv) plans to address the modifications [7]. To enhance the quality of disclosure, we recommend issuers duly consider the following, to the extent applicable, for inclusion in their annual reports:

	Details of modifications and their actual or potential impact on the issuer's financial position – in describing the modifications, the issuer should disclose the underlying issues that led to the auditors' concerns and why it was unable to provide sufficient information to address these concerns, eventually resulting in the modifications.
	Management's position and basis on major judgmental areas, and how the management's view is different from that of auditors – this covers any situation where the different view has led to a modified audit opinion, whether it relates to, for example, a disagreement in accounting estimates based on assumptions and judgment or disagreement by the management with the auditors' request for information or audit evidence.
	Audit committee's view towards the modifications, and whether the audit committee reviewed and agreed with the management's position concerning major judgmental areas – where the audit committee disagreed, the issuer should disclose areas and basis of the committee's disagreement.
	Issuer's proposed plans to address the modifications – the issuer should disclose its action plan, implementation timetable and consider making progress update from time to time. In addition, for repeated modifications, the issuer should disclose the actions taken and whether it had followed its action plans during the current financial year, and the reasons for any material deviation.

Reminder on formulating plans to address audit modifications

- Issuers and their audit committees should engage in discussion with the auditors about the proposed action plans to increase the chance of successfully addressing the auditors' concerns and resolving the audit issues.

6 It covers "qualified opinion", "adverse opinion" and "disclaimer of opinion".
7 Paragraph 3.1 of Appendix D2 to the MB Rules / GEM Rule note to 18.47. The requirement will apply to annual reports in respect of financial years commencing on or after 1 July 2025.

2.2 Management discussion and analysis (MD&A)

2. The MD&A (or management commentary) on the financial statements provides narrative elaboration of the business trends and year-on-year variances (both positive and negative) of the financial results of an issuer compared to the preceding year. A well-prepared MD&A will enable investors to understand the key drivers of the issuer's financial performance, risks and uncertainties of its business and related mitigating measures.

3. The Rules highlight specific areas that issuers must, as a minimum, provide commentary on in the MD&A section[8]. To enhance the quality of disclosure, we recommend issuers duly consider the following in determining what information to present in their MD&A:

Business review

Issuers should provide sufficient explanations of their performance and identify the underlying causes or business factors that had led to their operating results during the financial year. For instance,

External factors – where the issuer experienced material changes in external environment relevant to its business (e.g. economic/industry downturn; increased market competition; and trade restrictions arisen from geopolitical tensions), it should enhance its industry overview disclosure and explain how, in concrete terms, these changes have impacted the issuer's financial performance and position. The issuer should also discuss its strategy and/or actions to tackle such changes.

Internal factors – the issuer should identify internal factors driving or contributing to its financial results. For example:

- significant events (e.g. launch of new products/services or breach of laws and regulations);
- significant transactions (e.g. mergers and acquisitions); and
- significant changes in, for instances, operating strategies (e.g. pricing policy or product mix), business model (e.g. shift from self-operated stores to franchising), or relationship with key stakeholders (e.g. success/failure in securing new contracts, or losing existing major customers).

The issuer should discuss the reasons underlying these changes and analyse the impact on its results.

Use of performance/efficiency indicators or industry specific ratios – where the management adopts such indicators or ratios (e.g. ARPU for telecom sector and GMV for e-commerce sector) to gauge and keep track of performance and efficiency, the issuer should disclose results of such indicators/ratios for the year, and also discuss factors causing any changes (or trend) to enable investors to evaluate how the issuer has performed over time and as compared to industry peers. As such disclosure typically involves presentation of non-GAAP financial measures, issuers should also take note of our guidance in section 3.7.

[8] Paragraphs 28(2)(d) and 32 of Appendix D2 to the MB Rules / GEM Rules 18.07A(2)(d) and 18.41

Business review (cont'd)

Material line items reported on the financial statements – the issuer should provide suitable explanations to facilitate investors' understanding of the nature of such items and reasons for changes during the year. For example,

Other expenses – where the issuer combined various costs and expenses and reported them as "other expenses" on its financial statements, it should provide additional information about such expenses (e.g. by providing breakdown in footnote) if they are material and further disclosure will be useful for investors to better understand the issuer's cost structure and drivers of its financial performance during the year.

Principal risks and uncertainties

They vary according to the nature of issuers' businesses and specific circumstances. Issuers should identify risks and uncertainties which are **most relevant and significant** for discussion and avoid obscuring material disclosure (i.e. the risks and uncertainties that issuers are genuinely concerned about) with unnecessary or immaterial information. The discussion should include management's assessment on how these risks and uncertainties:

have affected, and are likely to affect, their operation, financial position and business plans; and

can be mitigated, to the extent possible.

Liquidity and financial resources

Issuers should provide an assessment of their liquidity positions and working capital sufficiency with reference to their various needs and commitments. For example, where an issuer contemplated making a material capital investment (e.g. building new production plants), it should discuss:

how it plans to meet the relevant capital expenditure requirements, as well as the requirement to support daily operations and financial commitments (e.g. debt repayment); and

whether there are any tentative fundraising activities in the coming year.

Another example is the issuer's refinancing plan if maturity of material outstanding borrowings/debt instruments is approaching.

4. The above serves to provide general guidance on areas issuers should consider covering in their MD&A section, which are not meant to be exhaustive. Issuers should have due regard to their own circumstances in determining the appropriate information (in terms of type, scope and level of detail) with a view to facilitating investors in appraising the issuers' past and future performance.

The MD&A presentation should be…

Clear | Concise | Fair | Understandable | Balanced

5. In drafting MD&A, directors should also ensure that the presentation is fair, balanced and understandable, such that both good and bad news are presented and reported clearly and evenly, without glossing over or omitting material facts. Directors should endeavour to make the MD&A section informative and **avoid using boilerplate statements**. They are encouraged to challenge past practices of how key information is structured and conveyed, and make improvements as necessary.

6. **As a guiding principle, issuers should strive to have their MD&A disclosure on par with the disclosure standard of a listing document.**

Other reference materials

- Accounting Bulletin 5 published by the Hong Kong Institute of Certified Public Accountants (**HKICPA**)
- Clear and Concise: A Director's Guide to Writing the Business Review of an Annual Report published by the Hong Kong Institute of Directors
- Guidance materials on HKICPA's designated webpage "New Companies Ordinance Resource Centre"

2.3 Material asset impairments

7. Where an issuer reported a material asset impairment in its financial statement, it should discuss the circumstances that led to the impairment as part of its discussion on significant events or transactions during the financial year[9].

8. Where the impairment is supported by a valuation, issuers should disclose details of such valuation, including:

- Valuation method and reason for using that method
- Details of values of inputs used together with basis and assumptions
- Explanation on any changes in valuation method used or inputs or assumptions

Other references materials on directors' duties on acquisitions

- The Exchange's Listing Regulation and Enforcement (**LRE**) Newsletter Issue 5 (December 2021) – "Directors' responsibilities when assessing transactions"
- Guidance note on directors' duties in the context of valuations in corporate transactions (May 2017) published by the Securities and Futures Commission (**SFC**)

[9] Paragraph 32 of Appendix D2 to the MB Rules / GEM Rule 18.41

2.4 Material lending transactions

9. Issuers that conducted material lending transactions are encouraged to enhance their disclosure in annual reports on their lending activities or transactions for better transparency and accountability in how shareholders' funds have been utilised.

Money lenders

An issuer that reported money lending as a principal activity should disclose, at a minimum, the following:

- Description of business models, including the nature of lending services provided; customer profiles; risk management policies (including credit approval processes and credit risk assessment policies); and loan impairment policies.
- Breakdown of loan portfolios, including total outstanding loan receivables and number of borrowers; major terms of the loans (e.g. maturity profiles, interest rates, collaterals and/or guarantees obtained); breakdowns of loans by categories (e.g. types of borrowers, loan products or collaterals); size and diversity of borrowers (e.g. loans receivables from the five largest borrowers); and ageing analysis of the outstanding loans.
- Discussion of movements of impairments or write-offs of loan receivables and basis of impairment assessments, including assessments of impairments on material loans. The issuer should develop appropriate and supportable estimates to assess the recoverability of the loans to support the impairment assessments under the relevant accounting standards.

Non-money lenders

An issuer that engaged in money lending activities outside its ordinary and usual course of businesses should disclose the following:

- Details of loan receivables (including major terms).
- Discussion of any material impairments or write-offs of loan receivables and the basis of impairment assessments.
- Reasons for granting the loans and how they meet its business strategies.

Other reference materials on governance over lending transactions

- LRE Newsletter Issue 5 (December 2021) – "Directors' duties in assessing loans transactions"
- LRE Newsletter Issue 4 (May 2021) – "Guidance on lending transactions"
- Joint statement of the SFC and the Accounting and Financial Reporting Council in relation to loans, advances, prepayments and similar arrangements made by listed issuers (July 2023)
- The Exchange's Enforcement Bulletin (April 2024) – "Loans, advances and other similar arrangements"

2.5 Performance guarantees

10. In some acquisitions, the vendor might guarantee the performance of the acquired business and compensate the issuer for any shortfall from the guarantee. Under the Rules, an issuer is required to disclose in the annual report whether the actual performance of the acquired business meets the guarantee. If the guarantee is not met, the issuer is also required to disclose by announcement the shortfall; whether the vendor has fulfilled its obligation and the directors' opinion on the fairness of their decision to exercise (or not exercise) the issuer's rights under the terms of guarantee[10].

11. For better transparency and accountability, where the performance guarantee is not met, issuers are recommended to provide appropriate updates in annual reports about the actions the directors have taken so far, and intend to take. In the update, they should explain the directors' actions, in particular whether and how they are fair and reasonable and in the best interests of the shareholders.

Other reference materials on directors' duties in assessing transactions with terms involving performance guarantee

- LRE Newsletter Issue 5 (December 2021) – "Directors' responsibilities when assessing transactions"

[10] MB Rules 14.36B and 14A.63 / GEM Rules 19.36B and 20.61

2.6 Newly listed issuers

12. The IPO prospectus contains material information on the listing applicant's business, major shareholders, regulatory/industry environment, principal risks and other matters. After listing, issuers should disclose appropriate information in their annual reports to keep investors updated on the developments of major matters highlighted in the prospectus.

For example:

- Where there are material changes in circumstances as presented in the prospectus, such as material changes in financial performance and position, business environment and risks, business plans and use of IPO proceeds, the issuer should adequately discuss the changes and, if applicable, the directors' intended course of actions.
- Where the issuer was given non-competition undertakings by its major shareholders to establish a clear delineation between their businesses, the issuer should disclose whether such shareholders have fulfilled their undertakings.
- In some cases, the issuers might have undertaken (or required by the Listing Committee as a condition to listing) to take certain actions after listing (e.g. updating on latest regulatory developments and restrictions on use of IPO proceeds to finance or facilitate sanctioned activities). These issuers are expected to take appropriate actions to fulfill such undertaking (or condition) and make relevant disclosure in the annual reports.

Reference materials on profit warning / alert announcement

- SFC's Corporate Regulation Newsletters Issue 2 (April 2015) and Issue 4 (December 2016)

13. Specifically, in the MD&A section of their annual reports, newly listed issuers should present appropriate information and discussion to enable investors to evaluate whether the post-listing performance are in line with the track record, business plan and prospects outlined in the prospectus. **They should make reference to their IPO prospectuses in determining the appropriate level of information to be included in the MD&A section**. Please see section 2.2 on disclosure guidance on MD&A.

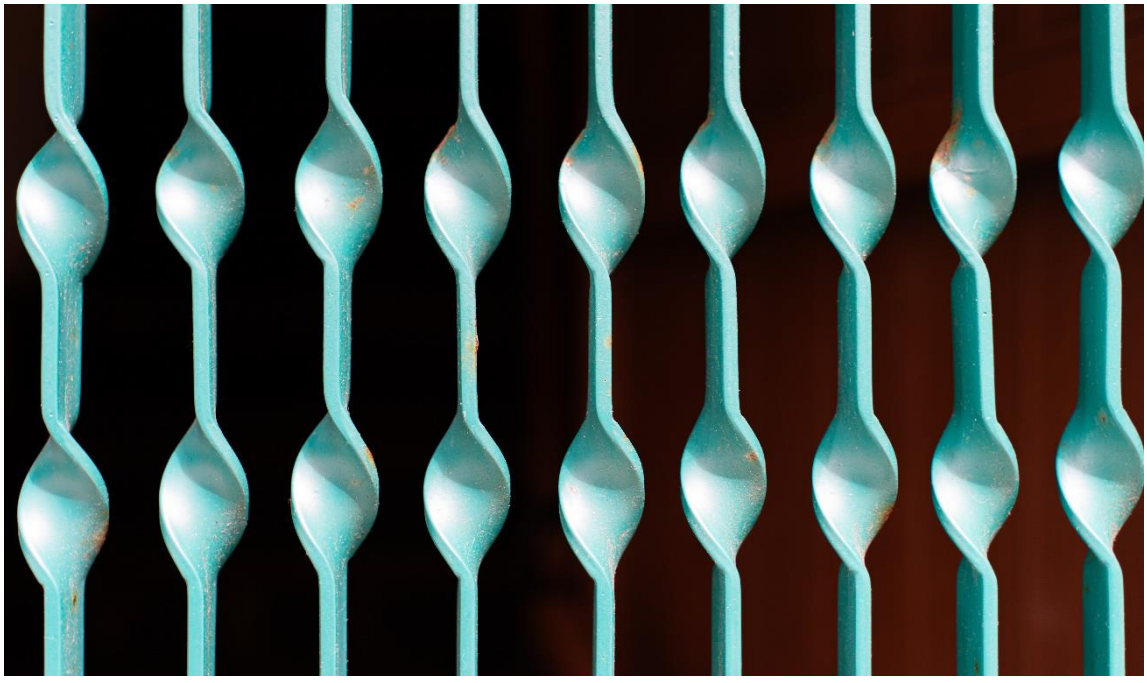
14. Before publication of annual report, newly listed issuers must consult their compliance advisers. They are encouraged to well utilise these compliance resources and seek guidance from the advisers on preparing annual reports and other compliance matters when necessary[11].

[11] Under MB Rule 3A.23 / GEM Rule 6A.23, a newly listed issuer must consult with and seek advice from its compliance adviser on a timely basis in the following circumstances (i) before the publication of any regulatory announcement, circular, or financial report; (ii) where a transaction, which might be a notifiable or connected transaction, is contemplated including share issues and share repurchases; (iii) where the issuer proposes to use the IPO proceeds in a manner different from that detailed in the listing document or where the business activities, developments or results of the issuer deviate from any forecast, estimate, or other information in the listing document; and (iv) where the Exchange makes an inquiry of the issuer under MB Rule 13.10 / GEM Rule 17.11.

2.7 Biotech companies under Chapter 18A of the MB Rules

15. A biotech company is required by the Rules to disclose in annual report the research and development status of its core products designated at the time of IPO[12]. To allow investors to have a more complete assessment of its drug/device portfolio as a whole and post-listing developments, a biotech company is recommended to also provide appropriate update and discussion on:

Non-core products at time of IPO	***Newly in-licensed or self-developed products after listing***
▪ Development stages ▪ Clinical trial status ▪ Regulatory approval status ▪ Post-commercialisation activities during the financial year, including revenue generated, details of commercialisation team, competition and marketing strategy, and market coverage, status of enrolment into insurance programme, and eligibility for government subsidies	Major developments, such as: ▪ progress to next stage of clinical trial ▪ progress to obtaining relevant regulatory approvals



[12] MB Rule 18A.08

3. Financial disclosure under prevailing requirements

1. Issuers should prepare the financial statements with a high standard of financial disclosure and ensure compliance with the applicable accounting standards[13].

2. Financial reporting, along with audit, plays a critical role in driving issuers' good corporate governance. Issuers and their audit committees must act proactively. They should ensure effective communication with their auditors about the audit plan, areas of audit focus and disclosure well in advance of the financial year-end and use their best endeavours to address the issues raised by the auditors in a timely manner. Doing so may minimise the possibility of last-minute surprises.

3. The table below highlights the common areas[14] requiring particular attention when preparing financial information in annual reports:

3.1 *Accounting policy information, judgements and estimates*

Materiality is a fundamental concept in financial reporting. HKFRS provide that: *"Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity."*

When preparing the financial statements, issuers should put in place a systematic process[15] in assessing whether the information is material for the purposes of recognition and measurement as well as presentation and disclosure. They should revisit the assessment in each year, by providing additional disclosure, removing immaterial information and reorganising existing disclosure (where appropriate).

Accounting policy information, judgements and estimates should focus on how issuers have applied the accounting requirements according to their own facts and circumstances, which are more useful to investors than the boilerplate description that solely duplicates or summarises the accounting requirements.

In particular, investors place more emphasis on the financial disclosure relating to those areas identified as key audit matters by the auditors (e.g. the application of accounting policies involved critical management judgements and estimates, the events or transactions occurred during the year that have had significant effects on the financial statements). Issuers should provide appropriate details for disclosure and develop robust interactions with their auditors.

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13 Notes 2.1 and 2.6 to paragraph 2 of Appendix D2 to the MB Rules / GEM Rules 18.04 and 18.06.

14 Unless otherwise specified, HKFRS Accounting Standards issued by the HKICPA (**HKFRS**) referred to in this section correspond to IFRS® Accounting Standards issued by the International Accounting Standards Board. The areas highlighted in this section are not exhaustive, readers should read the full HKFRS / IFRS Accounting Standards to understand the relevant requirements and implications.

15 Issuers are encouraged to read HKFRS Practice Statement 2 "Making Materiality Judgements", which provides non-mandatory guidance and examples in practice.

3.2 *Revenue*

Revenue is a key line item in the financial statements. Issuers should disclose sufficient qualitative and quantitative information to enable investors to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with their customers.

Clarity of disclosure can enhance the financial reporting integrity. Issuers are reminded of the following non-exhaustive areas:

- **Significant judgements** – where concluding the revenue recognition involves complex arrangements or significant judgements (e.g. whether a performance obligation is satisfied at a point in time or overtime; how to determine and allocate the transaction price; whether they are acting as a principal or an agent), the disclosure should clearly articulate the link between the issuers' own circumstances (e.g. specifics of their business model) and the accounting requirements.

- **Disaggregated revenue** – when selecting the appropriate type of categories, issuers should take into consideration: (i) how the revenue is presented outside the financial statements (e.g. MD&A); and (ii) whether such information should be included as part of the segment reporting, to enable investors to better understand how the revenue related to each reportable segment result and other information provided in the segment disclosure.

Recognising revenue often relies on IT systems and data inputs, issuers should therefore maintain effective and reliable internal controls to ensure their revenue figures are properly recorded and not misstated.

3.3 *Business combinations*

Issuers should disclose sufficient information to enable investors to evaluate the nature and financial effects of business combinations. The following are non-exhaustive examples for which greater clarity on disclosure is needed:

- Significant judgement is applied in determining whether the transaction is a business combination or an asset acquisition.

- Transaction involves complex arrangements (e.g. profit guarantee, derivative financial instrument, whether a contingent consideration obligation is a financial liability or an equity).

- Significant goodwill is recognised when the fair value of identifiable assets acquired is minimal.

- Significant gain on bargain purchase is recognised when the fair value of identifiable assets acquired is substantially higher than the consideration.

When entering into complex transactions, the boards and their management should have more in-depth discussion with their auditors and valuers at an early stage to consider the accounting implications in order to prevent any unintended accounting errors and regulatory consequences.

3.4 *Material intangible assets – impairment testing*

The cash-generating unit (**CGU**) containing goodwill and intangible assets with indefinite useful lives is required to perform an annual impairment test. Issuers should ensure that the valuation techniques, financial budgets and/or key assumptions used in the test are appropriate and reasonable, and not overly optimistic having regard to historical cash flows, available market information and future prospects.

When disclosing the required quantitative inputs (e.g. budget periods, discount rates and terminal growth rates) and qualitative information of the underlying key assumptions, issuers should pay attention to the level of detail of the disclosure. Boilerplate description (e.g. the values of key assumptions are based on *"past experience"* and *"external information sources"*) is not enough, issuers should further elaborate on how the projected cash flows link with the CGU's latest business development (e.g. the expected new product launch date).

The following additional information in the MD&A and financial statements (where appropriate) is recommended:

- Provide additional quantitative data of key assumptions (other than discount rate and terminal growth rate as required under accounting standards, e.g. gross and net margins), comparative information in the previous year and the explanation of significant changes to underlying assumptions.
- Provide a negative statement indicating that reasonably possible change in the key assumptions on which the management has based its determination of the CGU's recoverable amount would not cause an impairment loss.
- Provide the recoverable amount of the CGU and the headroom available.
- Highlight whether the impairment assessment is based on a valuation by an independent professional valuer.
- Provide details of further development of the CGU or segment, such as business plan and contracts with new customers in the coming year and their impact on the revenue and margins.

3.5 *Valuation of Level 3 financial assets*

Performing Level 3 valuation can be challenging. The following are non-exhaustive examples where issuers should revisit the valuation and enhance the clarity of disclosure:

- The projected cash flows, market multiples or discount for lack of marketability used in the valuation appear to be overly optimistic relative to the investee's historical performance and future prospects.
- The net asset value is determined solely based on the investee's management accounts without making any adjustments, in particular when the investee incurred a significant operating loss and has potential impairment on assets.

Directors are reminded of their fiduciary duties and duties of skill, care and diligence under MB Rule 3.08 (GEM Rule 5.01) that they must exercise their own judgement[16] to assess the reasonableness of the valuation techniques and underlying unobservable inputs and should not overly rely on valuers. They should obtain sufficient and timely information from investees (such as latest financial data, updates on operations and business plans, recent share transactions) for measuring fair values and provide robust disclosure on Level 3 measurement.

3.6 *Credit risk disclosure on trade receivables*

HKFRS disclosure requirements on the credit risk and expected credit losses (**ECL**) assessment are more objective-based. Issuers should carefully consider their circumstances and determine: (i) how much detail to disclose; (ii) how much emphasis to place on different aspects of the disclosure requirements; (iii) the appropriate level of aggregation or disaggregation; and (iv) whether shareholders and investors need additional explanations to evaluate the quantitative information disclosed.

Issuers normally provide more extensive quantitative disclosure, including: (i) percentages of the balances concentrated in the largest customer and top five customers; (ii) balances that are credit-impaired and assessed individually; and (iii) loss rates and/or provision matrices (e.g. by past due status) on the balances assessed collectively.

They should pay more attention to the qualitative disclosure. For example, they should clearly explain the reasons where there is a significant change in the loss rates from the previous year, instead of simply stating *"the current loss rates are calculated based on the historical loss rates and adjusted to reflect current and forward-looking information"*.

It is important for issuers to put in place appropriate systems and assessment processes to measure the ECL, including reconsidering the appropriateness of the methods adopted and using up-to-date inputs (e.g. debtors' creditworthiness) at each reporting date.

3.7 *Presentation of non-GAAP measures*

Issuers should follow our guidance GL103-19 when non-GAAP measures are used as a complement to GAAP financial information in the annual report. They should take a holistic approach to ensure non-GAAP measures present a fair and balanced view of the performance, position and cash flow and are not misleading. The audit committees, as gatekeepers, should monitor the integrity of non-GAAP disclosure.

Key considerations when presenting non-GAAP measures:

- **Definitions** – non-GAAP measures should be defined (by reflecting their composition) and explained the basis of calculation. They should be appropriately labeled (e.g. *"adjusted net profit (non-GAAP measure)"*) to distinguish from GAAP measures.

[16] SFC's guidance note on directors' duties in the context of valuations in corporate transactions (May 2017) and statement on the conduct and duties of directors when considering corporate acquisitions or disposals (July 2019)

- **Reasons for presenting non-GAAP measures** – issuers should justify why the information is useful and provides additional value to investors (e.g. non-GAAP measures are commonly used in their industries or peers).

- **Prominence** – issuers should ensure prominence of GAAP measures over non-GAAP measures (e.g. GAAP loss for the year should be presented immediately before *"adjusted net loss (non-GAAP measure)"*).

- **Reconciliation and nature of adjustments** – the quantitative reconciliation should begin with GAAP measures and be reconciled to non-GAAP measures with reconciling items derived from the financial statements reported in GAAP (when a reconciling item cannot be extracted directly from the financial statements, show how this figure is calculated). Issuers should explain the nature of each adjusting item and remove any adjusting item which is considered as normal, recurring, cash operating expenses necessary to their business operations (e.g. impairment of trade receivables relating to issuers' normal businesses).

- **Comparatives** – issuers should consistently present non-GAAP measures for comparative periods.

3.8 *Disclosure of possible impact of applying a new or amended standard in issue but not yet effective*

Issuers should stay alert to the changes and developments in accounting standards. Implementation of new standards is not just an accounting exercise, but is expected to have a significant impact on some issuers, particularly on their business processes, IT systems and internal controls. Issuers should carefully assess the impact and develop a detailed action plan.

HKFRS require issuers to disclose the possible impact of new or amended standard. Generic disclosure (such as *"currently assessing the possible impact of the new standard"*) repeated in each year appears to indicate a lack of readiness for implementation. Disclosure should be timely and progressively to provide more entity-specific information, including but not limited to:

- The fact that issuers have substantially completed their implementation analyses and the stage of implementation they are at.

- The accounting policy options (if available) expected to be applied, including those relating to the transition approach and the use of practical expedients.

- The amount and nature of the expected impact on financial statement line items affected.

To avoid unintended errors due to inappropriate application of new standards, issuers are encouraged to early consult their auditors. In particular, they should consider whether it is necessary to engage their auditors to perform a review of their interim financial statements in the period of initial application.

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Guidance for issuers subject to market commentaries or rumours

I. Background and purpose

1. The Exchange is the front-line regulator of listed issuers. It has a statutory obligation under the Securities and Futures Ordinance (**SFO**) to ensure, so far as reasonably practicable, an orderly, informed and fair market in the trading of securities.

2. In recent years some listed issuers have, from time to time, become subjects of market commentaries or rumours with allegations of fraud, material accounting or corporate governance irregularities (together **allegations**). These allegations were made by market commentators or research firms, and have caused or could have caused intense price pressure in the issuer's listed securities.

3. This letter provides guidance to issuers subject to these allegations and their obligations in handling such matters. Listed issuers should announce information to clarify matters where, in the view of the Exchange, there is a possible development of a false or disorderly market in its securities. Listed issuers should always maintain appropriate and effective risk management and internal control systems to safeguard their assets and monitor their operations.

4. Listed issuers may refer to the "Guidelines on Disclosure of Inside Information" published by the Securities and Future Commission (**SFC**) for guidance on discharging their obligations to announce inside information under Part XIVA of the SFO, and to the Exchange's Guidance Letter (GL83-15) for principles and best practices in applying for trading halts.

II. Issuer's action

To address false or disorderly market concerns

5. Where there are allegations circulating in the market regarding an issuer, the Exchange may be concerned that the allegations may disrupt orderly share trading. Under these circumstances the Exchange may make an enquiry under MB Rule 13.10 / GEM Rule 17.11.

6. If the allegations have, or are likely to have, an effect on the issuer's share price such that, in the view of the Exchange, there is or there is likely to be a false or disorderly market in the listed issuer's securities, the issuer must make a clarification announcement promptly. The issuer must apply for a trading halt if it cannot promptly publish the clarification announcement to prevent the possible development of a false or disorderly market.

7. The duration of any trading halt should be for the shortest possible period. If trading is halted, the issuer must ensure trading resume as soon as practicable following publication of a clarification announcement (MB Rule 6.05 / GEM Rule 9.09).

8. The clarification announcement serves to inform the market. It should make reference to the allegations and inform the market about the issuer's position regarding each allegation so as to avoid a false or disorderly market. To the extent possible, the clarification announcement should also contain particulars to address, or to refute, the allegations. The issuer should also disclose any inside information required to be disclosed under Part XIVA of the SFO where applicable, or an appropriate negative statement.

9. The Exchange would not normally pre-vet the clarification announcement and would expect such announcement to be made as soon as practicable by the issuer such that the duration of any necessary trading halt is kept to the minimum. For the avoidance of doubt, the issuer has an obligation to issue a clarification announcement to prevent the possible development of a false or disorderly market. This obligation exists whether or not the Exchange makes enquiries under MB Rule 13.10 / GEM Rule 17.11.

10. Save for exceptional circumstances, the Exchange would expect share trading to resume (if it was halted) following publication of a clarification announcement. If the Exchange believes that the announcement would not address the concerns on false or disorderly market, it may require the issuer to provide further information and halt trading pending further clarification. This may be the case where, for example, the clarification announcement contains information materially inconsistent with its other published documents, or contains information which creates market confusion so as to raise the Exchange's concerns about the possible development of a false or disorderly market in the trading of the shares.

Continuing reviews or investigations

11. Following publication of the clarification announcement, the Exchange may continue to follow up with the issuer on any further disclosures, reviews or investigations it considers necessary on matters that have arisen out of the allegations. Depending on the nature, gravity and creditability of the allegations, the Exchange may require the issuer to provide further information to support its denials of allegations, to review or conduct investigations into the claims and documents purportedly reviewed or used to support the allegations.

12. The Exchange takes follow up action to require an issuer to demonstrate that its responses to allegations are supported and the basis for that support and that it has in place internal controls and risk management measures to safeguard its assets, and financial and reporting controls to promote reporting that is timely and materially accurate. Where appropriate, the issuer is expected to identify and correct any weaknesses in its internal controls, and adopt good corporate governance practices to address the inconsistent information identified in the allegations.

13. In the absence of a material development that raises concerns about trading in an orderly manner, the Exchange's follow up action should normally not affect the trading of the issuer's securities.

14. Where the follow up action reveals that any issuer announcement or document was materially inaccurate or misleading, or that there are serious concerns about the issuer's compliance with the Rules, the Exchange may suspend the issuer's share trading pending further clarification. Where appropriate, the Exchange may make a referral to an appropriate law enforcement agency (e.g. the SFC) for consideration of action under the law (e.g. the SFO).

Whether the Exchange would grant listing approval for a placing of new shares if there was a leakage of inside information before the announcement of the placing

Facts

1. On Day 1, the price and trading volume of the shares of a listed issuer (**Company A**) started to increase. Such increase continued until Day 7. On Day 4, the increase in the share price intensified and the Exchange contacted a director of Company A enquiring into the reasons for such increase. The Exchange was advised by Company A that there was no information that ought to be released pursuant to Rule 13.09 or Rule 13.23. Accordingly a standard announcement pursuant to Rule 13.10 was released on the Exchange's teletext system on Day 5.

2. After trading hours on Day 6, the Exchange was informed by a financial adviser on behalf of Company A that Company A had concluded a placing agreement for the issue of new shares in Company A.

Analysis

3. Upon enquiry, Company A admitted that it had on Day 2 appointed a consultant to identify on a "no name" basis a suitable brokerage firm which would be interested in arranging a share placing for Company A. The instructions to the consultant were still open on Day 4 and Day 5 when Company A released its standard Rule 13.10 announcement.

4. Company A reiterated that it was not aware of the reasons for the increase in the price and trading volume of Company A's shares during the period from Day 1 to Day 6. Company A considered that the issue of the standard Rule 13.10 announcement was appropriate on Day 4 and Day 5 as Company A had not commenced any negotiations for a placing with any agent on or before Day 4 and a premature announcement at that stage might have led to unnecessary speculation in Company A's shares.

5. It appeared, however, that Company A or its advisers had permitted price-sensitive information regarding the proposed issue of new securities to leak out onto the market prior to its proper publication and certain people had acted upon this information and traded in Company A's shares.

Conclusion

6. Pursuant to paragraph 5 of Practice Note 11, the Exchange decided not to approve Company A's application for the listing of the placing shares.

Continuing obligations

General disclosure obligation

1. What is a "false market"?

The term "*false market*" refers to a situation where there is material misinformation or materially incomplete information in the market which is compromising proper price discovery. This may arise, for example, where:

(a) a listed issuer has made a false or misleading announcement;

(b) there is other false or misleading information, including a false rumour, circulating in the market;

(c) a listed issuer has inside information that needs to be disclosed under the Inside Information Provisions but it has not announced the information (e.g. the listed issuer signed a material contract during trading hours but has not announced the information); or

(d) a segment of the market is trading on the basis of inside information that is not available to the market as a whole.

Where a media or analyst report appears to contain information from a credible source (whether that information is accurate or not) and:

(a) there is a material change in the market price or trading volume of the listed issuer's securities which appears to be referrable to the report (in the sense that it is not readily explicable by any other event or circumstance); or

(b) if the market is not trading at the time but the report is of a character that when the market starts trading, it is likely to have a material effect on the market price or trading volume of the listed issuer's securities,

the listed issuer must announce information necessary to avoid a false market in its listed securities.

MB Rules 13.09(1), 13.10, 37.46A, 37.47(b), para 3 of PN11, App E4 and E5 – 1(1)(a), App E4 – 27 and App E5 – 26
GEM Rules 17.10(1), 17.11, 30.39A, 30.40(b), 31.04(2) and 31.05
First released: April 2013; last updated: May 2024

2. What is the meaning of the term "such enquiry with respect to the issuer as may be reasonable in the circumstances"? What sort of enquiry is a listed issuer required to make in response to the Exchange's enquiries? When will a listed issuer be expected to contact its controlling shareholders when they are not directors or officers of the listed issuer?

The facts and circumstances giving rise to each enquiry are different. Therefore, what enquiry is reasonable depends on the circumstances, and there are no hard and fast rules. The test is one of reasonableness.

To facilitate compliance, it is crucial that a listed issuer implements and maintains adequate and effective internal control systems and procedures to ensure material information concerning the listed issuer and its business would be promptly identified, assessed and escalated to the Board for consideration and action from a Rule compliance perspective. This would require a timely and structured flow to the Board of information arising from the development or occurrence of events and circumstances so that the Board can decide whether disclosure is necessary.

A listed issuer is generally not expected to contact (a) its controlling shareholders when they are not directors or officers of the listed issuer, or (b) counterparties to a transaction, except if there is information available to the listed issuer suggesting that the subject matter of the enquiry is related to the controlling shareholders or the counterparties to a transaction. For example, the listed issuer is aware of its controlling shareholder's plan to dispose of its interest in the listed issuer, and there is an unusual increase in the trading volume of the listed issuer's shares. Another example is where there are press articles suggesting that the counterparty to a disclosed transaction may not be able to complete the transaction as a result of difficulties in obtaining financing.

MB Rules 13.10(2), 37.46A(b), App E4 - 27(2), App E5 - 26(2)
GEM Rules 17.11(2), 30.39A(b) and *31.05(2)*
First released: April 2013; last updated: May 2024

3. A listed issuer has inside information which is exempted from disclosure under one or more of the safe harbours in the Inside Information Provisions. If there are market rumours which are unrelated to this information, but have resulted in unusual trading movements, does the listed issuer need to publish a standard announcement?

If the standard announcement states that there is no inside information that needs to be disclosed under the Inside Information Provisions, but the listed issuer subsequently discloses the information, say a month later, will this result in market uncertainty?

Whether an announcement is required to be issued under these provisions depends on the facts and circumstances of the matter. It is only if and when requested by the Exchange that an announcement needs to be issued.

Information that is exempted from disclosure under the Inside Information Provisions does not fall within the term "any inside information that needs to be disclosed under Part XIVA of the Securities and Futures Ordinance" contained in the standard announcement. Therefore, a standard announcement issued under those circumstances will not be inaccurate.

To avoid market uncertainty arising from the subsequent disclosure of the inside information previously exempted from disclosure, the listed issuer can clarify in the disclosure announcement that the information was exempted from disclosure when the standard announcement was issued.

MB Rules 13.10(2), 37.46A(b), App E4 - 27(2), App E5 - 26(2)
GEM Rules 17.11(2), 30.39A(b) and 31.05(2)
First released: April 2013; last updated: May 2024

3A. A listed issuer plans to publish a profit warning or alert announcement to inform the market of an expected change in the net profit or loss of its group for the current year or interim period. Should the issuer also disclose the expected change in the "profit or loss attributable to shareholders"?

The issuer should observe the general disclosure principle in MB Rule 2.13 / GEM Rule 17.56.

Where profit or loss figures are disclosed, the mere disclosure of the expected profit or loss for a financial period or the expected changes in profit or loss across the reporting periods might be confusing or misleading in some circumstances, for example, where the issuer expects to record a profit for the financial period but a loss attributable to shareholders, or where the profit or loss attributable to shareholders are expected to change in the opposite direction as compared to the trend shown by the profit or loss for the financial period. In such circumstances, the issuer should also consider disclosing information on the expected profit or loss attributable to shareholders as this would provide a clearer picture of the impact on the shareholders' interests in the issuer by excluding the portion attributable to other entities.

In addition, issuers are also reminded to observe the principle on timely disclosure of material information under MB Rule 2.03 and 13.09(1) / GEM Rules 2.06 and 17.10(1) and publish announcement to inform the market as soon as they become aware of events or factors that may materially affect their financial performance, regardless of whether specific profit or loss figures for the financial period are available.

Issuers should also refer to the SFC's Corporate Regulation Newsletters Issue 1 (July 2014), Issue 2 (April 2015) and Issue 4 (December 2016) for further guidance on disclosure in profit warning / alert announcements.

MB Rules 2.03, 2.13 and 13.09(1)
GEM Rules 2.06, 17.10(1) and 17.56
First released: December 2024

Overseas regulatory announcement

4. A PRC issuer whose H shares are listed on the Exchange will issue a prospectus in the PRC in connection with its proposed issue of A shares. Is the PRC issuer required to publish the A-share prospectus on the Exchange's website if it has announced all inside information identified during preparation of the prospectus or as a consequence of other development?

Yes. The PRC issuer should publish the A-share prospectus on the Exchange's website in the form of an overseas regulatory announcement at the same time as it is released in other market(s).

MB Rules 13.09(2) and 13.10B
GEM Rules 17.10(2) and 17.12
First released: November 2008; last updated: May 2024

Advance to an entity

5. How should the assets ratio for an advance to an entity be calculated?

The assets ratio should be calculated in the same manner as a provision of financial assistance pursuant to MB Rule 14.12 / GEM Rule 19.12.

MB Rules 13.13, 13.14, 13.16 and 14.12
GEM Rules 17.15, 17.16, 17.18 and 19.12
First released: March 2004; last updated: May 2024

Pledge of shares by controlling shareholder

6. Does the announcement requirement under MB Rule 13.17 / GEM Rule 17.19 apply if the controlling shareholder of a listed issuer deposited the share certificate of its shares in the listed issuer to a third party, or used its interest in the listed issuer's shares for the purpose of securing the listed issuer's performance of an obligation?

Yes. MB Rule 13.17 / GEM Rule 17.19 applies to any arrangement, in any form and however the arrangement is named, where the controlling shareholder effectively uses all or part of its interest in the listed issuer's shares to, directly or indirectly, secure the listed issuer's debts, or to secure guarantees or other support of the listed issuer's obligations.

MB Rule 13.17
GEM Rule 17.19
First released: May 2018; last updated: May 2024

Next day disclosure return and monthly return

7. A listed issuer published a next day disclosure return upon a repurchase or redemption of shares. Is it required to publish another next day disclosure return upon cancellation of those shares?

No. However, the number of shares cancelled and the date(s) of cancellation should be disclosed in the subsequent monthly return or next day disclosure return published for any other event (whichever is earlier).

MB Rule 13.25A(2)(a)(vii)
GEM Rule 17.27A(2)(a)(vii)
First released: November 2008; last updated: May 2024

Dividend distribution

8. When an A+H issuer proposes a corporate action (e.g. distribution of dividends or other entitlements), does it need to disclose the timetables for both A and H shareholders in the same announcement?

Yes. The listed issuers should ensure clear communications to all shareholders if they propose different timetables (e.g. ex-entitlement date, record date and payment date) for their distributions to shareholders in the two markets.

MB Rules 13.45(1) to (3) and 13.66
GEM Rule: N/A
First released: November 2014; last updated: May 2024

Vote of shareholders at general meeting

9. MB Rule 13.39(4) / GEM Rule 17.47(4) allows a resolution which relates purely to a procedural to administrative matter to be voted on by a show of hands. Are there any examples of procedural and administrative matters?

Procedural and administrative matters include, for example, adjourning a meeting by resolution to:

(a) ensure orderly conduct of the meeting (e.g. if the meeting facilities to house the number of members attending has become inadequate); or

(b) maintain the orderliness of the meeting, e.g. if it becomes impossible to ascertain the views of the members, or there is disorder or threat of disorder from members or if there is a disturbance caused by members or the uninvited public; or

(c) respond to an emergency such as a fire, a serious accident or hoisting of tropical cyclone warning signal No. 8 during a meeting; or

(d) announce results at the end of the annual general meeting.

Note to MB Rule 13.39(4)
Note to GEM Rule 17.47(4)
First released: December 2011; last updated: May 2024

Board meeting

10. A listed issuer has published an announcement on the board meeting date to approve its annual results 7 clear business days before the board meeting. If the listed issuer subsequently decides to postpone the board meeting to a later date, is it required to give another 7 day notice?

Subject to its articles of association, the listed issuer does not need to give another 7-day notice. However, it should, as soon as practicable, announce the postponement of board meeting and the revised board meeting date.

MB Rule 13.43
GEM Rule 17.48
First released: December 2011; last updated: May 2024

Directors' service contracts

11. Is a director's service contract subject to shareholders' approval under MB Rule 13.68 / GEM Rule 17.90 if it does not have a fixed term and is terminable by either party by giving notice of 6 months?

The purpose of the Rule is to ensure that the listed issuer is not unduly burdened by service contracts that are for an inordinate length or which require heavy compensation or lengthy notice for early termination. Such contingent liabilities may be significant, in which case, shareholders' approval must be obtained for these service contracts. As the service contract do not have a specific term and only six-month notice is required for termination, there is no significant commitment on the listed issuer. Therefore, no shareholders' approval is required.

MB Rule 13.68
GEM Rule 17.90
First released: March 2004; last updated: May 2024

Publication of constitutional documents

12. Can listed issuers publish their constitutional documents in a single language (i.e. English or Chinese only)?

No, the constitutional documents must be published in both English and Chinese.

MB Rule 13.90
GEM Rule 17.102
First released: December 2011; last updated: May 2024

13. If a listed issuer has amended its constitutional document (memorandum and articles of association, bye-laws or other equivalent constitutional document) many times over the years since its incorporation, is it required to post to the Exchange website its documents incorporating all the previous amendments?

The listed issuer is required to publish a consolidated version of the constitutional document which has incorporated all the changes. This may be a conformed copy or a consolidated version not formally adopted by shareholders at a general meeting. However, if the listed issuer does so, the front page of the published constitutional document should include a statement that it is a conformed copy or a consolidated version not formally adopted by shareholders at a general meeting.

MB Rule 13.90
GEM Rule 17.102
First released: December 2011; last updated: May 2024

Submission of documents

14. How should documents be submitted to the Exchange by electronic means under the paperless regime?

The Exchange will establish a new online platform (**Issuer Platform**) as a designated channel for two-way communication between the Listing Division and new applicants/ listed issuers (except for structured products issuers). New applicants/ listed issuers and their professional parties will be able to use this platform to submit all documents and e-Forms to the Division electronically. The Exchange will update the market prior to the launch of the Issuer Platform, with necessary guidance.

Until that time, new applicants and listed issuers (and their advisors) should continue to submit documents to the Listing Division through the existing permitted electronic means (e.g. by email or via HKEX-ESS).

Structured products issuers should continue to submit documents to the Listing Division by email or via the "SPRINTS" platform

MB Rule 2.07(3A)
GEM Rule 2.21
First released: December 2023; last updated: May 2024

15. Is digital signature required for documents electronically submitted to the Exchange that require signature?

No, except for documents that are to be electronically submitted to the Exchange for the purpose of authorisation of prospectus registration under the Companies (Winding Up and Miscellaneous Provisions) Ordinance.

MB Rules 1.02A and 2.07(3A)
GEM Rules 1.03A and 2.21
First released: December 2023; last updated: May 2024

Electronic dissemination of corporate communications

16. Are listed issuers required to notify their securities holders of the new mandatory requirement for electronic dissemination of corporate communications?

Before a listed issuer adopts any new arrangements on dissemination of corporate communications (e.g. transitioning from physical copy to electronic dissemination, or adopting a different consent mechanism for electronic dissemination), it should send a one-time notification to its securities holders individually, in hard copy or electronically[1], to: (a) inform them of the new arrangements (including how securities holders may make requests for hard copy corporate communications under the new arrangements) and (b) solicit their electronic contact details. Listed issuers should use best efforts to follow-up on this solicitation of electronic contact details by, for example, sending periodic reminders to securities holders asking them to provide their electronic contact details if they have not done so.

[1] in case where the holder has previously agreed to be notified by a particular electronic means

Also, all listed issuers must disclose on their websites (e.g. in the investor relations section), on an ongoing basis, the relevant arrangements for the electronic dissemination of their corporate communications (including the arrangements by which holders can make hardcopy requests). This will enable new securities holders (who only become securities holders of the listed issuer after the implementation of any new arrangements and have not received the abovementioned one-time notification) to understand the relevant arrangements in place.

Listed issuers are expected to clearly inform securities holders of the purpose of obtaining their electronic contact details when soliciting them from the holders (e.g. that the listed issuer will be using the electronic contact details to send actionable corporate communications). Listed issuers should also draw their securities holders' attention to the consequence of providing non-functional electronic contact details.

MB Rule 2.07A
GEM Rule 16.04A
First released: December 2023; last updated: May 2024

17. Can securities holders make requests for hard copies of corporate communications?

What measures should a listed issuer put in place to ensure that securities holders wishing to request hard copy corporate communications are properly informed of how they can do so?

Yes.

A listed issuer must send corporate communications in printed form to a securities holder upon the request of a holder. Where a listed issuer receives instructions indicating a securities holder's preference to receive hard copies of the listed issuer's corporate communications (or refusal to receive them by electronic means), such instructions should be regarded as a request for hard copy unless such instructions have been revoked, have been superseded or have expired.

Please refer to Question 16 for the measures a listed issuer should put in place to ensure that securities holders wishing to request hard copy corporate communications are properly informed of how they can do so.

MB Rules 2.07A(4)
GEM Rule 16.04A(4)
First released: December 2023; last updated: May 2024

18. Can a request for hard copy corporate communications be valid for a specified period or must securities holders make a separate request for each and every corporate communication?

Listed issuers may devise their own arrangements on how hardcopy requests are made and handled. However, listed issuers should not make the process so unduly burdensome or oppressive that it negatively prejudices the interests of their securities holders.

For example, the Exchange would view an arrangement whereby securities holders are required to request hard copies on a per document basis as unduly burdensome for securities holders and listed issuers should not adopt such arrangements.
Equally, a one-time request from a securities holder for corporate communications in hard copy should not be valid indefinitely.

We would view an arrangement whereby a request for hard copy corporate communications was valid for a fixed period (e.g. one year) as reasonable. Any such request should be valid until the instructions have been revoked, have been superseded or have expired.

MB Rule 2.07A(4)
GEM Rule 16.04A(4)
First released: December 2023; last updated: May 2024

19. Are listed issuers required to amend their constitutional documents in light of the new electronic dissemination rules under the expanded paperless listing regime?

No. A listed issuer is required to amend its constitutional documents only if its constitutional documents contain any provision which restricts its ability to disseminate its corporate communications electronically (e.g. any provision that mandates hardcopy dissemination as the only means of dissemination of corporate communications). If such a restriction is due to a requirement under the applicable laws and regulations the listed issuer is subject to, the listed issuer will be required to amend its constitutional documents to facilitate its compliance with the relevant Listing Rules, if and when, the relevant restriction is removed from the applicable laws and regulations.

MB Rule 2.07A(4)
GEM Rule 16.04A(4)
First released: December 2023; last updated: May 2024

20. Must listed issuers continue to send corporate communications by airmail to securities holders with a contact address outside Hong Kong?

The requirement of MB Rule 13.76 on the use of airmail for communications sent across national borders continues to apply to communications and documents that are sent in hardcopy (e.g. a cheque refund).

MB Rules 2.07A, 13.76
GEM Rule: N/A
First released: December 2023; last updated: May 2024

21. What constitutes an "electronic form" of corporate communication? Is SMS or other electronic messaging systems accepted as a means to disseminate corporate communications electronically?

Generally, the Exchange would view any communication that is supplied in the form of a record generated in digital form by an information system, that can be transmitted and stored, as being in "electronic form".

The interpretation used in Companies (Winding Up and Miscellaneous Provisions) Ordinance as to how documents or information is considered to be sent or supplied in electronic form is a useful reference in this regard.

The Exchange does not prescribe detailed requirements on this matter and issuers have the flexibility to devise their own arrangements based on their own circumstances.

MB Rule 2.07A
GEM Rule 16.04A
First released: December 2023; last updated: May 2024

22. What should listed issuers do if they try to send corporate communications to individual securities holders electronically but find that the electronic contact details provided to them by a securities holder are non-functional?

The Exchange will not hold listed issuers responsible for failed electronic communications that are due to non-functional electronic contact details provided to them by securities holders.

However, listed issuers are expected to take appropriate steps to minimise the chance of unsuccessful electronic communication (e.g. by drawing the securities holders' attention to the risk of providing non-functional electronic contact details; reminding securities holders to use legible handwriting if they are filling in the relevant contact details in a paper form; or requiring securities holders to input the relevant contact details twice if an electronic form is used, etc.).

The Exchange will consider a listed issuer to have complied with its obligations if the listed issuer has used reasonable efforts to contact a securities holder using the electronic contact details provided. In general, a listed issuer is considered to have complied with the requirements if it sends corporate communications to the electronic contact details provided by the securities holders without receiving any "non-delivery message".

If a listed issuer has attempted to send a corporate communication electronically and received a non-delivery message, the listed issuer should re-send the corporate communication using other contact details provided by the securities holder (if any) in the manner the listed issuer considers appropriate (e.g. in hard copy). In the case of actionable corporate communications, the listed issuer must send the actionable corporate communication in printed form that includes a request for the holder's functional electronic contact details for the purpose of its future compliance with the Listing Rules.

Note 3 to MB Rule 2.07A
Note 3 to GEM Rule 16.04A
First released: December 2023; last updated: May 2024

23. What constitutes "actionable corporate communications"?

An "actionable corporate communication" is any corporate communication that seeks instructions from listed issuer's securities holders on how they wish to exercise their rights or make an election as the listed issuer's securities holder.

The list of items that the Exchange considers to fall within "actionable corporate communications" are as follows:

a) Election forms in connection with a dividend payment (e.g. choice of scrip or cash dividend, currency) (Note 1);
b) Excess application forms in connection with a rights issue or open offer;
c) Application forms for assured entitlement under an open offer;
d) Blue application forms for a preferential offering;
e) Pink application forms for employee reserved shares;
f) Acceptance forms in connection with takeovers, mergers and share buy-backs (including acceptance forms in general offers and acceptance and approval form in partial offers); and
g) Provisional allotment letters in connection with a rights issue (Note 2).

The Exchange does not consider notices of general meetings and proxy forms to be actionable corporate communications. Notices of general meetings only serve to inform securities holders of an upcoming general meeting and securities holders are not required to respond to such notices with their instructions. Holders wishing to appoint a proxy to attend a general meeting on their behalf can download the proxy forms from the Exchange's or the listed issuer's website for completion.

Similarly, the Exchange does not consider any form that is designed for securities holders to amend (i) their previously provided information or preference; or (ii) any default preference that is pre-selected by the listed issuer pursuant to its policy (e.g. a form to change communication language preference, a form to change their address, or a form to change default currency option for receiving dividends etc.) to be actionable corporate communications. This includes forms designed for securities holders to amend information they have provided in response to an actionable corporate communication.

Securities holders who wish to be notified of corporate communications that are not actionable corporate communications may subscribe for electronic alerts, such as the News Alert service on HKEX website, to receive instant notification of listed issuers' announcements.

Notes:

1. *In relation to election forms in connection with a dividend payment, please also refer to the Guide on Distribution of Dividends and Other Entitlements (Section 6: Entitlement with election(s)).*

2. *In relation to provisional allotment letters in connection with a rights issue, such letters are a form of temporary documents of title and must be despatched in printed form to securities holders in accordance with paragraph 2 of Appendix B1 of the MB Rules (paragraph 2 of Appendix B1 of the GEM Rules).*

MB Rule 1.01, App B1 - 2
GEM Rule 1.01, App B1 - 2
First released: December 2023; last updated: May 2024

24. The deemed consent mechanism has been removed from the Listing Rules, does that mean listed issuers are no longer permitted to rely on that mechanism?

A listed issuer is able to use the consent mechanism of its choice for disseminating corporate communications electronically provided that the chosen mechanism is permissible under the laws and regulations applicable to it.

This means that a listed issuer may adopt an electronic dissemination method consistent with the deemed consent mechanism previously provided by the Listing Rules if it wishes to do so.

MB Rule 2.07A(2A)
GEM Rule 16.04A(2A)
First released: December 2023; last updated: May 2024

25. How do the requirements on the electronic dissemination of corporate communications apply to beneficial holders of securities held in CCASS?

The Listing Rule requirements on electronic dissemination of corporate communications do not apply to the manner in which corporate communications are disseminated by intermediaries to beneficial holders of securities held in CCASS (with the exception set out in the next paragraph). The mode of delivery of corporate communications between these intermediaries and these beneficial holders is governed by the terms agreed between them.

However, "Non Registered Holders" (as defined by the Listing Rules) can notify a listed issuer, through HKSCC, that they wish to receive corporate communications pursuant to the Listing Rules. Listed issuers remain responsible for disseminating corporate communications to such Non-Registered Holders in the same way as to Registered Holders in accordance with the Listing Rules under the expanded paperless regime, and should send the one-time notification referred to in Question 16 above to Non Registered Holders individually under the circumstances specified in that question.

MB Rule 13.56
GEM Rule 17.60
First released: December 2023; last updated: May 2024

26. How should a Hong Kong incorporated listed issuer disseminate corporate communications to its securities holders under the new electronic dissemination rules under the expanded paperless listing regime?

Under the existing Hong Kong company laws, Hong Kong incorporated listed issuers are not able to rely on an implied consent from securities holders for electronic dissemination of corporate communications. They should take steps to obtain express or deemed consent to electronic communications under these laws, and should disseminate corporate communications in hard copy if such express or deemed consent has not been given.

MB Rule 2.07A(1)
GEM Rule 16.04A(1)
First released: December 2023; last updated: May 2024

27. Are listed issuers required to notify securities holders when they publish a corporate communication on their website / the Exchange's website?

No, except where the listed issuer is disseminating an actionable corporate communication, which must be sent to securities holders individually.

As mentioned in Question 23 above, securities holders who wish to be notified of corporate communications may subscribe to electronic alerts, such as the free News Alert service on HKEX website.

MB Rule 2.07A(4)
GEM Rule 16.04A(4)
First released: December 2023; last updated: May 2024

28. Are listed issuers required to put in place mechanisms to receive electronic instructions from securities holders in response to actionable corporate communications?

The Listing Rules do not prescribe how a securities holder must respond to actionable corporate communications they receive from a listed issuer. Similarly, the Listing Rules do not prescribe the mechanism that a listed issuer must put in place to receive instructions from securities holders in response to actionable corporate communications. This mechanism could be, for example, a designated email box, an electronic online platform or hardcopy by post.

MB Rule 2.07A(4)
GEM Rule 16.04A(4)
First released: December 2023; last updated: May 2024

11

Notifiable transactions

11.1 Backdoor listings

Guidance letter – Guidance on application of the reverse takeover Rules	GL104-19	11.1 – 1
Guidance letter – Guidance on large scale issues of securities	GL105-19	11.1 – 32
Guidance letter – Guidance to issuers contemplating (i) a spin-off and separate listing of businesses or assets on the Exchange; or (ii) a reverse takeover where the issuer is deemed a new listing applicant	GL69-13	11.1 – 37

11.2 Definition of transactions and calculation of percentage ratios

Listing decision – Whether the payment of a deposit by a listed issuer under an escrow agreement was a major transaction	LD93-1	11.2 – 1
Listing decision – Whether the on-market share repurchase by a listed subsidiary was a transaction for the listed parent, and if so, whether it would be aggregated with the listed parent's previous acquisition of shares in the subsidiary	LD5-2011	11.2 – 3
Listing decision – Whether a listed issuer was required to classify its subscription for a convertible note issued by a third party as if the notes were fully converted at the time of entering into the subscription agreement	LD55-2013	11.2 – 5
Listing decision – In respect of a placing and top-up subscription proposed by a listed subsidiary, whether the listed parent was allowed to calculate the percentage ratios for its disposal and acquisition of interests in the subsidiary on a net basis, and if not, whether a waiver from the major transaction requirements would be granted	LD75-3	11.2 – 8

Listing decision – Whether a contractual right given to a joint venture partner to acquire the listed issuer's interest in the joint venture was an option, and if so, whether it would be classified as a major transaction	LD2-2011	11.2 – 12
Listing decision – Whether the Exchange would disregard the consideration ratio for a disposal of investments by a listed issuer	LD20-2011	11.2 – 15
Listing decision – Whether the Exchange would disregard the consideration ratio and accept the alternative ratio proposed by a listed issuer for its capital contribution to a non wholly-owned subsidiary	LD62-1	11.2 – 18
Listing decision – Whether the Exchange would disregard the assets and revenue ratios for a disposal of interest in a joint venture	LD21-2011	11.2 – 21
Listing decision – Whether the Exchange would disregard the percentage ratios for a transaction between two subsidiaries of a listed issuer and accept the alternative percentage ratios calculated based on the net effect of the transaction	LD62-2	11.2 – 24
Listing decision – Whether the Exchange would accept the alternative revenue ratio proposed by a listed issuer due to a change in its accounting policy for jointly controlled entities	LD61-2013	11.2 – 28
Listing decision – Whether the Exchange would disregard the revenue ratio for a disposal of a target company whose business was different from the principal businesses of the listed issuer	LD62-4	11.2 – 31
Frequently asked questions – Definition of transactions and calculation of percentage ratios for notifiable transactions	FAQ11.2 – No.1-33	11.2 – 34

11.3 Aggregation of transactions

Listing decision – Whether a listed issuer was required to aggregate its proposed guarantee for a bank loan to be granted to a joint venture and its initial capital contribution to the joint venture	LD80-2014	11.3 – 1
Listing decision – Whether a listed issuer was required to aggregate three work packages awarded to a contractor which involved different types of work in different locations	LD93-2	11.3 – 3

Listing decision – Whether a listed issuer was required to aggregate its acquisitions of machinery and equipment from the same supplier	LD64-1	11.3 – 5
Listing decision – Whether a listed issuer was required to aggregate its acquisitions of two pieces of land from different parties for redevelopment into a single property	LD64-2	11.3 – 8
Frequently asked questions – Aggregation of transactions	FAQ11.3 – No.1-7	11.3 – 10

11.4 Shareholders' approval requirement

Listing decision – Whether the Exchange would accept a listed issuer's proposal to seek a prior approval in advance from its shareholders for (1) a proposed acquisition of land through public tender; or (2) a proposed disposal of a property, which constituted a major transaction	LD6-2011	11.4 – 1
Listing decision – Whether the Exchange would accept a listed issuer's proposal to seek a prior approval in advance from its shareholders for a disposal of listed investments which constituted a very substantial disposal	LD112-1	11.4 – 4
Listing decision – Whether a listed issuer was required to seek reapproval from its shareholders for changing the terms of a very substantial acquisition after it had been approved by shareholders	LD93-5	11.4 – 7
Listing decision – Whether a listed issuer was required to seek reapproval from its shareholders for changing the terms of a very substantial acquisition after it had been approved by shareholders	LD62-2013	11.4 – 9
Listing decision – Whether the circular and shareholders' approval requirements applied to a disposal of the listed issuer's business by provisional liquidators	LD112-2	11.4 – 11
Listing decision – Whether two shareholders, who had been partners in a project, constituted a closely allied group of shareholders for the purpose of providing a written shareholders' approval for a major transaction	LD8-3	11.4 – 13
Listing decision – Whether the Exchange would waive the general meeting requirement and accept a written shareholders' approval for a very substantial acquisition	LD49-3	11.4 – 14

Listing decision – Whether certain shareholders of a listed issuer had a material interest in a proposed acquisition	LD73-1	11.4 – 16
Listing decision – Whether certain shareholders of a listed issuer had a material interest in the issuer's proposal to privatise a listed subsidiary	LD73-2	11.4 – 19
Frequently asked questions – Shareholders' approval requirements for notifiable transactions	FAQ11.4 – No.1	11.4 – 24

11.5 Disclosure and other requirements

Guidance letter – Disclosure of the basis of consideration and business valuations in notifiable transactions	GL116-23	11.5 – 1
Listing decision – Whether the Exchange would waive the profit forecast requirements in respect of a valuation report on the disposal target disclosed in the listed issuer's announcement and circular for the disposal	LD93-3	11.5 – 8
Listing decision – Whether the Exchange would waive the circular requirement for a major transaction	LD69-2013	11.5 – 11
Listing decision – Whether the Exchange would waive the requirements for disclosing certain information of the counterparties and the assets to be acquired under a discloseable transaction	LD68-2013	11.5 – 13
Listing decision – Whether the Exchange would waive the requirement for disclosing the consideration for certain technology and patent to be acquired by the listed issuer under a discloseable transaction	LD75-5	11.5 – 16
Listing decision – Whether the Exchange would impose additional requirements on a proposed distribution in specie of interests in an overseas listed subsidiary by a listed issuer	LD93-4	11.5 – 20
Frequently asked questions – Disclosure and other requirements for notifiable transactions	FAQ11.5 – No.1-22	11.5 – 24

11.6 Online display of documents

Frequently asked questions – Online display of documents	FAQ11.6 – No.1-3	11.6 – 1

11.7 PRC filing requirements for overseas listings and securities offerings by Mainland companies

Guidance on application of the reverse takeover Rules

I. Background and purpose

1. This guidance letter provides guidance on the application of the reverse takeover (**RTO**) Rules (**RTO Rules**) and related requirements, with an appendix setting out examples to illustrate how the Exchange applies the RTO Rules.

2. Under the RTO Rules, a reverse takeover is defined as an acquisition or series or acquisitions which, in the opinion of the Exchange, constitutes an attempt to achieve a listing of the assets acquired and a means to circumvent the new listing requirements (**principle based test**)[1].

3. The RTO Rules also contain two specific forms of RTOs involving a change in control of the listed issuer (as defined under the Takeovers Code) and an acquisition or a series of acquisitions of assets from the new controlling shareholder and/or its associates at the time of, or within 36 months of the change in control (**bright line tests**)[2].

4. In recent years, the prevalence of backdoor listings has resulted in a substantial increase in the value of a listing status, leading to extensive activities related to investors acquiring controls of listed issuers for their listing platforms (rather than the underlying business) with a view to eventual backdoor listings, and listed issuers undertaking corporate actions (such as disposals of businesses) to facilitate the sale of their listing platforms. Such activities also led to opportunities for market manipulation and undermine investors' confidence in our market. Where these "shell" companies subsequently enter into significant acquisitions, the Exchange would apply the RTO Rules to discourage "shell" activities.

5. In July 2019, the Exchange published its consultation conclusions on *Backdoor Listing, Continuing Listing Criteria and Other Rule Amendments*. The Rule amendments are intended to apply the RTO Rules to:

   - arrangements that circumvented the then RTO Rules, for example, structuring a RTO transaction as a series of smaller acquisitions, or re-sequencing transactions to acquire a new business before disposing of the original business, or through a series of acquisitions and disposals; and

   - arrangements involving an investor acquiring control of a listed issuer and using the listed issuer as a listing platform to achieve a listing of new businesses that may have no connection with the issuer's original business. These new businesses may be acquired by the listed issuer, or developed as greenfield operations and, following the disposal, cessation and/or curtailment of the original business operation, become the major operation of the listed issuer[3].

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1 See Rule 14.06B.
2 See Note 2 to Rule 14.06B.
3 Acquisition of new business(es) may be subject to the RTO Rules. Rule 14.06D (see paragraph 38) may apply to greenfield operations and large scale issue of securities, and Rule 14.06E (see paragraphs 39 to 42) may impose restrictions on disposals.

6. In applying the RTO Rules, the Exchange has regard to the following:

   - The RTO Rules are principle based, anti-avoidance provisions designed to prevent the circumvention of new listing requirements for the assets acquired and/or to be acquired. As such, the Exchange would apply the RTO Rules purposively and the six assessment factors described in the Listing Rules provide guidance to the market on factors that the Exchange would normally consider in a RTO assessment. The applications of these assessment factors would vary from case to case, depending on the specific circumstances of the issuer.

   - As the RTO Rules are principle based, they should provide a framework for addressing backdoor listings and sufficient flexibility to address changing RTO structures, without imposing undue restrictions on legitimate business activities of issuers.

   - The RTO Rules are not intended to restrict legitimate business activities of listed issuers, including business expansion or diversification that is part of the issuer's business strategies related to its existing business, or is consistent with the issuer's size and resources.

   - When applying the RTO Rules, the Exchange's approach is targeted towards transactions that represent an attempt to circumvent the new listing requirements, particularly those involving companies engaging in "shell" activities, as indicated by the factors (a) change in control or de facto control of the listed issuer and (b) fundamental change in the issuer's principal business.

7. All Rule references in this letter are to the Main Board Listing Rules. As GEM RTO Rules are the same as Main Board RTO Rules, the guidance in this letter also applies to GEM issuers.

II. Further guidance on the assessment factors under the principle based test

A. Rule 14.06B (principle based test)

8. Rule 14.06B defines a RTO to be *an acquisition or a series of acquisitions of assets by a listed issuer which, in the opinion of the Exchange, constitutes, or is part of a transaction and/or arrangement or series of transactions and/or arrangements which constitute, an attempt to achieve a listing of the acquisition targets and a means to circumvent the requirements for new applicants set out in Chapter 8 of the Listing Rules.* Note 1 to this Rule sets out factors the Exchange will normally consider in assessing whether the acquisition or series of acquisitions is a RTO transaction:

   i) the size of the acquisition or series of acquisitions relative to the size of the issuer;

   ii) a fundamental change in the issuer's principal business;

   iii) the nature and scale of the issuer's business before the acquisition or series of acquisitions;

   iv) the quality of the acquisition targets;

   v) a change in control (as defined in the Takeovers Code) or de facto control of the listed issuer (other than at the level of its subsidiaries); and/or

vi) other transactions or arrangements which, together with the acquisition or series of acquisitions, form a series of transactions or arrangements to list the acquisition targets.

9. Rule 14.04(2A) defines acquisition targets to be the assets to be acquired, or in the context of a series of transactions and/or arrangements, the assets acquired and/or to be acquired. In other words, a series of transactions and/or arrangements may include completed acquisition(s).

10. In assessing the principle based test, the Exchange will consider the six assessment factors and whether, taken together, the proposed acquisition (or series of acquisitions) would be considered an attempt to circumvent the new listing requirements and a means to achieve the listing of the acquisition targets.

B. The six assessment factors

i) Size of acquisition relative to the issuer

11. Where an issuer undertakes an acquisition of significant size, its existing principal business may become immaterial after the transaction, supporting a concern that the transaction may represent a means to achieve a listing of the target business.

12. The Exchange does not prescribe an absolute threshold in determining whether the size of an acquisition is significant[4]. In assessing the impact of the acquisition on the issuer, the Exchange will take into account other assessment factors such as the nature and scale of the issuer's existing business after the acquisition, and whether the acquisition would result in a fundamental change in the issuer's business.

ii) Acquisition(s) resulting in a fundamental change in the issuer's principal business

13. Where an issuer acquires a target business that is completely different from its existing business and that target business is substantially larger than its existing business, it may be viewed as a fundamental change in the issuer's principal business. This is more likely the case where the issuer's existing business is so immaterial that after the acquisition, the issuer would be substantially carrying on the target business.

14. For the avoidance of doubt, a "fundamental change in the issuer's principal business" does not refer to acquisitions that are part of the issuer's business strategies related to its existing business, including business expansion or diversification, or are consistent with the issuers' size and resources. This may involve an issuer expanding upstream or downstream into new business segments, or an issuer acquiring businesses as part of the issuer's expansion strategy as illustrated in the following examples:

- technology companies in the new economy sector making acquisitions of businesses in mature industries as part of their business strategies, where the acquisitions formed part of their expansion strategies.

- a listed issuer engaging in financial advisory and other financial services proposing to acquire an app-based retail banking services business, where the acquisition is part of the issuer's strategy to expand its business into the fintech sector.

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[4] It should be noted that under the Listing Rules, an acquisition below the size of a very substantial acquisition may be a RTO. This would normally be the case if there are other factors resulting in specific concerns about circumvention of the RTO Rules.

15. Further, where an issuer operating a mature business seeks opportunities to diversify its operations (and income stream) and acquires a target business that is completely different from its existing business, absent other factors (for example, a change in control or de facto control in the issuer and/or an acquisition that is substantial in size), the RTO Rules would not normally apply to restrict an issuer from such business diversification.

iii) Nature and scale of the issuer's business before the acquisition

16. A significant acquisition is more likely to be considered a RTO if the scale of the issuer's existing business is small, as the existing business would likely be immaterial after the acquisition and the issuer would be in substance operating the target business.

17. The Exchange will consider the nature of the issuer's existing business and its financial position. The RTO Rules address concerns about shell activities; accordingly, significant acquisitions by listed issuers with "shell" like characteristics are more likely to be RTO transactions. For example, an issuer that has wound down/disposed of its original business and moved into new businesses that can be easily discontinued (e.g. trading business or money lending business[5]) may suggest that the issuer is engaged in shell activities to facilitate backdoor listing. A newly listed issuer that conducted a series of arrangements (such as change in controlling shareholder, acquisitions and/or disposals) shortly after the lock-up period may also suggest shell activities.

iv) Quality of the acquisition targets

18. The Exchange would consider whether the target business can meet the eligibility and suitability criteria for new listing. In general, a substantial acquisition of a target business that is not suitable for listing will likely be considered circumvention of the new listing requirements, as that target business could not otherwise obtain a new listing. Examples include early exploration companies or a business that operates illegally. Similarly, acquisitions of new businesses or assets that have no track record or have yet to commence operations are more likely to raise questions. This is more so the case where the target business is completely different from that of the issuer. Examples include an acquisition of a patent for new technology or new business proposals where the infrastructure (e.g. production facilities) is under construction.

v) Change in control (as defined in the Takeovers Code) or de facto control of the listed issuer

19. Where a proposal does not fall under the bright line test, it may nevertheless be treated as a RTO under the principle based test. In assessing whether there has been any change in control or de facto control, the Exchange would consider:

    i) a change in the controlling shareholder of the issuer; or

    ii) a change in the single largest substantial shareholder who is able to exercise effective control over the issuer as indicated by factors such as a substantial change to its board of directors and/or senior management. For the avoidance of doubt, these are non-exhaustive factors. There could be other factors that the Exchange may consider as indication of exercise of effective control by the single largest substantial shareholder.

[5] See Guidance Letter GL96-18.

20. The Exchange will consider changes to the personnel and changes to the executive functions of the existing directors when making an assessment. Examples of substantial change of board and/or senior management include change in a majority of the issuer's executive directors and/or senior management carrying executive functions; change in a majority of the directors and/or their executive functions; or change of the chief executive officer.

21. The "change in control or de facto control" factor would not normally apply if (a) the new substantial (and not controlling) shareholder is a passive investor in the issuer; or (b) there are changes in the issuer's board of directors and/or senior management but not its controlling or single largest substantial shareholder. However, where the issuer does not have a controlling or single largest substantial shareholder, a substantial change in its board of directors and/or senior management may raise questions about whether there is a change in de facto control in the issuer.

22. The Exchange normally applies this factor in conjunction with the "series of transactions and/or arrangements" factor. For example, an investor may acquire material shareholding interests in an issuer, appoints new directors to the board which oversees the operations and direction of the listed issuer, and subsequently acquires new businesses. The new directors have no experience in the issuer's original business but have expertise in the new business acquired by the issuer. The Exchange may apply the RTO Rules if, taking into account other factors, it considers that such actions are a means to achieve a listing of the new business and to circumvent the new listing requirements.

23. As described in paragraph 5 above, in the Exchange's experience a change of control together with a series of corporate actions (such as disposals of the issuer's existing business and acquisitions of different lines of businesses)[6] are commonly associated with new investors attempting to achieve a listing of new businesses and circumventing the new listing requirements. In those circumstances the Exchange would more likely apply the RTO Rules.

24. We also clarify that this assessment factor is applied only in the RTO context to identify the circumstances where there may be a backdoor listing concern. It is not a determinant of whether an issuer has "changed control" under the Takeovers Code or for other Rules purposes.

25. ***Change in de facto control arising from issue of restricted convertible securities***[7] - in circumstances involving the issue of restricted convertible securities, the Exchange would consider whether in substance, the issuance serves to allow the vendor (who will hold the issuer's convertible securities) to effectively "control" the issuer. For example, the vendor would become a controlling shareholder of the issuer assuming the convertible securities were fully converted and where i) the issuer has no controlling shareholder when it proposes the acquisition; or ii) the existing controlling shareholder would cease to be a controlling shareholder after the conversion.

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[6] An example involves an issuer engaged in garment business conducting a very substantial acquisition to acquire a property development business from a third party vendor, and shortly after that the issuer's original controlling shareholder proposed to sell its entire interests in the issuer to the vendor, which would result in a change in control of the issuer. The close nexus between the change in control and the completed acquisition may raise concern about circumvention of the new listing requirement. The Exchange may consider these events as a series of arrangements in assessing whether the RTO Rules would apply to the completed acquisition.

[7] Restricted convertible securities are convertible securities with a conversion restriction mechanism to avoid triggering a change in control under the Takeovers Code.

vi) Events and transactions which together with the acquisition form a series of transactions and/or arrangements to circumvent the RTO Rules

26. As set out in paragraph 5 above, the amended RTO Rules address arrangements that are conducted as a series of transactions and/or arrangements over time to achieve a listing of new businesses and circumvention of the new listing requirements. Examples of such arrangements include a series of smaller acquisitions that result in the listing of a new business, or re-sequencing transactions to acquire a new business before disposing of the original business of the issuer, or a series of acquisitions and disposals. This is achieved by assessing a series of transactions and/or arrangements in totality when considering the application of the RTO Rules.

27. The "series of transactions and/or arrangements" factor is normally applied in conjunction with other assessment factors such as the relative size of the transactions to the issuer, and whether the series of transactions and/or arrangements would lead to a fundamental change in the issuer's principal business.

a) A series of transactions or arrangements within 36 months or are otherwise related

28. The Exchange may regard transactions and arrangements as a part of a series if they take place in reasonable proximity to each other (normally within a 36-month period) or are otherwise related. Transactions or arrangements may include change in control or de facto control, acquisitions or disposals of businesses.

29. The RTO Rules are not intended to unduly restrict business expansion or diversification by issuers that take place over a reasonable period where there would be more disclosure for shareholders and the public to assess the issuers' business operations and developments. The Exchange would not normally consider a transaction or arrangement outside the 36-month period as part of the series, unless there is clear nexus between the transactions and/or arrangements, or where there are specific concerns about circumvention of the RTO Rules. For example:

- a transaction proposed shortly outside the 36-month period and which was likely under contemplation during the 36-month period;
- where an issuer terminated a proposed acquisition of a target business (or downsized the acquisition) in response to the Exchange's RTO ruling, the Exchange may treat any further acquisition(s) of the target business made outside the 36-month period as part of a series;
- where an issuer acquired a new business together with an option to acquire another target business and this option is exercised more than 3 years from the original acquisition, the Exchange may consider these acquisitions as a series.

30. Where an issuer acquires new business(es) over a period of time, the Exchange may aggregate the acquisitions when considering whether the acquired businesses together are substantial to the issuer and a means to achieve a listing of the acquired businesses. Acquisitions that are considered as part of a series would normally bear some relationship to each other, for example: (a) acquisitions that are part of a similar line of business, or (b) acquisitions of interests in the same company or group of companies in stages; or (c) acquisitions of businesses from the same or related party.

31. Absent indication of an attempt to achieve a listing of assets and a means to circumvent the new listing requirements, acquisitions of multiple businesses from different parties would not normally be aggregated in a RTO assessment. Circumstances indicating circumvention of the new listing requirements may include a change in control in the issuer followed by a disposal of its original business and acquisitions of multiple lines of new businesses from various parties.

32. When considering whether the size of the acquisitions in a series is substantial, the Exchange would normally aggregate the financial figures/consideration of the acquisition targets (at the time of the respective acquisitions), compared to the size of the issuer, being the lower of (i) the issuer's latest published financial figure (i.e. revenue/profits/assets) or market capitalization before the first transaction in the series; and (ii) its latest published financial figure or market capitalization at the time of the last transaction in the series.

33. When considering whether there is a fundamental change in business over the 36-month period, the Exchange will have regard to the size of the acquisition targets (at the time of their respective acquisitions), compared to the size of the original business (at the time of the last transaction in the series).

34. In addition, where an issuer disposes the business it operated at the commencement of the series of transactions (the original business), it has the effect of reducing the size of the issuer and consequently, may have a bearing on the Exchange's assessment of other assessment factors, including whether there is a fundamental change of business of the issuer, whether the size of the acquisitions are substantial, and whether the issuer is a "shell"[8].

35. Where an issuer conducts shell activities through a series of transactions and/or arrangements involving greenfield operations, equity fundraisings, and/or termination of all or some of its original businesses and such activities are not within the scope of the RTO Rules, the Exchange may exercise its rights under Rule 2.04 to impose additional conditions, for example, requiring the issuer to comply with the RTO requirements. The Exchange may also address shell maintenance concerns (e.g. an issuer operates multiple lines of new businesses or terminates its businesses) by applying Rule 6.01(4) (suitability for listing)[9] or Rule 13.24 (sufficiency of operations)[10].

b) Treating a series of transactions as one transaction

36. When applying the RTO Rules, a series of transactions would be treated as if they were one transaction. Consequently, while an acquisition of the new business may have been completed at an earlier time within the period, by viewing the series of arrangements as one transaction, the RTO Rules would also apply to that completed acquisition.

37. Where the proposed series of transactions and/or arrangements involve a disposal that is preceded by an acquisition (or acquisitions) of a target business, both the RTO Rules and the continuing listing requirements (Rule 13.24) may apply. The target business (i.e. the issuer's remaining business after the proposed disposal) must meet the continuing listing requirement under Rule 13.24[11], failing which the issuer may be subject to the delisting procedures under Rule 6.01(3). Additionally, the RTO Rules may apply to the target business (i.e. the acquisition(s)) that is part of the series of transactions and/or arrangements.

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8 See footnote 5.
9 See Guidance Letter GL96-18.
10 See Guidance Letter GL106-19.
11 Specifically, Rule 13.24 requires an issuer to carry on a sufficient level of operation and have sufficient asset to support its operations to warrant its continued listing.

III. Large scale issue of securities

38. Rule 14.06D describes circumstances involving an investor acquiring control or de facto control of a listed issuer through a large scale subscription of the issuer's securities, and the listed issuer using the proceeds to acquire or develop a new business unrelated to the original business of the listed issuer, achieving a listing of that new business and circumventing the new listing requirements. These arrangements involve a change in control or de facto control and acquisition of new business and/or greenfield operations as discussed in paragraph 5 above. Its application is set out in Guidance Letter GL105-19.

IV. Restriction on disposals

39. Rule 14.06E[12] imposes restriction on a disposal or distribution in specie (or a series of disposals or distributions) that involves all or a material part of the issuer's existing business at the time of, or within 36 months from a change in control (as defined in the Takeovers Code) of the issuer, unless the remaining business or the assets acquired by the issuer can meet the requirements under Rule 8.05 (or Rule 8.05A or 8.05B).

40. This Rule complements the RTO bright line tests in Note 2 to Rule 14.06B to discourage investors from re-sequencing a RTO transaction by acquiring a new business before disposing its original business, thereby circumventing the bright line test (which involves acquisitions that are classified as very substantial acquisitions). The Rule may also apply where an issuer develops a new business through greenfield operation after a change in control, with a view to operating the new business through the listed issuers and circumventing the new listing requirements. As these arrangements do not involve acquisitions, they are not caught by Rule 14.06B.

41. The Note to Rule 14.06E provides the Exchange discretion to apply the same restriction to disposal(s) or distribution(s) by a listed issuer of all or a material part of its existing business at the time of, or within 36 months from a change in de facto control of the listed issuer (by reference to the "change in control or de facto control" factor in the principle based test), where the Exchange considers that the disposal(s) and/or distribution(s) form part of a series of transactions/arrangements to circumvent the new listing requirements. In making this assessment the Exchange would make reference to the six assessment factors under the principle based test. The Exchange would apply this Rule to a series of arrangements that involve an issuer developing a new business through greenfield operation after a change in control or de facto control[13], with a view to operating the new business through the listed issuer and circumventing the new listing requirements (see paragraph 5).

42. Rule 14.06E is not intended to restrict issuers from disposing part of their businesses or assets for commercial reasons. For example, an investor may acquire control in the listed issuer and thereafter, conduct a series of business reorganizations to streamline the underlying business, including the disposal of certain non-performing segments of the issuer's business, provided that is not all or a material part of the issuer's business.

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[12] This Rule incorporates former Rule 14.92.
[13] See paragraphs 19 to 25 for the factors set out in the "change in control or de facto control" factor.

V. Extreme transaction

43. The RTO Rules apply to acquisitions that constitute an attempt to achieve a listing of the assets to be acquired and a means to circumvent the new listing requirements under Chapter 8 of the Listing Rules. Where an acquisition or a series of acquisitions of assets, which individually or together with other transactions or arrangements, may, by reference to the factors under the principle based test have the effect of achieving a listing of the acquisition targets, but the issuer can demonstrate that it is not an attempt to circumvent the new listing requirements, the proposed acquisition (or series of acquisitions) may be classified as an "extreme transaction" under Rule 14.06C.

44. The extreme transaction classification would not be available where the listed issuer demonstrates "shell" like characteristics. This is because the RTO Rules discourage activities related to the trading of, or acquisitions of "listed shells" for backdoor listings. The Exchange will assess the application of the "extreme transaction" category case by case. For an acquisition (or series of acquisitions) to be qualified as an extreme transaction, the issuer has to satisfy the following additional requirements in addition to demonstrating that it is not an attempt to circumvent the new listing requirements:

    i) the issuer has been under the control or de facto control of the same person or group of persons for a long period (normally not less than 36 months) prior to the proposed transaction, and the transaction would not result in a change in control or de facto control of the issuer. The Exchange would make reference to the "change in control or de facto control" factor under the principle based test (see paragraphs 19 to 25) in making this assessment; or

    ii) the issuer has been operating a principal business of substantial size, which will continue after the transaction.

        As general guidance, this may include an issuer with annual revenue or total asset value of HK$1 billion or more based on the latest published financial statements. When assessing the size of the issuer, the Exchange will also take into account the issuer's financial position, the nature and operating model of the business and the issuer's future business plans. For example, an issuer that meets the HK$1 billion in revenue but has very small net asset value (or is in a net liability position) and operates an indent trading business may not meet this test.

Procedural and compliance requirements for extreme transactions

45. Rule 14.06C(2) requires that (i) the acquisition targets must meet the suitability for listing requirement (Rule 8.04) and the new listing track record requirements (Rule 8.05 or 8.05A or 8.05B); and (ii) the enlarged group must meet all the new listing requirements set out in Chapter 8 of the Listing Rules (except Rule 8.05).

46. The issuer would be required to provide sufficient information to the Exchange to demonstrate that the acquisition target meets Rule 8.04 and Rule 8.05 (or Rule 8.05A or 8.05B). This may be in the form of a draft circular with material information, including, for example, draft accountants' report of the acquisition target for the track record period, detailed description of its business and its management, risk factors, legal compliance and any other information as requested by the Exchange. Failure to provide sufficient information for the Exchange to make a determination may result in a RTO ruling.

47. Rule 14.53A requires the issuer to appoint a financial adviser to perform due diligence on the acquisition targets and to provide the declaration in the form set out in Appendix 29. The Listing Committee may, in principle, allow the issuer to classify its proposed acquisition as an extreme transaction based on the information provided in its written submission and/or draft circular and any additional information requested by the Department. However, this classification is subject to the completion of the financial adviser's due diligence work on the target business and its submission of a declaration to support that the acquisition target can meet Rule 8.04 and Rule 8.05 (or Rule 8.05A or 8.05B).

48. The Exchange will require the issuer to reclassify the acquisition as a RTO if the financial adviser cannot provide the declaration, or where there is additional information indicating that the acquisition target cannot meet Rule 8.04 and Rule 8.05 (or Rule 8.05A or 8.05B), or where there are any other concerns about circumvention of the new listing requirements.

VI. Compliance requirements applicable to RTO

Compliance with new listing requirements

49. Where a transaction is ruled as a RTO, the issuer will be treated as if it were a new listing applicant. Rule 14.54(1) requires that (i) the acquisition targets must meet the suitability for listing requirement (Rule 8.04) and the new listing track record requirements (Rule 8.05 or Rule 8.05A or 8.05B); and (ii) the enlarged group must meet all the new listing requirements under Chapter 8 of the Listing Rules (except Rule 8.05).

50. Under Rule 14.54(2), where the issuer has failed to comply with Rule 13.24(1), the acquisition targets must also meet Rule 8.07. The issuer and its sponsor must demonstrate that there is sufficient public interest in the business of the acquisition target and the enlarged group. This may be demonstrated by, for example, conducting a public offer or other analysis with evidence to demonstrate a sufficient level of public interest in the acquisition targets. For this purpose, it would not be sufficient to simply rely on the issuer's existing shareholder base to satisfy the requirements.

51. Note 1 to Rule 14.54 states that if the Exchange is aware of information suggesting that the RTO is to avoid any new listing requirements, the issuer will be required to demonstrate that the acquisition targets meet all the new listing requirements set out in Chapter 8 of the Listing Rules.

52. Where the RTO transaction involves a series of acquisitions (including completed acquisitions), all the acquisition targets in the series of acquisitions must as a whole comply with the requirements in Rule 14.54.

VII. Compliance requirements relating to RTOs or extreme transactions that involve a series of transactions

Track record and due diligence requirements

53. Where the Exchange considers a series of transactions and/or arrangements to constitute a RTO or an extreme transaction, the entire series of acquisitions should, as a whole, meet the new listing requirements of Rule 8.05.

54. The issuer is required to provide sufficient information to the Exchange to demonstrate that the acquisition targets can meet Rule 8.05, including financial information of the targets based on accountant's report or audited financial information[14]. For this purpose the track record period for the completed acquisition(s) and the proposed acquisition(s) in the series shall be referenced to the latest proposed transaction and covers the three financial years [15] immediately prior to the issue of circular for that transaction.

55. The due diligence requirements for RTOs or extreme transactions apply to the acquisition targets that form part of the series as mentioned above[16].

56. As the RTO or extreme transaction Rules apply to i) acquisitions from various independent parties and ii) a series of acquisitions, including completed acquisitions, it is possible that the issuer may not meet the management and/or ownership continuity requirements in the eligibility criteria. The Exchange would consider granting waivers on a case by case basis.

Shareholders' approval requirement

57. Rules 14.53A and 14.55 require shareholders to approve a RTO or an extreme transaction. Where a RTO or extreme transaction involves a series of transactions, this approval requirement applies to the proposed transaction only. In other words, a listed issuer is not required to seek shareholders' approval for the completed transaction(s) that form part of the series.

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[14] Such approach is in line with our practice in requiring an issuer to provide to the Exchange financial results of its remaining group to demonstrate that the remaining group can meet Rule 8.05 in a spin-off under Practice Note 15.

[15] For GEM issuers, the track record period covers the two financial years immediately prior to the issue of circular for that transaction (see GEM Rule 19.57A).

[16] Where during the course of due diligence review the financial adviser identifies issues (e.g. legal non-compliance), the issuer is expected to take measures to resolve these issues.

Appendix

This appendix sets out the cases to illustrate how the Exchange applies the RTO Rules in circumstances described in the guidance letter.

	Case number	Description
I.	**Principle based test under the RTO Rules**	
	Case 1	Acquisition that was significant in size based on its financial forecast
	Cases 2 and 3	Acquisitions of target companies that were considered unsuitable for listing
	Cases 4 and 5	Acquisitions of minority interests in target companies
	Cases 6, 7 and 8	Acquisitions of mining companies
	Case 9	Acquisition that formed part of the issuer's expansion strategies related to its existing business
II.	**Bright line test under the RTO Rules**	
	Case 10	Significant acquisition that would result in a change in the issuer's immediate holding company but not the ultimate controlling shareholder
	Case 11	Waiver from the RTO Rules
	Case 12	Proposed change to the terms of restricted convertible securities previously issued by the issuer in connection with a very substantial acquisition
III.	**Application of Rule 2.04 to require issuers to comply with the RTO requirements**	
	Case 13	Shell activities through a series of arrangements involving continuing connected transactions with the new controlling shareholder
	Case 14	Shell activities through a series of arrangements involving termination of part of the original business
IV.	**Extreme transactions**	
	Case 15	Acquisition of a target company that met the new listing requirements
	Case 16	Acquisition of a target company with a substantial change in its business model during the track record period

I. Principle based test under the RTO Rules

Case number / Listing Rule reference	Background and Decision
Case 1 Rule 14.06B	**Background** 1. Company A was principally engaged in hotel business. Its principal assets comprised one hotel property and cash. It has been loss making over the last five years. 2. Company A proposed to acquire a majority interest in a target company that was newly established to carry out a natural gas project involving the construction and operation of gas pipes and gas stations in the PRC. The target company had signed relevant contracts for the natural gas project and expected to commence the sales of natural gas upon completion of the construction work for the project. 3. The target company was expected to record substantial amounts of revenue and profits in the coming years. The proposed acquisition constituted a disclosable transaction for Company A based on the historical financials of the target company. However, based on the forecast financials of the target company, the acquisition was substantial with projected annual revenue at over 20 times of the revenue of Company A's hotel business. **Decision** 4. The Exchange considered the proposed acquisition would constitute a reverse takeover because: • Company A's existing business had a low level of operations. Based on the target company's business plan and financial forecast, its natural gas business would be significantly larger than the existing business of Company A in terms of revenue and profits. • The target company's natural gas business was different from, and unrelated to, Company A's existing business. The proposed acquisition would lead to a fundamental change in Company A's principal business. • The target company had not generated any revenue before the proposed acquisition. It did not have a track record and could not meet the new listing requirements.

Case number / Listing Rule reference	Background and Decision
Case 2* Rule 14.06B	**Background** 1. Company A was principally engaged in trading of food and beverage products. 2. It proposed to acquire a target company that was engaged in production and sale of organic fertilizers. The revenue, consideration and equity ratios of the proposed acquisition were between 110% and 150%, and the asset ratio was about 90%. 3. Company X (the vendor) was the target company's sole supplier of a major raw material critical for production of the target company's fertilizer products. 4. Company X produced such raw material using its proprietary technology. Company X intended to authorise the target company to use such technology to produce the raw materials and expected the target company could master the technology and achieve full scale production of the raw material within three years. **Decision** 5. The Exchange considered the proposed acquisition would constitute a reverse takeover because: • The target company's business was different from, and unrelated to, Company A's existing business. The proposed acquisition would lead to a fundamental change in Company A's principal business given the significant size of the target company's business. • The proposal involved Company A acquiring part, and not the whole, of an integrated business from Company X. While the target company had planned to manufacture the raw material itself, it was uncertain as to whether and when the target company would be able to do so, and the impact of any such change in its business model and on its financial results. Thus, the target company's historical track record could not reflect its performance after completion of the proposed acquisition. • The target company was unsuitable for listing. It relied on Company X as the sole supplier of the critical raw material that has no alternative suppliers or substitutes for its products. The target company did not have the technology or expertise to produce the critical raw material independently. Company A could not demonstrate that the target company was, or would upon completion of the proposed acquisition be, capable of carrying on its business independently from Company X.

Case number / Listing Rule reference	Background and Decision
Case 3* Rule 14.06B	**Background** 1. Company A was principally engaged in manufacturing and sale of household products. 2. It proposed to acquire a target company which was newly set up by Mr. X (the vendor) to hold certain inventories, machinery and equipment for the production of beverage products (the Target Assets). 3. The asset ratio, the consideration ratio and equity ratio for the transaction were between 200% and 300%. 4. As the target company had not yet obtained a manufacturing licence, it would enter into supply and sales contracts with a PRC company for a term of three years upon completion of the proposed acquisition, such that: • the PRC company would manufacture the beverage products for the target company using the Target Assets; and • the target company would sell the beverage products back to the PRC company. **Decision** 5. The Exchange considered that the proposed acquisition would constitute a reverse takeover because: • The target company did not meet the new listing requirements as it had no trading record. Further, the target company would be unsuitable for listing as it would heavily rely on the PRC company for both the production and sale of its products and would be unable to carry on its business independently from the PRC company. • The target company's business was different from, and unrelated to, Company A's existing business. The proposed acquisition would lead to a fundamental change in Company A's principal business given the significant size of the target company's business. 6. After the Exchange decided to treat the proposed acquisition as a reverse takeover, Company A submitted a revised proposal to acquire only a 30% interest in the target company.

Case number / Listing Rule reference	Background and Decision
	7. The Exchange noted that the revised proposal was made for the purpose of downsizing the acquisition to slightly below 100% (i.e. the threshold for very substantial acquisitions). Notwithstanding the change, the Exchange maintained its view that the revised proposal would still be a reverse takeover as the proposed acquisition was substantial based on the asset and consideration ratios and a means to circumvent the new listing requirements, and the target company was not suitable for listing.
Case 4* Rule 14.06B	**Background** 1. Company A was principally engaged in the businesses of property investment, fund management, and fund and securities investment. 2. Company A proposed to subscribe in the Fund as a limited partner with commitments of about HK$4.5 billion. Company A would have no control over or right to participate in the management of the Fund and the investments to be made by the Fund. 3. The proposed subscription represented about 80% of the asset value and over 900% of the market capitalisation of Company A. Company A intended to finance the subscription using a loan facility granted to it by its controlling shareholder and its internal resources. 4. The Fund was a newly established partnership. It did not have any investments, assets or liabilities, and had not recorded any income or expenses. Company A submitted that the Fund had a clear investment objective to invest in debt instruments of companies established to develop real estates in the PRC. Company A had considered the experience and track record of the directors of the Fund's general partners and was confident in the prospects of the Fund. The proposed subscription would allow Company A to leverage on the Fund's expertise, experience, relationship and resources to source and manage potential investments in the PRC real estate market. **Decision** 5. The Exchange considered that the proposed subscription in the Fund would constitute a reverse takeover because: • The subscription was of a significant size to Company A. Should Company A proceed with the subscription, the investment in the Fund would represent a significant part of Company A's assets.

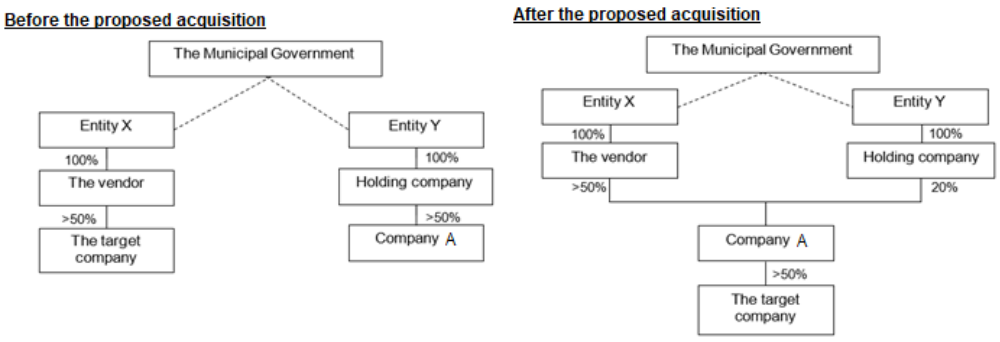
Case number / Listing Rule reference	Background and Decision
	• The Fund was newly set up and did not have any track record, investments or assets. • Although Company A would invest a significant amount of money in the Fund, it would have no control over or right to participant in the management of the Fund or the investments to be made by the Fund. • The subscription was a means to circumvent the new listing requirements. This raised a concern about suitability of listing.
Case 5* Rules 14.06B and 14.54	**Background** 1. Company A proposed to acquire 50% interest in a target company. Upon completion, the investment in the target company would be accounted for as an interest in an associated company or an investment in Company A's financial statements. 2. Company A would pay for the acquisition in cash and by issuing consideration shares and restricted convertible securities to the vendor. 3. The target company was engaged in the manufacturing and trading of sanitary ware products, which was different from Company A's principal businesses. It was significantly larger than Company A based on the asset ratio of about 40 times and a revenue ratio of about 11 times. 4. Company A submitted that the target company could meet the profit requirement for new listing applicants under Rule 8.05(1). The acquisition should not be treated as a reverse takeover. **Decision** 5. The Exchange considered that the proposed acquisition would constitute a reverse takeover because: • Given the significant size of the target company, Company A's existing businesses and assets would be relatively immaterial to the enlarged group upon completion of the acquisition. The acquisition was a means to achieve the listing of the investment in the target company.

Case number / Listing Rule reference	Background and Decision
	• Company A asserted that the target company could meet requirement under Rule 8.05(1). However, as Company A would account for the investment in the target company as an interest in an associated company or an investment, the Exchange considered that the target company's trading record should be excluded for the purpose of Rule 8.05(1).
Cases 6, 7 and 8* Rules 14.06B and 18.03(2)	**Background** 1. Each of Companies A, B and C proposed to acquire a target company which was engaged in mining activities. 2. The size of the acquisitions was very significant to each of the Companies. When assessing whether the acquisitions would constitute reverse takeovers, one of the factors that the Exchange considered was whether the target companies could meet the new listing requirements for a mineral company. 3. In these cases, there was an issue whether the target company could meet Rule 18.03(2) which requires a new applicant mineral company to have at least a portfolio of Indicated Resources, and the portfolio must be meaningful and of sufficient substance: • In the case of Company A, the target company was engaged in oil and natural gas exploration, extraction and processing. It had exploration and extraction rights in two gas fields. One gas field was in a preliminary exploration stage and had resources classified as Prospective Resources under the Petroleum Resources Management System (PRMS). The target company had yet to commence any exploration work in the other gas field. • In the case of Company B, the target company was engaged in the exploration, exploitation and processing of mineral resources in some offshore areas. It was agreed that: - Company B would pay 10% of the consideration to the vendor upon completion of the acquisition on the basis that the vendor produced a valuation report showing that the offshore areas had Indicated Resources of value not less than 10% of the consideration. - Company B would deliver to an escrow agent convertible securities representing the remaining 90% of the consideration. After completion of the acquisition, the vendor could perform extra works in the offshore areas during a specified period, and the escrow agent would release an amount of convertible securities to the vendor according to the value of any additional Indicated Resources discovered. After

Case number / Listing Rule reference	Background and Decision
	the specified period, Company B would cancel any convertible securities that had not been released to the vendor, and the consideration for the acquisition would be reduced accordingly. Company B submitted that it would only pay the consideration based on the value of the Indicated Resources identified under a reporting standard acceptable by the Listing Rules. The portfolio of mineral resources to be acquired was meaningful and of sufficient substance. • In the case of Company C, the target company held mining rights of certain iron mines in the PRC but had not yet commenced production. To address the issue, Company C provided the estimate of resources and reserves for the iron mines identifiable under the Chinese standard. It would appoint a competent person to report on the resources and reserves under the JORC Code when preparing the circular for the acquisition at a later stage. **Decision** 4. In these cases, the Exchange considered that none of the target companies could meet the new listing requirements and thus the proposed acquisitions would constitute reverse takeovers: • Company A failed to demonstrate that the target company had at least a portfolio of Contingent Resources as required under Rule 18.03(2). • In the case of Company B, at the time of the proposed acquisition, the parties could only prove the existence of Indicated Resources of value representing 10% of the consideration, and a substantial part of the target company's portfolio of minerals was not substantiated in the competent person's report. The vendor was given a long period after completion of the acquisition to ascertain whether there were any additional Indicated Resources in the offshore areas. The circumstances of the case indicated that the target company was an early exploration company at the time of the acquisition and did not meet the requirements of Rule 18.03(2). • Company C could only provide the estimate on resources and reserves under the Chinese standard when determining the transaction classification at the announcement stage. However, Chinese standards are not yet recognised as acceptable reporting standards for the purpose of the Chapter 18 requirements. As the basis for information presentation under Chinese standards and JORC-like codes are fundamentally different, resources and reserves presented under Chinese standards may not be recognised as such under JORC-like codes.

Case number / Listing Rule reference	Background and Decision
Case 9 Rules 14.06B and 14.06C	**Background** 1. Company A was principally engaged in the provision of drug discovery services since its initial listing. 2. It proposed to acquire a majority interest in a target company that was engaged in the provision of drug development and manufacturing services. The consideration would be settled by cash. 3. The revenue ratio of the proposed acquisition was about 380% while the asset, profit and consideration ratios were between 20% and 80%. 4. The target company had a trading record of more than three years and recorded profits of more than RMB130 million in aggregate in the last three financial years. Company A considered the proposed acquisition would allow it to expand its business vertically along the pharmaceutical outsourcing service value chain to the drug development and manufacturing business, which formed part of its business strategies disclosed in the IPO prospectus. **Decision** 5. The Exchange agreed that the proposed acquisition would be treated as a very substantial acquisition but not a reverse takeover nor an extreme transaction because: • The proposed acquisition would not lead to a fundamental change in Company A's business as it represented a vertical expansion of Company A's existing business which was in line with Company A's business strategies as disclosed in the IPO prospectus. • The size of the proposed acquisition was not extreme compared to Company A's existing business which had been sizable in scale since listing and would continue to be Company A's principal business after the proposed acquisition.

II. Bright line test under the RTO Rules

Case number / Listing Rule reference	Background and Decision
Case 10* Rule 14.06B	**Background** 1. Company A proposed to acquire from the vendor its interest in a target company. Company A and the target company were engaged in the same line of business. 2. Since Company A would settle part of the consideration by issuing new shares to the vendor, the acquisition would result in a change in its shareholding structure. The simplified group structures before and after the acquisition are:  3. The proposed acquisition was a connected transaction for Company A as the Exchange had deemed the vendor and its associates to be Company A's connected persons since the listing of Company A. Based on the percentage ratio calculation, the acquisition was also a very substantial acquisition. 4. Company A considered that the proposed acquisition was not a reverse takeover. Although the acquisition would result in the vendor acquiring a controlling interest in Company A, there would not be a change in control because: • Both Entity X and Entity Y were subordinate departments of the Municipal Government and under its supervision. Through these entities, the Municipal Government had exercised control over each of the Company A's holding company, Company A, the vendor and the target company, including through the exercise of voting rights. • The Municipal Government had, and would continue to have, ultimate control over Company A before and after the proposed acquisition.

Case number / Listing Rule reference	Background and Decision
	Decision 5. The Exchange agreed that the proposed acquisition would not constitute a reverse takeover because: • Since the Municipal Government would remain as Company A's controlling shareholder following the proposed acquisition, there would not be a change in its ultimate control as a result of the proposed acquisition. • The Exchange also took into account the assessment of "control" under the Takeovers Code. In this case, the Takeovers Executive had granted a waiver to the vendor from its obligation to make a general offer under Note 6(a) (acquisition from another member) to Rule 26.1 of the Takeovers Code.
Case 11 Rule 14.06B	**Background** 1. Company A operated port terminals in the PRC. 2. Company X (controlling shareholder of Company A) was originally wholly owned by the Provincial Government. About a year ago, Company Y acquired 51% equity interest in Company X from the Provincial Government. This constituted a change in control of Company A under the Takeovers Code. *Proposed transaction* 3. Company A proposed to merge with a target company which was listed on a PRC stock exchange and controlled by Company X. The target company also operated port terminals in the PRC. 4. The proposed merger would constitute a reverse takeover under the bright line tests as it was a very substantial acquisition from Company X (being an associate of Company Y) within 36 months of Company Y gaining control of Company A through Company X. The profit ratio was about 120%. Other size tests were below 100%. 5. The proposed merger would allow Company A to expand its existing port terminal business by integrating its port-related resources with those held by the target company and bringing synergy amongst the port operators controlled by Company X. Company A submitted that the proposed merger was not an attempt to achieve a listing of new business and sought a waiver from applying the bright line tests of Rule 14.06B to the merger.

Case number / Listing Rule reference	Background and Decision
	Decision 6. The Exchange agreed that the proposed merger was not a backdoor listing of new business by the incoming controlling shareholder and granted the waiver to Company A for the following reasons: • The proposed merger was in line with Company A's strategies to expand its port terminal business and the size of the merger was not significant to Company A. It would not result in a fundamental change to Company A's principal business. • The proposed merger represented an internal restructuring of the port-related businesses held under Company X which controlled Company A and the target company before the proposed merger and would continue to do so after the merger. There was no injection of asset or business from Company Y.
Case 12* 14.06B and 28.05	**Background** 1. About a year ago, Company A acquired a target company from the vendor. The target company's principal business was different from that of Company A before the acquisition. 2. The consideration was paid in (i) cash, (ii) consideration shares and (iii) restricted convertible notes. The convertible notes were redeemable only upon maturity three years after issue. 3. The terms of the convertible notes included a conversion restriction which did not allow any conversion which would trigger a mandatory general offer under the Takeovers Code. The acquisition was classified as a very substantial acquisition based on percentage ratio calculations. *Proposal to change the terms of the restricted convertible notes* 4. Company A proposed an open offer, fully underwritten by the vendor, to raise funds for its business operations. If no shareholders took up their entitlements and the vendor took up all the offer shares, the vendor's interest in Company A would increase from 18% to approximately 40%.

Case number / Listing Rule reference	Background and Decision
	5. Under the underwriting agreement, the vendor would fulfil its underwriting obligation partly in cash and partly by offsetting the convertible notes. To facilitate this offsetting arrangement, the parties proposed to change the terms of the convertible notes to make them redeemable before maturity. This would require the Exchange's prior approval. **Decision** 6. At the time of the acquisition, the Exchange did not classify the acquisition as a reverse takeover given the terms of the acquisition and in particular, the conversion restriction was structured to avoid triggering the change in control test under the bright line tests of the RTO Rules. 7. In considering whether to approve the proposed change in the redemption clause of the convertible notes, the Exchange was concerned that its purpose was to circumvent the RTO Rules because: • The proposed change was to facilitate the offsetting arrangement which, together with the open offer, would allow Company A to redeem the convertible notes before its maturity and to issue new shares to the vendor resulting in the vendor taking control of Company A. This would effectively change the structure based on which the acquisition had not been treated as a reverse takeover. • Company A had no other reason to immediately redeem the convertible notes which would mature in two years. 8. In response to the Exchange's concern, Company A and the vendor agreed to revise the open offer structure. There would be no change in the terms of the convertible notes and the vendor would not take control (as defined under the Takeovers Code) of Company A under the revised structure of the open offer.

III. Application of Rule 2.04 to require issuers to comply with the RTO requirements

Case number / Listing Rule reference	Background and Decision
Case 13* Rules 2.04	**Background** 1. At the time of its initial listing, Company A was principally engaged in the original business of leasing and trading of construction machinery in Hong Kong. 2. Mr. X (the founder, the chairman and an executive director of Company A) disposed of his controlling interest in Company A to Mr. Y shortly after the 12 month lock-up period. 3. Mr. Y made a general offer for all the remaining shares in Company A under the Takeovers Code. Upon close of the offer, all the directors of Company A have resigned and new directors (including Mr. Y) were appointed to the board of Company A. The new directors did not have experience in the original business. A majority of the new directors were also directors of Company Z which was controlled by Mr. Y and engaged in property business in the PRC. 4. The first annual results released by Company A after its listing showed a 30% drop in revenue from the original business. Company A disclosed that the industry of the original business would slow down and it intended to diversify its business by leveraging on the experience of its directors in the PRC. *Proposed transactions with Company Z* 5. A few months after the close of the offer, Company A proposed to engage in a new business by entering into a framework agreement with Company Z for the provision of property management services to the properties controlled or being developed by Company Z. 6. The transaction with Company Z would constitute a continuing connected transaction (the Proposed CCT). Based on the highest annual cap proposed by Company A, the revenue contributed from the Proposed CCT would represent over 70% of Company A's revenue in the first year after listing. 7. Company A also intended to further expand the new business and was negotiating similar property management service agreements with independent third parties.

Case number / Listing Rule reference	Background and Decision
	Decision 8. The Exchange was concerned that Company A was engaging in shell activities as indicated by a change in control shortly after the lock-up period. The post-listing developments appeared to deviate significantly from the disclosures in Company A's IPO prospectus about its business plans and the rationale for its listing. This suggested that Mr. Y acquired Company A for its listing status rather than the developments of its underlying business. 9. The Exchange informed Company A of its intention, to exercise its right to impose additional conditions on the Proposed CCT under Rule 2.04, by treating Company A as if it were a new listing applicant and requiring it to comply with the requirements for a RTO. In arriving at such decision, the Exchange considered that the Proposed CCT would be an attempt to circumvent the new listing requirements because: • The new business was completely different from the original business and its size would be significant to Company A based on the annual cap for the Proposed CCT. The Proposed CCT would lead to a fundamental change in Company A's business and represent an attempt to achieve a listing of the new business through greenfield operations which had no track record and would not meet the new listing requirements. • While Company A submitted that the Proposed CCT would not be its major operation based on its projected revenues of the original business for the next three years, the Exchange noted that such projection was made on the assumption that the original business would grow at a compound growth rate which was contrary to the performance of the original business after listing, and Company A had not provided any information to support the assumption. The Exchange did not consider this sufficient to address its concern.
Case 14* Rules 2.04	**Background** 1. At the time of its initial listing, Company A was principally engaged in the original business of operating entertainment venues at separate locations under different brand names. 2. Mr. X (the founder, the chairman and an executive director of Company A) disposed of his 70% equity interest in Company A to Mr. Y shortly after the 12 month lock-up period.

Case number / Listing Rule reference	Background and Decision
	3. Mr. Y made a general offer for all the remaining shares in Company A under the Takeovers Code. Upon close of the offer, all the directors of Company A resigned and new directors (including Mr. Y) were appointed to the board of Company A. The new directors did not have experience in the original business. A few months later, Company A closed down two of its entertainment venues that were loss-making. 4. About two years after the offer, Company A acquired from Mr. Y a target company engaged in property management business, which constituted a major and connected transaction. At that time, Company A stated that the acquisition would enable it to diversify its income stream and it had no intention to dispose of or terminate the original business. *Proposal to terminate part of the original business* 5. A few months after the completion of the acquisition, Company A proposed to terminate the lease agreement for one of its two remaining entertainment venues (the Proposal). That entertainment venue contributed a material part of Company A's revenue from the original business but it was operated at a loss in the latest financial year. 6. Company A submitted that a new tenant had leased a venue in the same building to operate an entertainment business in competition with that of Company A. The Proposal was initiated by the landlord who offered Company A a rent-free period before the termination date in exchange for an early termination. **Decision** 7. The Exchange was concerned that Company A was engaging in shell activities as indicated by a change in control shortly after the lock-up period. The subsequent events, including the change in its board of directors, the injection of the new business into Company A and the series of actions to scale down the original business, suggested that Mr. Y acquired Company A for its listing status rather than the developments of its underlying business. 8. The Exchange made the decision to exercise its right to impose additional conditions on the Proposal under Rule 2.04, by treating Company A as if it were a new listing applicant and requiring it to comply with the requirements for a RTO. In arriving at such decision, the Exchange considered that the Proposal, together with the acquisition, would be an attempt to circumvent the new listing requirements because:

Case number / Listing Rule reference	Background and Decision
	• The Proposal would lead to the termination of a material part of the original business and the new business would become the major operation of Company A. The Proposal, which was made shortly after the acquisition, would be a means to "cleanse" the listed shell. It formed part of a series of arrangements to achieve a listing of the new business that would not have otherwise met the new listing requirements. • While Company A submitted that the Proposal was initiated by the landlord and was carried out for commercial reasons, the Exchange did not consider this sufficient to address the concerns.

IV. Extreme transactions

Case number / Listing Rule reference	Background and Decision
Case 15 Rules 14.06B and 14.06C	**Background** 1. Company A was principally engaged in leasing of properties, production and sale of education-related equipment and money lending. The leasing and education-related equipment businesses contributed over 95% of Company A's revenue in recent years. 2. Company A proposed to acquire a target company from Company X (controlling shareholder of Company A for more than three years). The proposed acquisition would not result in a change in control of Company A. 3. The target company was engaged in the provision of financial leasing and factoring services in the PRC. It was substantially larger than Company A, with percentage ratios between 10 and 35 times. **Decision** 4. The Exchange considered that the proposed acquisition would have the effect of achieving a listing of the target company's business because: • The size of proposed acquisition was extreme compared to Company A's existing businesses and the target company's business was different from Company A's core businesses. Given the significant size of the proposed acquisition, it would result in a fundamental change in Company A's principal business. • Company A argued that the proposed acquisition was not an extreme case as it represented an expansion of Company A's existing money lending business. However, the Exchange noted that the money lending business was small in scale. Further, the target company's business was substantially different from Company A's money lending business in terms of operating scale, business models and customers base. Company A would be substantially carrying on the target company's business after the proposed acquisition. 5. Nevertheless, the Exchange agreed that the proposed acquisition could be classified as an extreme transaction (and not a RTO) because: • The target company could meet the new listing requirements (Rule 8.05(1)) and the suitability for listing requirement (Rule 8.04) subject to the completion of the financial adviser's due diligence work on the target company. The proposed acquisition was not an attempt to circumvent the new listing requirements; and

Case number / Listing Rule reference	Background and Decision
	• Company A met the eligibility criterion set out in Rule 14.06C(1)(a) as it had been under control of Company X for more than 36 months and the proposed acquisition would not result in a change in control of Company A.
Case 16* Rule 14.06B	**Background** 1. Company A was principally engaged in trading business. It proposed to acquire a target company from Company X by issuing consideration shares. Upon completion of the acquisition, Company X would become a substantial shareholder of Company A (25% of the enlarged issued shares). 2. The target company was significantly larger than Company A given the asset ratio of about 8 times and revenue ratio of about 50 times. 3. The target company was principally engaged in coal mining. It owned two coal mines (Target Mines) which had been under commercial production for a few years. The information provided showed that there were changes in the business model of the target company: • During the track record period, the target company had been selling mixed coal by mixing the coal extracted from the Target Mines with different types of raw coal purchased from other coal mines owned by Company X (Other Mines). • The target company's coal products were mainly sold to Company X who then on-sell the products to customers for the purpose of centralised management and planning by Company X. Sales to Company X accounted for about 50% of the target company's revenue in the first year of the track record period, and over 90% in the last two financial years. • In light of the recent change in market conditions, the target company intended to sell coal produced from the Target Mines without mixing with raw coal from the Other Mines after completion of the proposed acquisition. • Further, the target company had set up its own sales and distribution team and started to sell its products directly to the customers. 4. Company A submitted that the target company could meet the profit requirement for new listing applicants under Rule 8.05(1) and the acquisition should be treated as an extreme transaction.

Case number / Listing Rule reference	Background and Decision
	Decision 5. The Exchange considered that the proposed acquisition would constitute a reverse takeover because: • Company A's existing business had a small scale of operations and the target company was significantly larger than Company A. • The proposed acquisition would result in a fundamental change in Company A's business. • Although Company A submitted that the target company would meet the profit requirement under Rule 8.05, the Exchange was concerned that the target company's historical financial information were not representative of its future performance due to the significant changes in its business model, including the type of coal sold and the sales and distribution arrangements. As these changes only took place recently, the target company's trading record could not provide sufficient information to allow investors to make an informed assessment of the management's ability to manage the target company's business and the likely performance of that business in the future. The Exchange was concerned that the target company could not satisfy the new listing requirements under Paragraph 2 of Practice Note 3.

*Note * While these cases happened before the amendments of the RTO Rules in October 2019, such amendments would not change the analysis and conclusion in these cases.*

Guidance on large scale issues of securities

I. Background and purpose

1. This letter provides guidance on the application of Rule 14.06D to large scale issues of securities by listed issuers.

2. In recent years the prevalence of backdoor listings has resulted in a substantial increase in the value of listing status, leading to extensive activities related to investors acquiring control of listed issuers for their listing platforms (rather than the underlying businesses) for backdoor listing. In particular, there were some issuers proposing large scale issues of securities to new investors with an intention to use the injected funds to start new businesses unrelated to the issuers' original businesses. The investors would be in effect listing, through the listed issuers, new businesses that would not have otherwise met the new listing requirements. In December 2015, the Exchange issued Guidance Letter GL84-15 on the application of the cash company Rules[1] to restrict these large scale issues of securities.

3. As part of the recent Rule amendments (effective on 1 October 2019) to address backdoor listings and shell activities, the Exchange codified the practices set out in Guidance Letter GL84-15 into Rule 14.06D. This guidance letter supersedes GL84-15.

4. All Rule references in this letter are to the Main Board Listing Rules. As GEM Rule 19.06D is the same as Main Board Rule 14.06D, the guidance set out in this letter also applies to GEM issuers.

II. Relevant Listing Rules

5. Rule 14.06D state that:

"Where a listed issuer proposes a large scale issue of new securities (including any shares, warrants, options or convertible securities) for cash to acquire and/or develop a new business, which, in the opinion of the Exchange, is a means to circumvent the new listing requirements and to achieve a listing of that new business, the Exchange may refuse to grant listing approval for the shares to be issued.

Note: This rule is an anti-avoidance provision to prevent circumvention of the new listing requirements. It is intended to apply to a large scale issue of securities for cash proposed by a listed issuer where there is, or which will result in, a change in control or de facto control of the issuer (by reference to the factor set out in Note 1(e) to rule 14.06B), and the proceeds are to be used to acquire and/or develop a new business that is expected to be substantially larger than the issuer's existing principal business. The effect of the proposal is to achieve a listing of the new business that would not have otherwise met the new listing requirements."

[1] Rules 14.82 to 14.84

III. Guidance

6. Rule 14.06D is an anti-avoidance provision designed to prevent circumvention of new listing requirements through large scale equity fundraisings. When applying this Rule, the Exchange's approach is targeted towards large scale equity fundraisings that are made to facilitate investors in acquiring controls of the issuers for listing of new businesses that would not have otherwise met the new listing requirements.

Application of Rule 14.06D

7. Rule 14.06D is a purposive test and is assessed based on all relevant facts and circumstances of the issuer. This assessment is not simply based on the size of the equity fundraising proposed by the issuer, but also other factors including the nature and scale of the issuer's business and its financial position before the fundraising, its business plans and the intended use of proceeds, and whether there is, or will be, any change in control or de facto control of the issuer[2].

8. In general, an equity fundraising with the following characteristics would normally be caught under Rule 14.06D:

   (a) The size of the fundraising would be very significant to the issuer and would bear little or no correlation with the needs of the issuer's existing principal business.

   (b) Funds raised would be used largely in developing and/or acquiring a new business with little or no relation to the issuer's existing principal business. This would include circumstances where the issuer has started the new business shortly before the proposed fundraising (e.g. obtained a money lending license or acquired a small size money lending company).

   (c) Employing the cash obtained from the fundraising, the issuer would proceed to operate the new business which is expected to be substantially larger than the original business.

   (d) The investor would obtain control or de facto control of the issuer through the subscription of securities in the issuer. The effect is that the investor would obtain a listing platform for listing the new business. This is a circumvention of the new listing requirements as the lack of a track record would render such business unsuitable for listing.

   Two examples are set out in Part IV below.

[2] In making the assessment, the Exchange will consider whether there is any change in the controlling shareholder of the issuer, or any change in the single largest substantial shareholder who is able to exercise effective control over the issuer as indicated by factors such as a substantial change in its board and/or senior management. Where the case involves an issue of restricted convertible securities to the investor, the Exchange will consider whether in substance, the issue serves to allow the investor to effectively "control" the issuer. Please refer to Note 1(e) to Rule 14.06B and paragraphs 19 to 25 of Guidance Letter GL104-19 for details.

Other points to note

9. Rule 14.06D is not intended to restrict fundraising activities of issuers for legitimate business expansions or diversifications. As general guidance, the Rule will not normally apply to an issue of securities if, taking into account the proceeds from the issue[3], less than half of the issuer's assets would consist of cash as a result of the fundraising. Nevertheless, if the Exchange considers that any fundraising, acquisition or other corporate action of the issuer in the future together with the current fundraising are a means to list a new business that is not suitable for listing or otherwise circumvent the new listing requirements, the Exchange may exercise its discretion under Rule 2.04 to impose additional requirements or conditions on such future arrangement(s).

10. Further, the Exchange acknowledges that issuers engaging in asset-light businesses (for example, technology companies in the new economy sector) may have a cash to asset ratio exceeding 50% after fundraising activities. As set out in paragraph 7 above, the Exchange will consider all factors in totality when determining whether an issuer's proposed equity fundraisings is an attempt to circumvent the new listing requirements. The assessment is not simply an analysis of the cash to asset ratio of the issuer.

11. For the avoidance of doubt, the Exchange may apply the RTO Rule 14.06B when issuers use the funds raised for acquisitions of new businesses. This may be the case where an equity fundraising was not caught under Rule 14.06D (e.g. there was no change in control or de facto control of the issuer as a result of the fundraising) but the subsequent acquisition using the funds raised constitutes an attempt to circumvent the new listing requirements under the principle based test of Rule 14.06B.

Consultation with the Exchange

12. Listed issuers who intend to undertake large scale equity fundraisings are encouraged to contact the Exchange at the earliest possible opportunity to seek guidance on the application of Rule 14.06D in individual cases.

IV. Examples

13. In each of the following two examples, the Exchange considers that Rule 14.06D would apply to the proposed issue of securities.

Example 1

14. Company A is principally engaged in the garment business. It recorded revenue of about HK$60 million and a net loss of about HK$20 million in the latest financial year, and its total assets value was about HK$100 million.

15. The proposed subscriptions: Company A signed subscription agreements to raise a total of HK$400 million by issuing restricted convertible bonds[4] to subscribers:

[3] These include any proceeds that are intended to be used for specific purposes (whether by way of legally binding agreements or other commitments)

[4] Convertible bonds with a restriction from conversion to avoid triggering a change in control under the Code on Takeovers and Mergers.

- Upon completion, over 85% of the company's assets would consist of cash. The proceeds from the subscriptions would be mostly used to develop a new mobile game business.

- Assuming full conversion of the bonds, the conversion shares would represent about 4 times of the company's existing issued shares, and the major subscriber would hold more than 60% of the company's shares as enlarged by the conversion shares.

The major subscriber is an entrepreneur.

16. Immediately after signing the subscription agreements, Company A completed an acquisition of a newly set up company engaged in distributing and marketing mobile games. Taking this into account, Company A's cash would represent 65% of its total assets upon completion of the subscriptions.

17. The Exchange's analysis: The Exchange considers that Rule 14.06D would apply to the proposed subscriptions for the following reasons:

    (a) Under the proposal, the subscription amount is significant to the company and the cash level would be 65% of the company's total assets upon completion. The company's assets would comprise substantially of cash.

    (b) The subscriptions would be a means to list a new business which is unsuitable for listing:

        - The company has been engaging in the garment business since listing. It acquired a company engaged in the mobile game business only after it signed the subscription agreements.

        - The subscription amount is significant to the company. It has no correlation, and is completely disproportionate, to the company's existing garment business. The proceeds would be used to develop and operate a new mobile game business that would be significant relative to the existing business after the subscription.

        - The company would in effect be a listed vehicle for the subscriber (who would acquire a de facto control of the company using the restricted convertible bonds) to develop and operate a new mobile game business which has no track record and does not meet the new listing requirements.

Example 2

18. Company B is principally engaged in the business of manufacturing toys. It recorded revenue of about HK$200 million and a loss of HK$38 million in the latest financial year, and its total assets value was about HK$500 million.

19. Two months earlier, Company B obtained a money lender licence in Hong Kong and commenced a money lending business.

20. The proposed subscriptions: Company B signed subscription agreements to raise HK$1 billion by issuing shares to subscribers:

- Upon completion, about 75% of its total assets would consist of cash. The proceeds from the subscriptions would be mostly used to develop the money lending business. In particular, Company B signed loan agreements to provide financial assistance of a total amount of HK$900 million to several independent third parties. These agreements were subject to completion of the subscriptions.

- The subscribers would hold about 55% of Company B's shares as enlarged by the new shares.

The major subscriber is a money lending company.

21. *The Exchange's analysis*: The Exchange considers that Rule 14.06D would apply to the proposed subscriptions for the following reasons:

    (a) The subscription amount is significant to the company and the cash level would be 75% of the company's total assets upon completion. Company B's assets would comprise substantially of cash.

    (b) The subscriptions would be a means to list a new business which is unsuitable for listing:

    - Company B has been engaging in manufacturing toys. The money lending business commenced shortly before the subscriptions were agreed and is a new business of Company B.

    - The subscription amount is significant to Company B. It has no correlation, and is completely disproportionate, to Company B's original toy business. The proceeds would be used to develop and operate the money lending business that would be significant relative to the existing business after the subscription.

    - Company B would in effect be a listed vehicle for the subscribers (who would become controlling shareholders of Company B) to develop and operate the new money lending business that has no track record and does not meet the new listing requirements.

22. Whilst Company B has signed legally binding agreements (i.e. the loan agreements) to ensure that a substantial part of the subscription proceeds would be used shortly after completion of the subscriptions, this does not address the concern about backdoor listing of a new business to circumvention of new listing requirements. These proceeds would be counted for the purpose of calculating the cash to assets ratio of the issuer under Rule 14.06D.

Guidance to issuers contemplating (i) a spin-off and separate listing of businesses or assets on the Exchange; or (ii) a reverse takeover where the issuer is deemed a new listing applicant

A. Purpose

1. This letter provides guidance to issuers contemplating (i) a spin-off to effect a separate listing of businesses or assets on the Exchange; or (ii) a reverse takeover where the issuer is deemed a new listing applicant. In these circumstances, the issuer group (or the enlarged group) may have to fulfil both requirements applicable to listed issuers and to new applicants under the Listing Rules.

B. Background

2. Practice Note 15 of the Main Board Rules (Practice 3 to the GEM Rules) sets out the principles that an issuer should comply when proposing a spin-off of its businesses or assets. Where the company to be spun-off (**Newco**) is to be listed on the Exchange, it must satisfy all the new listing requirements under the Listing Rules.

3. Under Chapter 14 of the Main Board Rules (Chapter 19 of the GEM Rules), an issuer proposing a reverse takeover will be treated as if it were a new listing applicant (**Deemed New Applicant**).

4. Under Chapter 9 of the Main Board Rules (Chapter 12 of the GEM Rules), the Application Proof submitted by a new listing applicant must be substantially complete. The Application Proof must be posted on the Exchange's website at the same time the new listing applicant files its listing application with the Exchange.

C. Guidance

Spin-off

5. In a spin-off, the issuer must comply with Practice Note 15 and the continuing listing obligations under the Listing Rules, and Newco must also meet new listing requirements. Where there are ongoing relationships/transactions between the two entities, issues may arise relating to potential conflicts between interests of the two groups of shareholders. The issuer should give due consideration to these conflict issues, and resolve the matters before it submits the Application Proof.

6. The following are examples of conflicts issues commonly found in new listing application of Newco:

   - competition, including the degree of overlapping business with its parent company and clear business delineation with its parent company;
   - reasons for exclusion of overlapping business of its parent company;
   - extent of future potential/actual competition with its parent company;
   - corporate governance measures to manage future potential/actual conflicts with its parent company; and
   - how the listing applicant can function independently of its parent company including management, operational and financial independences.

7. Under Practice Note 15, an issuer must submit its spin-off proposal to the Exchange for approval. After receipt of the spin-off proposal, the Exchange will comment on the issuer's compliance with the Listing Rules. Where necessary, Newco should make a pre-IPO enquiry to address its position on compliance with the new listing requirements.

8. The Exchange will approve the spin-off proposal after these compliance issues have been addressed. However, Newco's new listing application will be subject to review by the Exchange and approval by the Listing Committee and this approval may or may not be granted.

Reverse takeovers

9. In the case of reverse takeovers, the issuer must ensure that the assets to be acquired must meet the suitability requirement and the track record requirements for a new listing and the enlarged group must meet all the new listing requirements (except the track record requirements) under the Listing Rules (see Main Board Rule 14.54(1)/GEM Rule 19.54(1)). Under Main Board Rule 14.54(2) (GEM Rule 19.54(2)), where the issuer has failed to comply with Main Board Rule 13.24(1) (GEM Rule 17.26(1)), the acquisition targets must also meet the sufficient public interest requirement for a new listing. Since the Application Proof must be substantially complete, the Deemed New Applicant should make pre-IPO enquiries on any issues relating to its compliance with the new listing requirement before submission of the Application Proof (see paragraph 6 above for examples of potential issues).

Whether the payment of a deposit by a listed issuer under an escrow agreement was a major transaction

Parties

- **Company A** – a Main Board issuer and a shareholder of the Target
- **Target** – Company A's acquisition target

Facts

1. Company A announced a general offer to acquire all the Target's shares it did not already own. If all the offerees accepted the offer, the acquisition would be a very substantial acquisition for Company A and would require shareholder approval.

2. A day before the announcement, Company A had entered into an escrow agreement with the Target which was not conditional on approval by Company A's shareholders. Under the agreement, Company A would pay a deposit to an escrow agent upon irrevocable undertakings from the Target's other major shareholders to accept the offer in respect of 50% of the Target's existing share capital. The deposit represented approximately 30% of Company A's total assets. It would be applied to partially pay for the acquisition if the offer became unconditional before a deadline, and was refundable upon a breach of the undertakings. However, the Target would be entitled to the deposit if the offer did not materialise before the deadline for example, if Company A failed to obtain shareholder approval for the acquisition.

3. Company A submitted that the escrow agreement formed part of the commercial arrangement for the offer, and was not a separate transaction. It therefore did not require separate shareholder approval.

Relevant Listing Rules

4. Rule 14.04(1)(a) states that for the purposes of Chapter 14:

   (1) any reference to a "transaction" by a listed issuer:

      (a) includes the acquisition or disposal of assets, including deemed disposals as referred to in rule 14.29 …

5. Rule 14.06(3) states that:

   major transaction — a transaction or a series of transactions (aggregated under rules 14.22 and 14.23) by a listed issuer where any percentage ratio is 25% or more, but less than 100% for an acquisition or 75% for a disposal …

6. Rule 14.40 states that:

   A major transaction must be made conditional on approval by shareholders.

Analysis

7. Chapter 14 governs certain transactions of an issuer, principally acquisitions and disposals having a material impact on its financial position. It seeks to ensure that shareholders are being informed of these transactions and, if they are material, have an opportunity to vote on them.

8. Rule 14.04(1)(a) defines a "transaction" to include an acquisition or disposal of assets. In this case, the purpose of the deposit was to secure an undertaking from certain existing shareholders of the Target to accept the offer. The deposit would be forfeited if Company A failed to obtain shareholder approval and complete the acquisition. This was different from cases where a deposit was refundable upon termination or non-completion of an acquisition for whatever reason.

9. In the circumstances, the deposit payment could be viewed as an acquisition of an intangible asset (i.e. the undertaking to accept) or a disposal of asset (i.e. parting with the deposit to the Target). In either case, it was itself a transaction under Rule 14.04(1)(a).

Conclusion

10. Since the size of the deposit exceeded the threshold for a major transaction, the agreement to pay the deposit should have required prior approval of Company A's shareholders.

Whether the on-market share repurchase by a listed subsidiary was a transaction for the listed parent, and if so, whether it would be aggregated with the listed issuer's previous acquisition of shares in the subsidiary

Parties

- **Company A** – a Main Board issuer
- **Subsidiary B** – Company A's subsidiary and listed on an overseas stock exchange

Facts

1. Company A purchased certain shares in Subsidiary B on the overseas stock exchange (the **On-market Acquisition**).

2. A few months later, Subsidiary B proposed an on-market repurchase of its shares (the **Share Repurchase**).

3. There was a question whether the Share Repurchase was a transaction for Company A under Chapter 14 and if so, whether it would be aggregated with the On-market Acquisition.

4. The Share Repurchase would be a discloseable transaction if it was aggregated with the On-market Acquisition. Company A submitted that the transactions should not be aggregated because they were of different nature and conducted separately.

Relevant Listing Rules

5. Rule 14.01 states that:

   This Chapter deals with certain transactions, principally acquisitions and disposals, by a listed issuer.…

6. Rule 14.04(1) states that:

   any reference to a "transaction" by a listed issuer includes the acquisition or disposal of assets …

7. Rule 14.04(6) states that:

   For the purpose of this Chapter, a "listed issuer" means a company or other legal person whose securities are already listed on the Main Board, … and unless the context otherwise requires, include its subsidiaries;

8. Rule 14.22 states that:

> … the Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are all completed within a 12 month period or are otherwise related. …

9. Rule 14.23 states that:

> Factors which the Exchange will take into account in determining whether transactions will be aggregated include whether the transactions:
>
> (1) are entered into by the listed issuer with the same party or with parties connected or otherwise associated with one another;
>
> (2) involve the acquisition or disposal of securities or an interest in one particular company or group of companies;
>
> (3) involve the acquisition or disposal of parts of one asset; or
>
> (4) together lead to substantial involvement by the listed issuer in a business activity which did not previously form part of the listed issuer's principal business activities.

Analysis

Share Repurchase by Subsidiary B

10. Chapter 14 governs transactions, including acquisitions and disposals of assets, by an issuer and any of its subsidiaries.

11. Here the Share Repurchase was conducted by a subsidiary of Company A and it resulted in an increase of Company A's equity interest in the subsidiary. It was a transaction for Company A.

Aggregation

12. Under Rule 14.22, the Exchange may require an issuer to aggregate a series of transactions if they are completed within a 12 month period or are otherwise related.

13. Rule 14.23 sets out a non-exhaustive list of factors which the Exchange will consider in applying the aggregation rule. The Rule is intended to provide guidance on the circumstances where aggregation may be required. When determining whether aggregation is required in a particular case, the Exchange will consider all relevant facts and circumstances.

14. The Exchange considered that the On-market Acquisition and the Share Repurchase should be aggregated because they were executed closely in time, and both resulted in an increase of Company A's interest in Subsidiary B, albeit through different channels.

Conclusion

15. The Share Repurchase was a transaction for Company A, and it should be aggregated with the On-market Acquisition.

Whether a listed issuer was required to classify its subscription for a convertible note issued by a third party as if the notes were fully converted at the time of entering into the subscription agreement

Parties

- **Company A** – a Main Board issuer
- **Company B** – another Main Board issuer independent from Company A

Facts

1. Company A proposed to subscribe for certain convertible notes to be issued by Company B (the **Subscription**). Under the terms of the notes, Company A had the right to convert the notes into new shares of Company B any time during the conversion period. Any outstanding amount would be redeemed by Company B at the maturity date of the bonds.

2. The Subscription was a transaction for Company A under Chapter 14 as it involved provision of financial assistance to Company B. There was an issue whether Company A would also need to classify the Subscription as if the notes were fully converted.

3. Company A submitted that it had the sole discretion on the conversion of the notes, and it had yet to decide whether and when to exercise its conversion rights. If it proposed to convert the notes, it would comply with the notifiable transaction requirements for acquiring an interest in Company B.

Relevant Listing Rules

4. Rule 14.04(1) provides that:

   "any reference to a "transaction" by a listed issuer:

   (a) includes the acquisition or disposal of assets, …;

   (b) includes any transaction involving a listed issuer writing, accepting, transferring, exercising or terminating (in the manner described in rule 14.73) an option (as defined in rule 14.72) to acquire or dispose of assets or to subscribe for securities;

   (c) …;

   (d) …;

(e) includes granting an indemnity or a guarantee or providing financial assistance by a listed issuer, …

…"

5. Rule 14.12 states that:

"Where the transaction involves granting an indemnity or guarantee or providing financial assistance by a listed issuer, the asset ratio will be modified such that the total value of the indemnity, guarantee or financial assistance plus in each case any monetary advantage accruing to the entity benefiting from the transaction shall form the numerator of the assets ratio. The "monetary advantage" includes the difference between the actual value of consideration paid by the entity benefiting from the transaction and the fair value of consideration that would be paid by the entity if the indemnity, guarantee or financial assistance were provided by entities other than the listed issuer."

6. Rule 14.26 states that:

"In an acquisition or disposal of equity capital, the numerators for the purposes of the (a) assets ratio, (b) profits ratio and (c) revenue ratio are to be calculated by reference to the value of the total assets, the profits attributable to such capital and the revenue attributable to such capital respectively."

7. Rule 14.74 states that:

"The following apply to an option involving a listed issuer, the exercise of which is not at the listed issuer's discretion:—

(1) on the grant of the option, the transaction will be classified as if the option had been exercised. For the purpose of the percentage ratios, the consideration includes the premium and the exercise price of the option; and

(2) on the exercise or transfer of such option, such exercise or transfer must be announced by the listed issuer by means of an announcement published in accordance with rule 2.07C as soon as reasonably practicable if the grant of the option has previously been announced pursuant to the requirements of this Chapter."

8. Rule 14.75 states that:

"The following apply to an option involving a listed issuer, the exercise of which is at the listed issuer's discretion:—

(1) on the acquisition by, or grant of the option to, the listed issuer, only the premium will be taken into consideration for the purpose of classification of notifiable transactions. Where the premium represents 10% or more of the sum of the premium and the exercise price, the value of the underlying assets, the profits and revenue attributable to such assets, and the sum of the premium and the exercise price will be used for the purpose of the percentage ratios; and

(2) on the exercise of such option by the listed issuer, the exercise price, the value of the underlying assets and the profits and revenue attributable to such assets, will be used for the purpose of the percentage ratios. Where an option is exercised in stages, the Exchange may at any stage as the Exchange may consider appropriate require the listed issuer to aggregate each partial exercise of the option and treat them as if they were one transaction (see rules 14.22 and 14.23).

Analysis

9. The Subscription would be a transaction for Company A that involved provision of financial assistance to Company B and accepting an option to convert the notes into Company B's shares. The Exchange agreed that when Company A entered into the subscription agreement:

- it should classify the Subscription by calculating the percentage ratios for the provision of financial assistance to Company B; and

- it was not necessary to classify the Subscription as if the notes were fully converted given that the conversion was at Company A's discretion. If Company A subsequently proposed to exercise the conversion rights, it would be required to classify the conversion as a transaction at that time taking into account the conversion price and Company B' total assets, revenue and profits. This was in line with the approach applicable to transactions involving options under Chapter 14.

Conclusion

10. The Subscription would be classified as a transaction of Company A based on the percentage ratio calculations for providing financial assistance to Company B.

In respect of a placing and top-up subscription proposed by a listed subsidiary, whether the listed parent was allowed to calculate the percentage ratios for its disposal and acquisition of interests in the subsidiary on a net basis, and if not, whether a waiver from the major transaction requirements would be granted

Parties

- **Company X** – a Main Board listed company**,** and the controlling shareholder of Company Y
- **Company Y** – another Main Board listed company

Facts

1. Company X, Company Y and a placing agent entered into a placing and subscription agreement (the **Agreement**) under which Company X agreed to place a certain number of its existing shares in Company Y to independent investors at a fixed price (the **Placing**) and to subscribe for the same number of new shares to be issued by Company Y at the placing price (the **Top-up Subscription**).

2. The Placing was unconditional. Completion of the Placing would take place a few days after the execution of the Agreement.

3. Completion of the Top-up Subscription was subject to various conditions, including completion of the Placing, Exchange approval for listing the new shares to be issued by Company Y under the Top-up Subscription, and a whitewash waiver being granted to Company X by the Executive Director of the Corporate Finance Division of the Securities and Futures Commission (**SFC**) under the Takeovers Code.

4. The Top-up Subscription constituted a connected transaction for Company Y under Chapter 14A. The Top-up Subscription would be exempt from all connected transaction requirements under Rule 14A.92(4) if it could be completed within 14 days after the execution of the Agreement.

5. Company X's shareholding in Company Y would decrease from 46% to 36% as a result of the Placing, but would be increased to 42% upon completion of the Top- up Subscription. When applying the percentage ratios to each of the Placing and Top-up Subscription, the transaction would constitute a major transaction for Company X under Chapter 14.

6. Company X submitted that the purpose of the Placing was to facilitate Company Y's funding raising, and Company Y would issue its new shares to Company X shortly after the Placing. When considering the Placing and the Top-up Subscription as a whole, there would be a net disposal of a 4% interest in Company Y. Company X was of the view that the net effect of the Placing and the Top-up Subscription should be considered in applying the percentage ratios for transaction classification.

7. Company X also requested that, if the Exchange disagreed with its view on the application of the classification rules, the Exchange grant a waiver from the major transaction requirements in respect of the Placing and the Top-up Subscription.

Relevant Listing Rules

8. Rule 14.04 provides that for the purposes of Chapter 14:

   (1) any reference to a "transaction" by a listed issuer:

      (a) includes the acquisition or disposal of assets, including deemed disposals as referred to in rule 14.29;

      …

9. Rule 14A.92 provides that:

   An issue of new securities by a listed issuer or its subsidiary to a connected person is fully exempt if:

   …

   (4) the securities are issued under a "top-up placing and subscription" that meets the following conditions:

      (a) the new securities are issued to the connected person:

         (i) after it has reduced its holding in the same class of securities by placing them to third parties who are not its associates under a placing agreement; and

         (ii) within 14 days from the date of the placing agreement;

      (b) the number of new securities issued to the connected person does not exceed the number of securities placed by it; and

      (c) the new securities are issued at a price not less than the placing price. The placing price may be adjusted for the expenses of the placing.

   …

Analysis

10. Under the notifiable transaction rules, when an issuer proposes a transaction, it must consider whether it falls into one of the classifications in the rules. A transaction includes an acquisition or disposal of assets.

11. In this case, although the fund raising by Company Y through a placing and top- up subscription would, if completed, have the same effect upon Company X as a straight placing by Company Y, it was necessary to have regard to the terms of the Placing and the Top-up Subscription in applying the notifiable transaction rules.

12. The Placing was unconditional while the Top-up Subscription was subject to certain conditions. One possible scenario was that after Company X's disposal of its 10% equity interest in Company Y under the Placing, the Top-up Subscription could not be completed. As the Placing and the Top-up Subscription were two transactions for Company X, being a disposal of existing shares in Company Y to third parties followed by a subscription of new shares in the same company, the Listing Rules required Company X to apply the percentage ratios to each of the Placing and the Top-up Subscription to determine the transaction classification.

13. In considering Company X's waiver application, the Exchange took into account the following factors:

    - The Placing had not been completed when the waiver application was being considered by the Exchange.

    - The parties to the Agreement had taken reasonable steps to ensure completion of the Top-up Subscription. In particular, before completion of the Placing, details of the placees had been submitted to the Exchange as required and Company X had applied to the SFC for, and had been granted, a whitewash waiver under the Takeovers Code. The only outstanding conditions precedent to the completion of the Top-up Subscription were (i) completion of the Placing and (ii) the Exchange's approval of the listing of shares in Company Y to be issued under the Top-up Subscription. Accordingly, the Exchange was satisfied that the concern about the Top-up Subscription failing to complete after the Placing had been addressed.

    - If both the Placing and the Top-up Subscription were completed, there would be a net disposal of a 4% equity interest in Company Y and its impact on Company X would not be material. The size of the net disposal would not trigger the notifiable transaction requirements.

    - Company X would disclose information relating to the Agreement in a joint announcement with Company Y.

14. Given the steps taken by the parties to the Agreement, it was unlikely that the Top-up Subscription would fail to complete after the Placing. The Exchange accepted that it would be unduly burdensome for Company X to comply with the major transaction requirements having regard to the overall impact on it. Granting the waiver would be unlikely to result in undue risks to Company X's shareholders.

Conclusion

15. Each of the Placing and the Top-up Subscription was a transaction for Company X. Company X should apply the percentage ratios to each transaction to determine the transaction classification under Chapter 14.

16. The Exchange granted a waiver to Company X from the major transaction requirements in respect of the Placing and the Top-up Subscription.

Whether a contractual right given to a joint venture partner to acquire the listed issuer's interest in the joint venture was an option, and if so, whether it would be classified as a major transaction

Parties

- **Company A** – a Main Board issuer
- **Partner** – an independent third party
- **Joint Venture** – a joint venture to be formed by Company A and the Partner

Facts

1. Company A proposed to enter into an agreement with the Partner to form the Joint Venture (the **Agreement**). Based on size test calculations, this would not be a notifiable transaction.

2. Under the Agreement, the Partner would have the right to acquire Company A's interest in the Joint Venture (the **Right**) in case of:

    a. a change in control of Company A within a prescribed period after the Joint Venture was formed;

    b. a deadlock on certain matters proposed but not passed at the board or shareholder meetings of the Joint Venture;

    c. Company A becoming insolvent; or

    d. Company A committing a material breach of the Agreement.

3. No premium was payable for the Right. In the case of a, b or c, the exercise price would be the fair market value of to be determined by an independent valuer jointly appointed by the parties. In the case of d, the exercise price would be determined based on the net asset value and other specific financial figures of the Joint Venture at that time.

4. Company A's directors considered that terms of the Agreement were fair and reasonable.

5. Company A sought the Exchange's view on the application of the notifiable transaction requirements to the Right. It submitted that the Right was a common commercial arrangement between joint venture partners to protect their rights and investments. It was not an "option" under Rule 14.72(1) because it was exercisable by the Partner only upon occurrence of events which might or might not happen.

6. If the Exchange disagreed, the Right would be classified as if it had been exercised under Rule 14.74(1). Company A proposed to calculate the size tests based on its estimation of the exercise price for the Right. On this basis, the Right would be below a major transaction.

Relevant Listing Rules

7. Rule 14.04(1)(b) states that any reference to a "transaction" by a listed issuer:

   includes any transaction involving a listed issuer writing, accepting, transferring, exercising or terminating (in the manner described in rule 14.73) an option (as defined in rule 14.72) to acquire or dispose of assets or to subscribe for securities.

8. Rule 14.72(1) defines "option" to mean:

   the right, but not the obligation, to buy or sell something; …

9. Rule 14.73 states that:

   the grant, acquisition, transfer or exercise of an option by a listed issuer will be treated as a transaction and classified by reference to the percentage ratios.

10. Rule 14.74(1) states that the following apply to an option involving an issuer, the exercise of which is not at the issuer's discretion:

    on the grant of the option, the transaction will be classified as if the option had been exercised. For the purpose of the percentage ratios, the consideration includes the premium and the exercise price of the option;

11. Rule 14.76(1) states that:

    For the purpose of rules 14.74(1) …, where, on the grant of the option, the actual monetary value of each of the premium, the exercise price, the value of the underlying assets and the profits and revenue attributable to such assets has not been determined, the listed issuer must demonstrate to the satisfaction of the Exchange the highest possible monetary value, which value will then be used for the purpose of classification of notifiable transaction. Failure to do so will result in the transaction being classified as at least a major transaction. …

Analysis

Whether the Right was an "option" under Chapter 14

12. The Exchange considered that the Right was an "option" which is defined widely in Rule 14.72 to mean the right "to buy and sell something". It disagreed with Company A's view on the application of this rule.

Classification of the Right

13. As the exercise of the Right was not at Company A's sole discretion, the grant of the Right would be classified as if it had been exercised.

14. In determining the classification of the Right, the Exchange considered the size test calculations for the Right prepared by Company A and the following:

    - The formation of the Joint Venture was not a material transaction to Company A.

    - The Right was an exit arrangement that was common in joint ventures. It would be exercised only upon occurrence of certain triggering events which were extraordinary or beyond the parties' control. This could be distinguished from other circumstances where put options were granted.

    - The exercise price would be based on the Joint Venture's fair market value determined by an independent valuer agreeable to both parties, which would protect Company A's interests in the Joint Venture in the event of a buyout, deadlock or insolvency. In the event of a default, Company A considered it reasonable to use a different basis for determining the exercise price when it was in breach of a material term of the Agreement.

    - The Joint Venture was not yet established and the exercise price of the Right had not been determined at the time of the Agreement. Even if the grant of the Right was classified as a major transaction and Company A's shareholders were given an opportunity to vote on it, they would have little information to make an informed decision.

15. In light of the above, the Exchange decided that the grant of the Right would not be treated as a major transaction. Despite this, the Exchange considered that Company A should disclose the formation of the Joint Venture and the terms of the Right because they would bind Company A to a possible disposal in the future which might be material to Company A at that time.

Conclusion

16. The Right was an "option" under Chapter 14. It would not be classified as a major transaction but its terms should be disclosed by an announcement.

Whether the Exchange would disregard the consideration ratio for a disposal of investments by a listed issuer

Parties

- **Company A** – a Main Board issuer
- **Target** – a company listed on an overseas stock exchange
- **Offeror** – a third party who made a general offer to acquire all the shares in the Target

Facts

1. The Offeror made a cash offer to acquire the Target's shares from its existing shareholders.

2. Company A held 15 per cent interests in the Target as an investment and was considering whether to accept the offer. It had a very short timeframe to make an acceptance. Its majority shareholder would approve the disposal by a written shareholder's approval.

3. The disposal would be a very substantial disposal as the consideration ratio exceeded 75 per cent. However, other percentage ratios indicated that the disposal was a major transaction only.

4. Company A submitted that the disposal should be a major transaction instead of a very substantial disposal. When the offer was first announced one month earlier, the consideration ratio was less than 75 per cent based on Company A's then market capitalisation. Since then, there was no material change in Company A's operations and financial position, but its share price had decreased substantially due to the general market downturn. The consideration ratio (calculated based on its latest market capitalisation) became substantially larger than the other percentage ratios. It considered the consideration ratio was anomalous.

Relevant Listing Rules

5. Rule 14.01 states that:

   This Chapter deals with certain transactions, principally acquisitions and disposals, by a listed issuer. …

6. Rule 14.07(4) provides the calculation of a consideration ratio as follows:

   the consideration divided by the total market capitalisation of the listed issuer. The total market capitalisation is the average closing price of the listed issuer's securities as stated in the Exchange's daily quotations sheets for the five business days immediately preceding the date of the transaction (see in particular rule 14.15); and

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.

Analysis

8. Chapter 14 governs an issuer's transactions, including acquisitions or disposals of assets having material impacts on its financial position.

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 and/or shareholders' approval requirements under Chapter 14.

10. The consideration ratio measures the materiality of a transaction by reference to the issuer's latest market capitalisation. It is an important size test as it takes into account the issuer's size at the time of the transaction.

11. This case involved Company A selling the Target's shares under an offer made by a third party. The Exchange noted that:

    - When the offer was made, the percentage ratios (including the consideration ratio) calculated at that time indicated that the disposal would be a major transaction.

    - There was no material change in Company A's financial position and the impact of the disposal on it. The consideration ratio changed only because of the substantial decrease in Company A's share price in a short period.

    - Company A held the Target's shares as an investment and it had other significant operations. The disposal could not be considered "very substantial" to Company A compared to its financial position. This was supported by the other percentage ratios which were substantially smaller than the consideration ratio.

    - The disposal required shareholders' approval whether it was treated as a major transaction or a very substantial disposal.

12. The Exchange considered it acceptable to disregard the consideration ratio.

Conclusion

13. The disposal was classified as a major transaction.

Note: On 1 October 2019, Rule 14.20 was 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 Chapter 14.

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

Whether the Exchange would disregard the consideration ratio and accept the alternative ratio proposed by a listed issuer for its capital contribution to a non wholly-owned subsidiary

Parties

- **Parent** – a Main Board listed company
- **Subsidiary** – a non wholly-owned subsidiary of the Parent

Facts

1. The Parent owned a 89.5% equity interest in the Subsidiary, and consolidated the results of the Subsidiary in its accounts.

2. The Parent proposed an increase in the Subsidiary's registered capital from RMB480 million to RMB1,350 million and for such purpose, the Parent would contribute RMB800 million to the registered capital of the Subsidiary (**Capital Contribution**). The remaining balance would be contributed by one of the minority shareholders of the Subsidiary.

3. As a result of the proposed Capital Contribution, the Parent's equity interest in the Subsidiary would increase by approximately 1.6%, from 89.5% to 91.1%. The Subsidiary would remain a subsidiary of the Parent and its results would continue to be consolidated in the Parent's accounts.

4. For the purposes of classifying the Capital Contribution, the Parent calculated the assets, profits and revenue ratios, none of which exceeded 0.4%.

5. The Capital Contribution of RMB800 million was the value of consideration under MB Rule 14.15 used for the purpose of calculating the consideration ratio which was over 7%. Having regard to other percentage ratios, the Parent submitted that the consideration ratio produced an anomalous result and requested the Exchange to disregard it under MB Rule 14.20.

6. The Parent submitted an alternative size test using, as the value of the consideration for the consideration ratio, the amount it contributed in excess of the contribution required to maintain its interest in the Subsidiary (i.e. RMB1,350 million x 1.6%). The result of the alternative size test was 0.2%.

Relevant Listing Rules

7. MB Rule 14.15(1) provides that when calculating the consideration ratio:

   the value of the consideration shall be the fair value of the consideration determined at the date of the agreement of the transaction in accordance with applicable accounting standards adopted for the preparation of the listed issuer's annual financial statements. Normally, the fair value of the consideration should be the same as the fair value of the asset which is the subject of the transaction. …

8. MB 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.

9. MB Rule 14.26 provides that:

   in an acquisition or disposal of equity capital, the numerators for the purposes of the (a) assets ratio, (b) profits ratio and (c) revenue ratio are to be calculated by reference to the value of the total assets, the profits attributable to such capital and the revenue attributable to such capital respectively.

10. MB Rule 14.28 provides that:

    the value of the entity's total assets, profits and revenue, … is to be multiplied by the percentage of the equity interest being acquired or disposed of by the listed issuer. However, 100% of the entity's total assets, profits and revenue will be taken as the value of the total assets, profits and revenue, irrespective of the size of the interest being acquired or disposed of, if:

    (1) the acquisition will result in consolidation of the assets of the entity in the accounts of the listed issuer; or

    (2) the disposal will result in the assets of the entity no longer being consolidated in the accounts of the listed issuer.

Analysis

11. MB Rule 14.07 sets out five percentage ratios for assessing the impact of a transaction on the listed issuer. The percentage ratio calculation forms the basis for classifying the transaction which determines whether the transaction is subject to any disclosure, reporting and/or shareholders' approval requirements under MB Chapter 14.

12. In the present case, the proposed Capital Contribution would result in an increase in the Parent's equity interest in the Subsidiary by 1.6%. Pursuant to MB Rule 14.28, when calculating the assets ratio, profits ratio and revenue ratio, the numerators would be the values of the Subsidiary's total assets, profits and revenue (calculated in accordance with MB Rule 14.27) multiplied by the percentage of the equity interest being acquired by the Parent (i.e. 1.6%).

13. As to the consideration ratio, MB Rule 14.15 requires the use of the total consideration payable by the listed issuer as the numerator, which in this case, would be the amount of capital proposed to be contributed by the Parent (i.e. RMB800 million).

14. When considering the Parent's request to adopt the alternative size test in place of the consideration ratio under MB Rule 14.20, the Exchange accepted that the consideration ratio produced an anomalous result having regard to the following factors:

    - The consideration ratio was calculated based on the total amount of Capital Contribution which included not only the amount payable for the additional 1.6% equity interest in the Subsidiary but also the contribution required to maintain the Parent's interest in the Subsidiary. However, as the Subsidiary was consolidated in the accounts of the Parent, the amount to be contributed by the Parent for maintaining its interest in the Subsidiary would have no impact on the consolidated financial position of the Parent group.

    - Unlike the consideration ratio, the other percentage ratios (i.e. the assets ratio, profits ratio and revenue ratio) measured the impact of the acquisition of 1.6% equity interest in the Subsidiary on the Parent and their results indicated that the impact of the transaction on the Parent was insignificant. The consideration ratio was substantially higher than the other percentage ratios.

15. In considering the appropriateness of the alternative size test submitted by the Parent, the Exchange noted that the test was calculated based on the value of the Capital Contribution which was in excess of the contribution required to maintain the Parent's interest in the Subsidiary. The alternative size test compared the consideration for acquiring the additional 1.6% equity interest in the Subsidiary and served to measure the impact of the acquisition on the Parent. This approach was in line with the principle for calculating the consideration ratio for a deemed disposal as a result of any issue of shares by a subsidiary of a listed issuer.

Conclusion

16. The Exchange decided to disregard the calculation of the consideration ratio in respect of the Capital Contribution as requested by the Parent and accept the alternative size test submitted by the Parent under MB Rule 14.20.

Note: On 1 October 2019, MB Rule 14.20 was 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 MB Chapter 14.

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

Whether the Exchange would disregard the assets and revenue ratios for a disposal of interest in a joint venture

Parties

- **Company A** – a Main Board issuer
- **Target** – a jointly controlled entity owned by Company A and certain third parties
- **Group** – Company A and its subsidiaries

Facts

1. Company A owned 40 per cent interest in the Target. It recorded the Target's results using the equity method of accounting.

2. Based on the Group's latest accounts, the share of net assets and profits from the Target represented about 50 per cent and 90 per cent of the Group's total assets and net profits.

The proposal

3. The Target would undergo a restructuring to comply with the Mainland regulations, which would involve a reduction of Company A's shareholding in the Target. The parties therefore proposed that:

    - Company A would sell a 7 per cent interest in the Target to third party purchaser(s) (the Disposal); and

    - the Target would issue new shares to third party investors to enlarge its capital base (the Capital Increase).

4. The Disposal and Capital Increase were separate transactions. Together they would reduce Company A's shareholding in the Target to about 15 per cent, which would be treated as an investment in the Group's accounts.

5. The Capital Increase would not be a deemed disposal by Company A because the Target was not its subsidiary.

Issues

6. For the Disposal, the profits and consideration ratios were less than 25 per cent whereas the assets and revenue ratios exceeded 75 per cent. Accordingly, it would be a very substantial disposal for Company A and subject to shareholders' approval.

7. Company A submitted that the assets and revenue ratios were anomalous. It was not meaningful to compare 7 per cent of the Target's assets and revenue with those of the Group as shown in its accounts because the Target was engaging in a business different from those of the Group, and the Target's assets and revenue were not consolidated in the Group's accounts.

8. It proposed to compare 7 per cent of the Target's assets/revenue with the Group's total assets/revenue adjusted by its proportionate interests in the assets/revenue of the Target and other jointly controlled entities. It also proposed to compare 7 per cent of the Target's net assets with the Group's net assets. Based on these alternative size tests, the Disposal should be classified as a discloseable transaction.

Relevant Listing Rules

9. Rule 14.01 states that:

   This Chapter deals with certain transactions, principally acquisitions and disposals, by a listed issuer. …

10. Rule 14.07(1) provides the calculation of an assets ratio as follows:

    the total assets which are the subject of the transaction divided by the total assets of the listed issuer…

11. 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…

12. Rule 14.20 states 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.

Analysis

13. Chapter 14 governs an issuer's transactions, including acquisitions or disposals of assets having material impacts on its financial position.

14. 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 and/or shareholders' approval requirements under Chapter 14.

15. In this case, the Exchange noted that:

- The Target was a material joint venture of Company A having regard to its contributions to the Group's net assets (50 per cent) and net profits (90 per cent). Company A had disclosed the Target's business as one of Company A's principal businesses in its financial reports.

- The Disposal formed part of a proposal to reduce Company A's interest in the Target. When classifying the Disposal, it was necessary to consider the overall impact of the Target's restructuring on the Group.

- The Disposal and the Capital Increase together would result in the Target ceasing to be a joint venture of Company A. As the proposal would have a significant impact on the Group's business and financial position, it was appropriate to classify the Disposal as a very substantial disposal for Company A.

- Company A's proposed alternative size tests were not acceptable as they did not take into account the overall impact of the Target's restructuring on the Group.

Conclusion

16. The Disposal was a very substantial disposal for Company A.

Note: On 1 October 2019, Rule 14.20 was amended to clarify that if any calculation of the percentage ratio produces an anomalous result 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 Chapter 14.

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

Whether the Exchange would disregard the calculation of percentage ratios in respect of the Transaction upon Company A's request and accept the alternative size tests submitted by Company A under Main Board Listing Rule 14.20

Parties

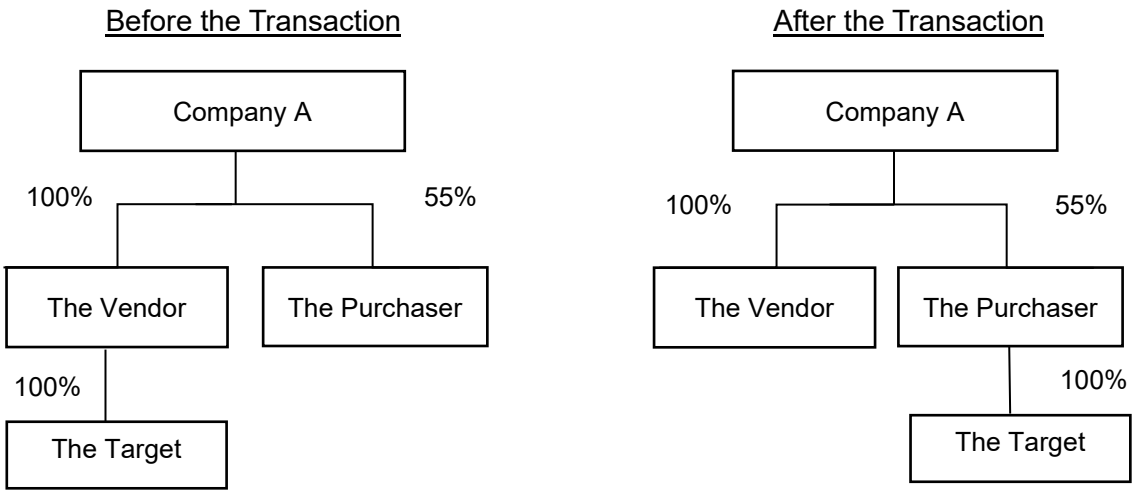
- **Company A** – a Main Board listed company
- **Vendor** – a wholly-owned subsidiary of Company A
- **Target** – a wholly-owned subsidiary of the Vendor
- **Purchaser** – a Main Board listed company and a non wholly owned subsidiary of Company A

Facts

1. Company A proposed to undergo a reorganization in its group that the Vendor would sell its entire interest in the Target to the Purchaser (the **Transaction**), the consideration for which would be paid partially in cash and partially by the Purchaser's issue of bonds.

2. As a result of the proposed Transaction, the Target would become a wholly owned subsidiary of the Purchaser and would remain as a subsidiary of Company A.

3. Set out below is the group structure before and after the proposed Transaction:



4. Company A submitted that the Transaction would involve a transfer of assets between its subsidiaries and there would be in effect a decrease in its interest in the Target by 45% only. Company A submitted alternative size tests in place of the percentage ratios to the Exchange for consideration, which were calculated on the basis of a net disposal of 45% interest in the Target by Company A.

Relevant Listing Rules

5. Main Board Listing Rule 14.15(1) provides that when calculating the consideration ratio:

   the value of the consideration shall be the fair value of the consideration determined at the date of the agreement of the transaction …. Normally, the fair value of the consideration should be the same as the fair value of the asset which is the subject of the transaction.

6. Main Board Listing 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.

7. Main Board Listing Rule 14.25 provides that:

   in circumstances where acquisitions or disposals of equity capital are made by a listed issuer, the provisions set out in rules 14.26 to 14.28 shall be applied in determining the classification of the transaction for the purposes of rule 14.06.

8. Main Board Listing Rule 14.26 provides that:

   in an acquisition or disposal of equity capital, the numerators for the purposes of the (a) assets ratio, (b) profits ratio and (c) revenue ratio are to be calculated by reference to the value of the total assets, the profits attributable to such capital and the revenue attributable to such capital respectively.

9. Main Board Listing Rule 14.27 provides that:

   for the purpose of rule 14.26:

   (1) the value of an entity's total assets is the higher of:

      (a) the book value of the entity's total assets attributable to the entity's capital as disclosed in its accounts; and

      (b) the book value referred to in rule 14.27(1)(a) adjusted for the latest published valuation of the entity's assets if such valuation is published after the issue of its accounts; and

         Note: This will normally apply to a valuation of assets such as properties, vessels and aircraft.

   (2) the value of an entity's profits and revenue is the profits and revenue attributable to the entity's capital as disclosed in its accounts.

10. Main Board Listing Rule 14.28 provides that:

> the value of the entity's total assets, profits and revenue, calculated in accordance with rule 14.27, is to be multiplied by the percentage of the equity interest being acquired or disposed of by the listed issuer. However, 100% of the entity's total assets, profits and revenue will be taken as the value of the total assets, profits and revenue, irrespective of the size of the interest being acquired or disposed of, if:
>
> (1) the acquisition will result in consolidation of the assets of the entity in the accounts of the listed issuer; or
>
> (2) the disposal will result in the assets of the entity no longer being consolidated in the accounts of the listed issuer.

Analysis

11. For the purposes of Chapter 14 of the Main Board Rules, the term "listed issuer" is defined under Rule 14.04(6) to include the listed company itself and its subsidiaries, unless the context otherwise requires. The requirements under this chapter apply to transactions undertaken by the listed company as well as any of its subsidiaries.

12. Rule 14.07 sets out five percentage ratios for assessing the impact of a transaction on the listed issuer. The percentage ratio calculation forms the basis of classifying the transaction which determines whether the transaction is subject to any disclosure, reporting and/or shareholders' approval requirements under Chapter 14.

13. In the present case, the proposed Transaction would involve a disposal of the entire interest in the Target by one subsidiary of Company A and an acquisition of the same by another subsidiary. However, from the perspective of Company A, the Transaction was in substance a group reorganisation which would result in an effective net disposal of a 45% interest in the Target to the minority shareholders of the Purchaser. Upon completion of the Transaction, the Target would remain as a subsidiary of Company A and would continue to be consolidated in Company A's accounts.

14. Having considered the substance of the Transaction and its impact on the consolidated financial position of Company A, the Exchange accepted that calculation of the percentage ratios on the basis of either (i) a disposal of the entire interest in the Target by the Vendor or (ii) an acquisition of the entire interest in the Target by the Purchaser would produce an anomalous result in respect of Company A.

15. Company A submitted alternative size tests for the Transaction by treating the Transaction as a net disposal of 45% interest in the Target by Company A. As the Transaction would not result in a de-consolidation of the Target from Company A's accounts, the Exchange accepted that the alternative size tests taking into account the net effect of the Transaction on the consolidated financial position of Company A were reasonable and appropriate for assessing the impact of the Transaction on Company A.

Conclusion

16. The Exchange decided to disregard the calculation of percentage ratios in respect of the Transaction and accept the alternative size tests submitted by Company A under Rule 14.20.

Note: On 1 October 2019, Rule 14.20 was amended to clarify that if any calculation of the percentage ratio produces an anomalous result 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 Chapter 14.

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

Whether the Exchange would accept the alternative revenue ratio proposed by a listed issuer due to a change in its accounting policy for jointly controlled entities

Parties

- **Company A** – a Main Board listed issuer
- **JCEs** – entities under the joint control of Company A and other venturers

Facts

1. Company A manufactured and sold automobiles in the Mainland through various JCEs. At the time of new listing of Company A, the Exchange imposed certain post-listing conditions on it with a view to regulating the JCEs (including new JCEs established after listing) in a manner consistent with regulating subsidiaries under the Rules.

2. In the last financial year, Company A changed its accounting policy and accounted for the JCEs using the equity method of accounting. Before the change, Company A had recognized its investments in the JCEs using the proportionate consolidation method (that is, the group combined its share of the JCEs' individual income and expenses, assets and liabilities and cash flows on a line-by-line basis).

3. As a result of the change in accounting policy, the revenue shown in Company A's latest published consolidated accounts (**Published Revenue**) no longer included its share of the JCEs' revenue.

4. Company A submitted that as it operated its business under a jointly controlled entity structure, using the Published Revenue as the denominator for calculating the revenue ratio would produce anomalous results and would not properly reflect the materiality of a transaction to Company A.

5. It therefore proposed to adopt an alternative revenue ratio for classifying its transactions where the denominator would be the sum of the Published Revenue and its share of the JCEs' revenue, with adjustments to eliminate the revenue from transactions between the JCEs and Company A (or its subsidiaries) (**Alternate Revenue**). This would assimilate the group's revenue as if the JCEs were still accounted for using the proportionate consolidation method. The figures used to calculate the Alternative Revenue would be disclosed in Company A's published accounts.

Relevant Listing Rules

6. Main Board Rule 14.04(9) states that:

   "percentage ratios" means the percentage ratios set out in rule 14.07, and "assets ratio", "profits ratio", "revenue ratio", "consideration ratio" and "equity capital ratio" shall bear the respective meanings set out in rule 14.07;

7. Main Board Rule 14.07(3) states that:

   Revenue ratio — the revenue attributable to the assets which are the subject of the transaction divided by the revenue of the listed issuer (see in particular rules 14.14 and 14.17);

8. Main Board Rule 14.14 states that:

   "Revenue" normally means revenue arising from the principal activities of a company and does not include those items of revenue and gains that arise incidentally. In the case of any acquisition or disposal of assets (other than equity capital) through a non wholly owned subsidiary, the revenue attributable to the assets being acquired or realised (and not the listed issuer's proportionate interest in such revenue) will form the numerator for the purpose of the revenue ratio (See also rule 14.17).

9. Main Board Rule 14.17 states that:

   The profits (see rule 14.13) and revenue (see rule 14.14) figures to be used by a listed issuer for the basis of the profits ratio and revenue ratio must be the figures shown in its accounts…

10. Main Board Rule 14.20 states 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.

11. Main Board 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.

12. Main Board Rule 14A.06(30) states that:

    "percentage ratios" has the meaning set out in rule 14.04(9);

Analysis

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

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

15. Here the substantial decrease in revenue as shown in Company A's consolidated accounts was due to the change in accounting policy. There was no change in its principal business or operating model.

16. Company A's business was mainly carried out under a jointly control entity structure, and the JCEs were treated and regulated as if they were Company A's subsidiaries for the purpose of the Rules. When assessing the materiality of a transaction using the revenue ratio, it would be reasonable to take into account the group's share of the JCEs' revenue.

Conclusion

17. The Exchange accepted Company A's proposal to use the Alternative Revenue in place of the Published Revenue when calculating the revenue ratio.

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 result 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.

Whether the Exchange would disregard the revenue ratio for a disposal of a target company whose business was different from the principal businesses of the listed issuer

Parties

- **Company A** – a Main Board issuer
- **Holding Company** – the holding company of Company A

Facts

1. Company A was principally engaged in the provision of banking and financial services.

2. In addition to Company A, the Holding Company was also the holding company of a group of companies engaged in insurance businesses.

3. In year 2005, Company A had acquired from a third party vendor (the **Vendor**) the entire equity interest in Target X (which was principally engaged in the provision of banking and financial services) together with about 95% of the equity interest in Target Y (which was principally engaged in insurance businesses) (the **Acquisition**).

4. At the time of the Acquisition, Company A had stated its intention to transfer the interest in Target Y to the Holding Company following the completion of the Acquisition. Nevertheless, Company A and the Holding Company had not entered into any contractual or binding arrangements in respect of the transfer of interest in Target Y to the Holding Company.

5. In year 2006, Company A proposed to enter into an agreement with the Holding Company for the transfer of its 95% equity interest in Target Y to the Holding Company (the **Transaction**).

6. In respect of the proposed Transaction, the assets ratio and profits ratio were less than 1%. The consideration ratio was about 2.1% and the revenue ratio was about 10%.

7. Company A submitted the following information to support its request to disregard the revenue ratio in respect of the Transaction under Rules 14.20 and 14A.80:

    - The calculation of the revenue ratio produced an anomalous result given that the revenue ratio was approximately 10% but the other percentage ratios were all below 2.5%.

    - The revenue ratio was not appropriate to the sphere of activity of Company A because of the difference in what constituted “revenue” for a banking company and an insurance company. It was not meaningful to compare the interest income of a bank with the premium income of an insurance company.

- The Acquisition and the proposed Transaction formed part of a single transaction. Company A's intention to transfer Target Y to the Holding Company was supported by the following facts:

  - the financial results of Target Y were not consolidated in Company A's accounts for the year 2005 given Company A's intention to transfer Target Y to the Holding Company; and

  - under the proposed Transaction, Target Y would be transferred to the Holding Company at cost plus interest payment determined with reference to the one-month HIBOR for the period during which the interest in Target Y was held by Company A.

8. Company A submitted some alternative size tests to the Exchange which compared (i) the premium income of Target Y with the interest earning loans of Company A or new deposits collected by Company A; (ii) the number of employees; or (iii) the net asset values.

Relevant Listing Rules

9. Main Board Listing Rule 14.07(3) provides that a "revenue ratio" refers to:

   the revenue attributable to the assets which are the subject of the transaction divided by the revenue of the listed issuer ….

10. Main Board Listing 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.:

11. Main Board Listing 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

12. Rule 14.07 sets out five percentage ratios for assessing the impact of a transaction on the listed issuer from different perspectives. The revenue ratio serves to assess the impact of a transaction on the listed issuer by measuring the relative level of activity of the target being acquired or disposed of against that of the listed issuer.

13. The percentage ratio calculation forms 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. A connected transaction on normal commercial term is exempt from shareholders' approval requirements if each of the percentage ratios (other than the profits ratio) is less than 2.5% (Note 1) .

14. When considering Company A's request to disregard the revenue ratio in respect of the proposed Transaction, the Exchange had taken into account the following factors:

- The revenue ratio indicated that the Transaction was of a material size that required independent shareholders' approval under Chapter 14A. This was not out of line with the results of other percentage ratios. In particular, the Exchange noted that the consideration ratio was close to the 2.5% (Note 1) threshold requiring independent shareholders' approval. The Exchange did not consider the result of the revenue ratio to be anomalous.

- The revenue ratio measured the impact of the Transaction on Company A by comparing the revenue generated from the principal activity of each of Target Y and Company A. While Target Y was engaging in a line of business different from Company A's principal activity, it did not mean that the calculation of the revenue ratio would be inappropriate in the sphere of activity of Company A. It was not uncommon for listed issuers to acquire or dispose of businesses that were not in line with the issuers' principal activities. The Exchange did not consider that Company A had provided compelling grounds to substantiate its case and declined to exercise its power under Rules 14.20 and 14A.80 to modify the percentage ratio calculation.

- At the time of the Acquisition, Company A and the Holding Company had not entered into any contractual or binding arrangements in respect of the transfer of interest in Target Y to the Holding Company. Although Company A had stated its intention to effect the transfer following the Acquisition, the proposed Transaction could not be viewed as part of the Acquisition in which Company A had complied with the Rule requirements. Accordingly, when Company A entered into the Transaction, it was required to comply with the Rule requirements which were assessed based on the terms of that transaction. The Exchange did not consider the circumstances of this case be exceptional that warranted the Exchange to disregard any percentage ratios.

15. The Exchange was not satisfied with the alternative tests submitted by Company A as they could not provide a meaningful measure of the relative level of activity of Target Y against that of Company A.

Conclusion

16. Based on the above analysis, the Exchange determined that it was inappropriate to disregard the revenue ratio in respect of the Transaction under Rules 14.20 and 14A.80.

Notes:

1. *Effective from 3 June 2010, the threshold for exempting a connected transaction from the independent shareholder approval requirement has been increased from 2.5% to 5%.*

2. *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.

Definition of transactions and calculation of percentage ratios for notifiable transactions

Acquisition or disposal of assets (including deemed disposals)

1. For an acquisition of fixed assets (e.g. equipment and machinery),

(i) how should a listed issuer calculate the assets ratio if the book value of the assets to the vendor is unknown?

The numerator of the assets ratio should be the consideration payable together with liabilities assumed (if any).

(ii) how should the listed issuer calculate the profits and revenue ratios if the assets do not have an identifiable income stream historically?

The profits and revenue ratios are not applicable in this case.

MB Rules 14.07(1), (2) and (3)
GEM Rules 19.07(1), (2) and (3)
First released: March 2004; last updated: May 2024

2. How should a listed issuer calculate the percentage ratios in an acquisition or disposal of equity interest in a company that is classified as an investment?

The listed issuer may apply alternative percentage ratios under the Listing Rules as follow:

- For the assets ratio, the fair value of the equity interest (determined in accordance with the applicable accounting standards adopted by the listed issuer) may be used as the numerator.

- For the profits and revenue ratios, the listed issuer may make reference to the dividend declared by the target company and any dividend policy established by the company.

MB Rules 14.07(1), (2) and (3), 14.20 and 14.28
GEM Rules 19.07(1), (2) and (3), 19.20 and 19.28
First released: March 2004; last updated: May 2024

3. Does the revenue exemption under MB Rule 14.04(1)(g) / GEM Rule 19.04(1)(g) apply to trading of securities carried out by a listed issuer for treasury management purposes?

No. The revenue exemption applies only to securities transactions carried out by any member of a listed issuer's group that is (i) a banking company; (ii) an insurance company; or (iii) a securities house that is mainly engaged in regulated activities under the Securities and Futures Ordinance.

MB Rule 14.04(1)(g)
GEM Rule 19.04(1)(g)
First released: September 2019; last updated: May 2024

4. Is the placing of new shares or treasury shares under general mandate by a listed subsidiary a transaction for the listed parent under the Listing Rules?

Yes. It would be a deemed disposal for the listed parent as it would result in a reduction in the equity interest held by the listed parent in the subsidiary.

Where the deemed disposal constitutes a major transaction or above, the placing is subject to approval by the listed parent's shareholders. In these circumstances, the listed parent should put in place appropriate procedures and mechanism to ensure compliance with the Listing Rules.

MB Rules 14.04(1)(a) and 14.29
GEM Rules 19.04(1)(a) and 19.29
First released: November 2008; last updated: June 2024

5. A subsidiary of a listed issuer proposes to adopt a scheme for granting share awards and options to participants of the scheme.

(i) Which percentage ratios apply for classifying the disposal of the listed issuer's interests in the subsidiary from the grants of awards and options under the scheme?

The disposal will be classified using the assets, revenue, profits and consideration ratios calculated based on the size of the scheme mandate, i.e., the maximum number of shares of the subsidiary that may be issued or transferred out of treasury in respect of awards and options to be granted under such mandate.

(ii) Which figure should be used as the numerator for calculating the consideration ratio?

The listed issuer should use the higher of (a) the fair value of the consideration (i.e. the grant price of share awards or the exercise price of share options); and (b) the fair value of the interests of the subsidiary to be disposed of (see MB Rule 14.15(1) / GEM Rule 19.15(1)).

MB Rules 14.32A and 14.15(1)
GEM Rules 19.32A and 19.15(1)
First released: July 2022; last updated: June 2024

6. Does it constitute an acquisition of assets under MB Rule 14.04(1)(a) / GEM Rule 19.04(1)(a) if a listed issuer subscribes for wealth management products with fixed or guaranteed returns offered by financial institutions?

Subscriptions of wealth management products classified as financial assets on the listed issuer's financial statements constitute acquisitions of assets under MB Rule 14.04(1)(a) / GEM Rule 19.04(1)(a).

For the avoidance of doubt, a transaction under MB Chapter 14 / GEM Chapter 19 normally does not include acquisition of investments classified as cash equivalents on the listed issuer's financial statements or placement of time deposits with a bank regardless of how it is accounted for.

MB Rule 14.04(1)
GEM Rule 19.04(1)
First released: May 2024

Formation of joint venture

7. Does the term "joint venture entity" under MB Rule 14.04(1)(f) / GEM Rule 19.04(1)(f) refer only to an entity which will be accounted for as a jointly controlled entity in the accounts of the listed issuer concerned?

No. The term "joint venture entity" under MB Rule 14.04(1)(f) / GEM Rule 19.04(1)(f) may refer to any entity in any form which is to be established by a listed issuer and any other party / parties.

MB Rule 14.04(1)(f)
GEM Rule 19.04(1)(f)
First released: November 2008; last updated: May 2024

8. (i) How should a listed issuer calculate the percentage ratios for a formation of joint venture?

For the assets and consideration ratios, the numerator will be the consideration determined with reference to MB Rule 14.15(2) / GEM Rule 19.15(2). The profits and revenue ratios are normally not applicable as the joint venture entity would be newly formed with no track record.

(ii) If the joint venture partner proposes to inject its assets (other than cash) as capital contribution, is the asset injection a transaction under the Listing Rules?

If the joint venture entity would be consolidated into the listed issuer's accounts as a subsidiary, the asset injection by the joint venture partner into the joint venture entity would constitute an acquisition of such assets by the listed issuer and is a transaction under the Listing Rules.

MB Rules 14.04(1)(f), 14.07(1), (2) and (3), 14.15(2)
GEM Rules 19.04(1)(f), 19.07(1), (2) and (3), 19.15(2)
First released: November 2008; last updated: May 2024

Leases where the listed issuer is the lessee

9. A listed issuer recognises a lease with fixed lease payments as a right-of-use asset under HKFRS / IFRS 16.

(i) How should the listed issuer classify the lease under the definition of transaction under the Listing Rules?

The lease should be classified as an acquisition of asset (being the right to use the underlying lease asset).

(ii) Do MB Rules 14.04(1)(c) or 14.04(1)(d) / GEM Rules 19.04(1)(c) or 19.04(1)(d) (finance lease or operating lease) apply?

No, as the listed issuer is the lessee.

(iii) Does the revenue exemption under MB Rule 14.04(1)(g) / GEM Rule 19.04(1)(g) apply to the lease?

No. The transaction is of a capital nature.

(iv) How should the listed issuer calculate the percentage ratios?

The assets and consideration ratios apply. The numerator will be the value of the right-of-use asset recognised by the listed issuer (which includes the present value of lease payments) according to HKFRS / IFRS 16.

MB Rules 14.04(1)(a), 14.04(1)(c), 14.04(1)(d), 14.04(1)(g), 14.07, 14.22, 14.23, 14A.24(1), 14A.24(3) and 14A.31
GEM Rules 19.04(1)(a), 19.04(1)(c), 19.04(1)(d), 19.04(1)(g), 19.07, 19.22, 19.23, 20.22(1), 20.22(3) and 20.29
First released: September 2018; last updated: May 2024

10. The lease payments include (i) a fixed dollar amount (fixed lease payments); and (ii) a variable amount determined as a percentage of the listed issuer's annual sales generated from the leased properties (variable lease payments).

Under HKFRS / IFRS 16, the listed issuer will recognise a right-of-use asset taking into account the fixed lease payments. The actual variable lease payments linked to sales will be recognised as expenses in the listed issuer's profit or loss accounts over the lease term.

How should the listed issuer calculate the percentage ratios for the lease?

The value of the right-of-use asset based on the fixed lease payments should be used as numerator of the assets and consideration ratios. The variable lease payments linked to sales will be expenses incurred by the listed issuer in its ordinary and usual course of business and will not form part of the percentage ratios calculation.

(Note: There are other types of variable lease payments (e.g. variable lease payments depending on an index or rate) that are included in the initial measurement of right-of-use asset under HKFRS / IFRS 16. The treatment would be the same as fixed lease payments for the purpose of the Listing Rules).

MB Rules 14.04(1)(a), 14.07, 14A.24(1), 14A.31
GEM Rules 19.04(1)(a), 19.07, 20.22(1) and 20.29
First released: December 2018; last updated: May 2024

11. Is the termination of a lease before its expiry by a listed issuer a transaction under the Listing Rules? How should the listed issuer calculate the percentage ratios for the termination?

Yes. As the early termination will result in a decrease in the amount of right-of-use asset recognised by the listed issuer, it is a disposal of asset under the Listing Rules.

The listed issuer should calculate the assets ratio based on the value of the remaining right-of-use asset and the consideration ratio based on the penalty or fee, if any, payable by the listed issuer for terminating the lease.

MB Rules 14.04(1)(a) and 14.07
GEM Rules 19.04(1)(a) and 19.07
First released: April 2020; last updated: May 2024

Leases where the listed issuer is the lessor

12. Is entering into an operating lease or a finance lease a transaction under the Listing Rules? How should a listed issuer calculate the percentage ratios for a finance lease?

Yes, if it meets the circumstances described in MB Rules 14.04(1)(c) or 14.04(1)(d) / GEM Rules 19.04(1)(c) or 19.04(1)(d).

For a finance lease, the listed issuer should calculate the percentage ratios for the disposal and the provision of financial assistance and classify the finance lease based on the highest percentage ratio.

MB Rules 14.04(1)(c), 14.04(1)(d) and 14.07
GEM Rules 19.04(1)(c), 19.04(1)(d) and 19.07
First released: September 2018; last updated: May 2024

Sale and leaseback transactions

13. Listed Issuer A entered into a sale and leaseback transaction by transferring the legal ownership of an asset to Listed Issuer B and leasing the asset back with an option to buy back the asset at the end of the lease period. Is this a transaction for Listed Issuer A and Listed Issuer B under the Listing Rules?

According to HKFRS / IFRS 16, the transaction will be accounted for as a financing arrangement by each of Listed Issuer A and Listed Issuer B (and not a sale and leaseback transaction).

In the circumstances described, the transfer of the legal ownership of the asset constitutes a disposal of asset by Listed Issuer A and an acquisition of asset by Listed Issuer B under the MB Rule 14.04(1)(a) / GEM Rule 19.04(1)(a).

For Listed Issuer B, the transaction is also a provision of financial assistance.

MB Rules 14.04(1)(a) and 14.04(1)(e)
GEM Rules 19.04(1)(a) and 19.04(1)(e)
First released: September 2018; last updated: May 2024

Financial assistance

14. How should a listed issuer calculate the revenue and profits ratios when it provides financial assistance to a third party?

The numerator of the revenue and profits ratios should be the annual amount of any identifiable income arising from the financial assistance (e.g. interest income).

MB Rule 14.07
GEM Rule 19.07
First released: December 2009; last updated: May 2024

15. Is a cash deposit made to a connected person (a finance company approved by regulatory authorities) a notifiable and connected transaction?

Yes. It is a provision of financial assistance by the listed issuer to the connected person.

MB Rules 14.04(1)(e) and 14A.24(4)
GEM Rules 19.04(1)(e) and 20.22(4)
First released: February 2013; last updated: May 2024

16. A listed issuer proposes to subscribe for a convertible bond. The bond may be convertible into shares of the bond issuer at the sole discretion of the listed issuer.

(i) Is the subscription of the convertible bond a transaction under the Listing Rules?

Yes, it constitutes provision of financial assistance to the bond issuer.

(ii) Is the exercise of the conversion rights a transaction under the Listing Rules? If yes, can the listed issuer seek shareholders' approval for the conversion at the time of subscription of the bond?

Yes, the conversion would result in an acquisition of shares and is a transaction under the Listing Rules. The listed issuer may seek shareholders' approval for the conversion at the time of subscription of the convertible bonds, provided that it can provide information to its shareholders to assess the transaction.

MB Rule 14.07
GEM Rule 19.07
First released: December 2009; last updated: June 2024

17. A listed issuer proposes to grant a loan to its substantial shareholder who has also provided a loan to the listed issuer. Can the loans to and from the substantial shareholder be netted off when calculating the percentage ratios for the financial assistance?

No. The proposed loan should be classified on a standalone basis.

MB Rules 14.07 and 14A.87
GEM Rules 19.07 and 20.87
First released: May 2021; last updated: May 2024

Right of first refusal

18. A joint venture agreement grants the joint venture parties a right of first refusal in the event the other joint venture partner(s) disposes of its interest in the joint venture. Is the grant of the right of first refusal by / to the listed issuer a transaction under the Listing Rules?

No. A right of first refusal is not a transaction under the Listing Rules given (i) no consideration is payable for the right; and (ii) the listed issuer will have the discretion on whether to acquire or dispose the joint venture interest when the right is exercised.

If the listed issuer or the joint venture partner exercises the right of first refusal, the disposal or acquisition (as the case may be) by the listed issuer will be a transaction under the Listing Rules.

MB Rule 14.04(1)
GEM Rule 19.04(1)
First released: December 2009; last updated: May 2024

Other corporate actions

19. Is a voluntary liquidation of a subsidiary by a listed issuer a transaction under the Listing Rules?

No. However, the liquidation process may involve transactions (such as disposal of the subsidiary's assets) which would constitute transactions for the listed issuer.

MB Rule 14.04(1)
GEM Rule 19.04(1)
First released: December 2009; last updated: May 2024

20. Is a forced sale of property by a listed issuer pursuant to a court order a transaction under the Listing Rules?

No, as the listed issuer is bound to follow the court order and has no discretion to act in a different manner.

MB Rule 14.04(1)(a)
GEM Rule 19.04(1)(a)
First released: December 2009; last updated: May 2024

Assets, profits and revenue ratios

21. (i) How should the total assets be adjusted if a dividend with a scrip alternative is proposed by a listed issuer?

A scrip dividend has no impact on total assets and no adjustment is required. However, if the number of scrip shares to be issued and / or transferred out of treasury is not known at the time of the transaction, the listed issuer should assume that the entire dividend is paid in cash when adjusting the total assets.

(ii) How should the total assets be adjusted if a dividend is proposed by a non-wholly owned subsidiary of the listed issuer?

If the dividend is proposed by a non-wholly owned subsidiary of the listed issuer, adjustment to total assets should be made to the extent that the total consolidated assets will be reduced by the dividend payable to non-controlling interests by the subsidiary.

MB Rule 14.16(1)
GEM Rule 19.16(1)
First released: March 2004; last updated: June 2024

22. Should a listed issuer's profits and revenue figures exclude the results of a major subsidiary that had been disposed of by the listed issuer after the year end?

Under MB Rule 14.17 / GEM Rule 19.17, the Exchange may be prepared to accept the exclusion of profits and revenue from the subsidiary that have been separately disclosed as discontinued operations in the listed issuer's accounts.

If the disposal does not fall under MB Rule 14.17 / GEM Rule 19.17 and the profits and / or revenue ratios produce an anomalous result, the listed issuer may consult the Exchange (or the Exchange may require) on the application of MB Rule 14.20 / GEM Rule 19.20.

MB Rules 14.07(2) and (3), 14.17 and 14.20
GEM Rules 19.07(2) and (3), 19.17 and 19.20
First released: November 2008; last updated: May 2024

23. Can a listed issuer use the total assets shown in its latest published unaudited quarterly results?

Although MB Rule 14.16 / GEM Rule 19.16 makes no reference to quarterly accounts, a listed issuer may use the total assets figure from its latest published quarterly results if it has adopted quarterly reporting (as recommended by the Corporate Governance Code set out in Appendix C1 to the MB Rules and GEM Rules).

MB Rules 14.04(2), 14.07(1), 14.16 and App C1
GEM Rules 19.04(2), 19.07(1), 19.16 and App C1
First released: November 2008; last updated: May 2024

24. Can a listed issuer use the profits and revenue figures shown in its latest published audited interim accounts?

No, a listed issuer should use the figures shown in its latest published audited accounts for the full financial year.

MB Rules 14.04(2) and 14.17
GEM Rules 19.04(2) and 19.17
First released: November 2008; last updated: May 2024

25. Can a listed issuer use the total assets, profits and revenue figures shown in its preliminary results announcement if it has not yet published the relevant annual report?

Yes, if a listed issuer has published a preliminary results announcement based on its audited financial statements and its accounts have been agreed with the auditors. In rare circumstances, where any such figures need to be revised in the audited accounts subsequently available, the listed issuer should re-compute the relevant percentage ratios and re-comply with any additional requirements if the proposed transaction results in a higher classification.

MB Rules 14.04(2), 14.16 and 14.17
GEM Rules 19.04(2), 19.16 and 19.17
First released: November 2008; last updated: May 2024

26. Is it necessary to annualise the revenue and profits of the listed issuer or the target company if (i) the latest audited accounts of the listed issuer cover a period of 18 months (due to a change in financial year end date); or (ii) the acquisition target commenced operation for less than one year?

No, the Listing Rules require a listed issuer to calculate the revenue and profits ratio based on figures shown in the accounts of the listed issuer and the target company.

However, if the profits and/or revenue ratios produce an anomalous result, the Exchange may exercise its discretion under MB Rule 14.20 / GEM Rule 19.20 and accept alternative size tests based on annualised revenue and profits. Listed issuers should consult the Exchange if it proposes to adopt alternative size tests.

MB Rules 14.04(2), 14.07(2) and (3), 14.17 and 14.20
GEM Rules 19.04(2), 19.07(2) and (3), 19.17 and 19.20
First released: November 2008; last updated: May 2024

27. Which figure should a banking company use as the denominator of the revenue ratio?

Net interest income plus other operating income. Operating income shall have the same meaning as in the Banking (Disclosure) Rules, Chapter 155M of the laws of Hong Kong.

MB Rules 14.07(3) and 14.14
GEM Rules 19.07(3) and 19.14
First released: March 2004; last updated: September 2024

Consideration ratio

28. How should a listed issuer calculate the market capitalisation if it has preference shares and warrants?

The market capitalisation should be calculated based on the total number of ordinary shares in issue (excluding treasury shares) of the listed issuer, excluding preference shares and warrants.

MB Rule 14.07(4)
GEM Rule 19.07(4)
First released: March 2004; last updated: June 2024

29. How should a PRC issuer calculate the market capitalisation if its domestic shares are quoted on NEEQ?

The market capitalisation should be calculated based on the PRC issuer's total number of shares in issue including H shares and domestic shares but excluding treasury shares, multiplied by the average closing price of its H shares for the 5 days preceding the date of the transaction and during which trading of its shares could be conducted on NEEQ.

MB Rules 14.07(4) and 19A.38A
GEM Rules 19.07(4) and 25.34C
First released: September 2019; last updated: September 2024

30. How should a listed issuer calculate the consideration ratio for an acquisition if the consideration includes (i) a fixed amount of cash; and (ii) an additional amount that may be payable upon occurrence of certain future events?

The numerator of the consideration ratio should include the fixed amount of cash and the maximum value of the additional consideration that may be paid by the listed issuer in the future. If the total consideration is not subject to a maximum or such maximum value cannot be determined, the proposed acquisition will normally be classified as a very substantial acquisition.

MB Rule 14.15(4)
GEM Rule 19.15(4)
First released: November 2008; last updated: May 2024

Equity capital ratio

31. Is a listed issuer required to calculate the equity capital ratio if the consideration for an acquisition is satisfied by shares of its subsidiary?

No, as the equity capital ratio applies only to a transaction involving an issue of equity capital and / or a transfer of treasury shares of the listed issuer as consideration.

MB Rule 14.07(5)
GEM Rule 19.07(5)
First released: December 2009; last updated: June 2024

Alternative percentage ratios

32. Can a listed issuer calculate the size tests on a net basis if it transfers assets from a wholly-owned subsidiary to a non-wholly owned subsidiary?

Where the proposed transaction (effectively a group restructuring) involves a disposal of assets by one subsidiary and an acquisition of the same assets by another subsidiary, calculations of the percentage ratios on a gross basis may produce an anomalous result for the purpose of classifying the transaction. The Exchange may accept alternative size tests calculated based on the net disposal of the listed issuer's interest in the assets.

Please see Listing Decision HKEX-LD62-2 for a case involving an intra-group transfer under a proposed group reorganisation. The Exchange accepted alternative size tests based on the net effect of the disposal in that case.

MB Rules 14.04(1)(a) and 14.20
GEM Rules 19.04(1)(a) and 19.20
First released: November 2008; last updated: May 2024

33. How should a listed issuer calculate the profits ratio if it has incurred a net loss in the latest financial year?

The profits ratio is not applicable in this case as the listed issuer was loss making. The listed issuer should provide alternative test(s) in respect of the profits ratio (such as a gross profit comparison) for the Exchange's consideration.

MB Rules 14.07(2) and 14.20
GEM Rules 19.07(2) and 19.20
First released: March 2004; last updated: May 2024

Whether a listed issuer was required to aggregate its proposed guarantee for a bank loan to be granted to a joint venture and its initial capital contribution to the joint venture

Parties

- **Company A** – a Main Board issuer
- **Company B** – a joint venture partner
- **Joint Venture** – a 40:60 joint venture company set up by Company A and Company B

Facts

1. Company A and Company B established a 40: 60 equity joint venture company (i.e. the Joint Venture) for the purpose of setting up the production facilities for certain chemical products. Under the joint venture agreement, the total investment amount for the Joint Venture was to be financed partly by the registered capital contributed by the joint venture partners and partly by bank borrowings.

2. At that time, Company A was only obliged to contribute its share of the registered capital to the Joint Venture, and there was no agreement or commitment for Company A to provide guarantee or indemnity for any bank borrowings of the Joint Venture to satisfy the balance of total investment amount. Based on the capital contribution by Company A, the formation of the Joint Venture was a discloseable transaction.

The proposed transaction

3. After 15 months, Company A and Company B proposed that the Joint Venture would seek a bank loan facility to satisfy part of the total investment amount, and they would provide guarantee for the loan facility in proportion to their respective interests in the Joint Venture.

4. The proposed guarantee itself would be a discloseable transaction for Company A. Company A enquired whether the guarantee would need to be aggregated with its capital contribution to the Joint Venture. If aggregation was required, the guarantee would constitute a major transaction.

Relevant Listing Rules

5. Rule 14.15 provides that when calculating the consideration ratio:

> "(2) where a transaction involves establishing a joint venture entity or other form of joint arrangement, the Exchange will aggregate:—
>
> (a) the listed issuer's total capital commitment (whether equity, loan or otherwise), including any contractual commitment to subscribe for capital; and
>
> (b) any guarantee or indemnity provided in connection with its establishment;
>
> Note: Where a joint venture entity or other form of joint arrangement is established for a future purpose, for example to develop a property, and the total capital commitment cannot be calculated at the outset, the Exchange will require the listed issuer to recalculate the relevant percentage ratios at the time when that purpose is carried out. The Exchange will look at the purpose of setting up the arrangement in terms of the initial transaction only. For example, the purpose could be the development of the property for which the arrangement was established. The Exchange will not look at subsequent transactions entered into under the arrangement for the purpose of calculating the total capital commitment in relation to the establishment of the arrangement."

6. Rule 14.22 provides that:

> "… the Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are … otherwise related…"

Analysis

7. Under Rule 14.22, the Exchange may require an issuer to aggregate a series of transactions if they are related. In the case of a transaction involving the formation of a joint venture, Rule 14.15(2) states that the Exchange will aggregate the issuer's total capital commitment and any guarantee provided in connection with its establishment. The note to Rule 14.15(2) also provides that where a joint venture is established for a future purpose and the total capital commitment cannot be calculated at the outset, the Exchange will require the listed issuer to recalculate the relevant percentage ratios at the time when that purpose is carried out.

8. In this case, the Joint Venture was established for the purpose of setting up certain production facilities. The capital contribution and the guarantee were provided by Company A to satisfy the total investment of the Joint Venture in connection with its establishment. They were related and should be aggregated.

Conclusion

9. Company A was required to aggregate the proposed guarantee with its capital contribution to the Joint Venture.

Whether a listed issuer was required to aggregate three work packages awarded to a contractor which involved different types of work in different locations

Facts

1. A Main Board issuer (**Company A**) was engaged in the telecommunication business.

2. It entered into a procurement agreement with an independent contractor to provide it with a turnkey delivery for network expansion in Country X. The agreement was divided into three work packages based on different work locations. Company A could terminate any part of the agreement at any time.

3. Company A considered that, although all three work packages were awarded to one contractor under one procurement agreement, each was a separate transaction and should not be aggregated because:

   a. Each work package was distinct and separate from the others, entailing different types of work, covering different locations, involving different technologies and calling for a different pace of expansion. Also, each had an individual contract value. Company A would need to issue individual orders under each work package before the contractor was obliged to provide services.

   b. During the tender process, bidders were invited to submit a tender for each of the three work packages or any combination.

   c. The procurement agreement was only a framework agreement and did not affect the distinctiveness and separateness of each work package. The purpose of using one agreement for all three work packages was to enhance efficiency and minimise costs and duplication of documents. It could also help lock in the contractor on terms favourable to Company A.

Relevant Listing Rules

4. Rule 14.22 states that:

> … the Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are all completed within a 12 month period or are otherwise related. …

5. Rule 14.23 further states that:

> Factors which the Exchange will take into account in determining whether transactions will be aggregated include whether the transactions:
>
> (1) are entered into by the listed issuer with the same party or with parties connected or otherwise associated with one another;
>
> (2) involve the acquisition or disposal of securities or an interest in one particular company or group of companies;
>
> (3) involve the acquisition or disposal of parts of one asset; or
>
> (4) together lead to substantial involvement by the listed issuer in a business activity which did not previously form part of the listed issuer's principal business activities.

Analysis

6. Under Rule 14.22, the Exchange may require an issuer to aggregate a series of transaction if they are completed within a 12 month period or are otherwise related.

7. Rule 14.23 sets out a non-exhaustive list of factors which the Exchange will consider in applying the aggregation rule. The Rule is intended to provide guidance on the circumstances where aggregation may be required. When determining whether aggregation is required in a particular case, the Exchange will consider all relevant facts and circumstances.

8. In this case, the Exchange considered that all three work packages were related because:

   a. Despite the differences identified by Company A, the three work packages were all related to the telecommunication network expansion in Country X and awarded to the same contractor.

   b. The value of each individual contract was pre-agreed under the same procurement agreement.

   c. The terms of the procurement agreement (including pricing) were negotiated and agreed with the same contractor as one package which, Company A submitted, could lock in the contractor on terms favourable to the company. This indicated that Company A considered the terms of all the work packages as a whole.

Conclusion

9. The Exchange required the three work packages to be aggregated.

Whether a listed issuer was required to aggregate its acquisitions of machinery and equipment from the same supplier

Parties

- **Company A** – a Main Board listed company
- **Company B and its subsidiaries** – independent third parties

Facts

1. Company A was at the material time engaged in sale of finished fabrics and provision of fabrics processing subcontracting services.

2. Company A and its subsidiaries (the **Group**) had been gradually expanding its scale of operations subject to the availability of financial resources. In the previous 12 months, Company A had acquired certain new machinery and equipment for its principal business from suppliers that were independent third parties to the Group. Among these acquisitions, there were a number of contracts (the **Contracts**) for acquiring various types of machinery and production equipment with different models and specifications (the **Machinery**) from Company B or its subsidiaries (the **Group B**) (collectively, the **Acquisitions**).

3. Company A submitted that it had no intention to limit the source of the Machinery to suppliers within the Group B. However, given that the Group B was one of the major suppliers of machinery and equipment in the market, it was inevitable for Company A to acquire from the Group B the machinery and equipment that were required in the ordinary and usual course of business of the Group.

4. Company A had not entered into any long term contract or master agreement with any members of the Group B for the supply of machinery and/or equipment to the Group. In respect of the Acquisitions, each of the Contracts was separately negotiated between Company A and the relevant supplier on an arm's length basis, and the contractual terms (including, among others, the price of the Machinery and terms of delivery) were subject to negotiation each time the relevant Contract was made.

5. The Machinery acquired by Company A under each Contract was functional on its own and it did not form part of any assembled machine acquired or to be acquired by Company A.

6. The Acquisition under each Contract itself did not constitute a notifiable transaction under Chapter 14 of the Main Board Rules. However, if the Acquisitions were aggregated, they would constitute a discloseable transaction. Company A sought guidance from the Exchange on whether the Acquisitions should be aggregated under Rule 14.22.

Relevant Listing Rules

7. Main Board Rule 14.22 provides that:

> … the Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are all completed within a 12 month period or are otherwise related. …

8. Main Board Rule 14.23 further provides that:

> Factors which the Exchange will take into account in determining whether transactions will be aggregated include whether the transactions:
>
> (1) are entered into by the listed issuer with the same party or with parties connected or otherwise associated with one another;
>
> (2) involve the acquisition or disposal of securities or an interest in one particular company or group of companies;
>
> (3) involve the acquisition or disposal of parts of one asset; or
>
> (4) together lead to substantial involvement by the listed issuer in a business activity which did not previously form part of the listed issuer's principal business activities.

Analysis

9. The purpose of aggregation is to prevent a listed issuer from "splitting" an otherwise large transaction into two or more smaller transactions so that, when size tests are applied to each smaller transaction, it does not reach the relevant thresholds for requiring disclosure and/or shareholders' approval under Chapter 14. Pursuant to Rule 14.22, the Exchange may require a listed issuer to aggregate a series of transactions if they are all completed within a 12 month period or are otherwise related.

10. Rule 14.23 sets out a non-exhaustive list of factors which the Exchange will take into account in applying the aggregation rule. The rule intends to provide guidance on the circumstances where the Exchange may require aggregation of transactions of a listed issuer. When determining whether aggregation of transactions is required in a particular case, the Exchange will consider all relevant facts and circumstances of the case.

11. In the present case, the Acquisitions were made within a 12-month period and they fell within the circumstances described in Rule 14.23(1) as the Machinery was acquired from companies within the Group B which, the Exchange considered, were "parties connected or otherwise associated with each other" under Rule 14.23(1).

12. In making the determination, the Exchange had taken into account the following submissions of Company A to substantiate that the Acquisitions were not connected or related in substance and the "splitting" of a transaction into smaller transactions was not a concern:

- each of the Contracts was separately negotiated between Company A and the relevant supplier on an arm's length basis. The Acquisitions were not made under any master agreement or long term contract between Company A and the Group B.

- the Machinery acquired by Company A under each Contract was functional on its own. Each of the Acquisitions was subject to the need of Company A from time to time, dependent on the progress of its production plan / requirements and the availability of funds. Given the facts of this case, the individual Machinery acquired did not form part of a single asset as referred in Rule 14.23(3).

- the Acquisitions were in line with the existing principal business of the Group and the circumstances described in Rule 14.23 (4) did not exist.

13. Having considered all relevant factors, the Exchange accepted that it was not appropriate to conclude that aggregation was required solely on the basis of the factor in Rule 14.23(1) applying.

Conclusion

14. The Exchange determined that the Acquisitions would not be aggregated under Rule 14.22.

Whether a listed issuer was required to aggregate its acquisitions of two pieces of land from different parties for redevelopment into a single property

Facts

1. A Main Board listed company (**Company X**) was at the material time engaged in property development and investment in the Mainland China.

2. Company X acquired from a government agency the land use right of a piece of land (the **Land A**) (the **First Acquisition**). The First Acquisition did not constitute a notifiable transaction under Chapter 14 of the Main Board Listing Rules.

3. Within a month after the First Acquisition, Company X proposed to participate in the open tender for the land use right of another piece of land (the **Land B**) which was adjacent to Land A (the **Second Acquisition**).

4. Completion of the First and Second Acquisitions was not conditional on each other.

5. Company X intended to redevelop Land A and Land B into a single property for commercial and residential uses.

6. The Second Acquisition itself constituted a discloseable transaction. If the First and Second Acquisitions (together the **Acquisitions**) were to be aggregated under Rule 14.22, the transaction would be classified as a major transaction.

Relevant Listing Rules

7. Main Board Rule 14.22 provides that:

   … the Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are all completed within a 12 month period or are otherwise related. …

   Main Board Rule 14.23 provides that:

   Factors which the Exchange will take into account in determining whether transactions will be aggregated include whether the transactions:

   (1) are entered into by the listed issuer with the same party or with parties connected or otherwise associated with one another;

   (2) involve the acquisition or disposal of securities or an interest in one particular company or group of companies;

(3) involve the acquisition or disposal of parts of one asset; or

(4) together lead to substantial involvement by the listed issuer in a business activity which did not previously form part of the listed issuer's principal business activities.

Analysis

8. The purpose of aggregation is to prevent a listed issuer from "splitting" an otherwise large transaction into two or more smaller transactions so that, when size tests are applied to each smaller transaction, it does not reach the relevant thresholds for requiring disclosure and/or shareholders' approval under Chapter 14. Pursuant to Rule 14.22, the Exchange may require a listed issuer to aggregate a series of transactions if they are all completed within a 12 month period or are otherwise related.

9. Rule 14.23 sets out a non-exhaustive list of factors which the Exchange will take into account in applying the aggregation rule. The rule intends to provide guidance on the circumstances where the Exchange may require aggregation of transactions of a listed issuer. When determining whether aggregation of transactions is required in a particular case, the Exchange will consider all relevant facts and circumstances of the case.

10. In the present case, the First and Second Acquisitions were closely associated in time (i.e. within one month). The Acquisitions fell under the circumstances described in Rule 14.23(3) as the Exchange considered that Land A and Land B formed part of one asset given the following the facts:

- Land A and Land B were adjacent to each other; and

- Company X acquired Land B with the intention to develop such piece of land together with Land A under the same project.

11. In its submissions against aggregation of the Acquisitions, Company X referred to the fact that (a) the completions of the First and Second Acquisitions were not inter-conditional; (b) at the time of the Second Acquisition, Company X was uncertain as to whether it would be successful in its bid for Land B; and (c) the vendors of the Acquisitions were different and were not parties connected or otherwise associated with each other.

12. Having considered all relevant factors, the Exchange was of the view that the facts mentioned in paragraph 10 were sufficient to conclude that the Second Acquisition was made in association with the First Acquisition. While there were commercial reasons for Company X to enter into the First and Second Acquisitions separately, the Acquisitions together formed a series of transactions which had a material impact on Company X and accordingly, shareholders of Company X should be given the opportunity to vote on the Second Acquisition.

Conclusion

13. The Exchange determined that the Acquisitions should be aggregated under Rule 14.22.

Aggregation of transactions

1. A listed issuer recently acquired 80% interest in a target company, representing a major transaction. It now proposes to acquire the remaining 20% interest in that company which, on a standalone basis, would be a disclosable transaction. Will the two transactions be aggregated for the purpose of calculating the percentage ratios for the second acquisition?

Yes.

If the aggregation results in a higher transaction classification compared to the first acquisition (i.e. a very substantial acquisition), the second acquisition would be subject to the Listing Rules requirements for a very substantial acquisition.

If the aggregation results in the same classification as the first acquisition (i.e. a major acquisition), the second acquisition would be subject to the requirements for a disclosable transaction. This is because the listed issuer had complied with the major transaction requirements initially.

MB Rule 14.22
GEM Rule 19.22
First released: November 2008; last updated: May 2024

2. A listed issuer recently completed an acquisition which did not constitute a notifiable transaction. It now proposes an acquisition which, on a standalone basis, would be a discloseable transaction and when aggregated with the first acquisition, would be a major transaction. How would the major transaction requirement apply to these acquisitions?

Normally, the major transaction requirement would only apply to the second acquisition. However, if information about the first acquisition is necessary for shareholders to decide on how to vote in respect of the second acquisition, the listed issuer should include those disclosure in the announcement and circular of the second acquisition.

MB Rule 14.22
GEM Rule 19.22
First released: November 2008; last updated: May 2024

3. The Listing Rules require a listed issuer to consult the Exchange on aggregation of transactions before it enters into any proposed transaction(s). Must a listed issuer consult the Exchange under all circumstances?

No. The purpose of the Listing Rules is to minimise the risk of non-compliance with the aggregation Rules by a listed issuer before it enters a transaction. A listed issuer does not need to consult the Exchange if that is not the case, for example:

- the proposed transaction when aggregated with the previous transaction(s), would not result in a higher transaction classification; or

- the listed issuer intends to aggregate the proposed transaction with the previous transaction(s) and comply with the relevant requirements.

MB Rules 14.23B, 14A.84, 14A.85 and 14A.86
GEM Rules 19.23B, 20.82, 20.83 and 20.84
First released: November 2008; last updated: May 2024

4. Is a listed issuer required to aggregate all its securities transactions within a 12-month period for the purpose of the notifiable transaction rules?

Normally a listed issuer is required to aggregate its securities transactions within a 12-month period if they are related. For example, securities transactions involving the same company, or are entered into by the listed issuer with the same party.

MB Rules 14.22 and 14.23
GEM Rules 19.22 and 19.23
First released: September 2019; last updated: May 2024

5. How should a listed issuer aggregate a series of acquisitions and disposals of listed shares in the same company within 12 months?

If the listed issuer proposes to acquire additional shares in the company, it should aggregate the shares to be acquired under the proposed transaction with the shares acquired within the last 12 months and still held by it.

For example, the listed issuer proposes to acquire 5 million shares in Company A and has in the past 12 months acquired 3 million shares and subsequently sold 1 million shares in the same company, it should aggregate the proposed acquisitions of 5 million shares with its current holdings of 2 million shares.

MB Rules 14.22 and 14.23
GEM Rules 19.22 and 19.23
First released: September 2019; last updated: May 2024

6. How should a listed issuer calculate the percentage ratios for a proposed acquisition of wealth management products (e.g. index or asset linked deposits) from a licensed bank if the listed issuer holds other wealth management products issued by the same bank?

Normally the listed issuer is required to aggregate its investment in wealth management products acquired from the same bank.

In calculating the percentage ratios, the numerator of the assets and consideration ratios would be the sum of the acquisition costs of (i) the wealth management products to be acquired; and (ii) the wealth management products previously acquired from the same bank and still held by the listed issuer. The numerator of the revenue and profits ratios would be calculated based on the aggregate expected income from these products e.g. annual interest income to be recognised by the listed issuer.

MB Rules 14.22 and 14.23
GEM Rules 19.22 and 19.23
First released: May 2021; last updated: May 2024

7. Is a listed issuer required to aggregate leases it entered into with the same party as lessee within a 12-month period?

Generally the Exchange would not require aggregation of the lease transactions solely because they are made with the same party. When applying the aggregation Rules, the Exchange would consider whether the lease transactions are connected or related in substance and whether there is a concern about "splitting" of a lease transaction into smaller ones to circumvent the notifiable / connected transaction requirements. It would take into account a number of factors, including:

- whether the leases are made under a master agreement or negotiated and concluded at the same time;
- whether the leased assets form part of one asset; and / or
- whether the leases would together lead to substantial involvement by the issuer in a new business activity.

(See also Listing Decisions HKEX-LD64-1 (2008) under Section 11 "Notifiable Transactions" and HKEX-LD76-3 (2009) under Section 12 "Connected Transactions" of the Guidance Materials for Listed Issuers).

MB Rules 14.22, 14.23, 14.23B, 14A.24(1), 14A.24(3),14A.31 and 14A.84
GEM Rules 19.22, 19.23, 19.23B, 20.22(1), 20.22(3), 20.29 and 20.82
First released: September 2018; last updated: May 2024

Whether the Exchange would accept a listed issuer's proposal to seek a prior approval in advance from its shareholders for (1) a proposed acquisition of land through public tender; or (2) a proposed disposal of a property, which constituted a major transaction

Parties

- **Company A** – a Main Board issuer
- **Company B** – another Main Board issuer

Facts

Company A

1. Company A was engaged in manufacturing. It intended to bid for a piece of land in the Mainland from a government authority under a public tender. The land would be used to construct new production facilities. The proposed acquisition would be a possible major transaction for Company A and the terms of the agreement would be subject to shareholders' approval.

2. The government authority had issued the tender notice (掛牌出讓公告) for the land which provided details of the land and other major terms of the tender, including the initial asking price for the bid (掛牌起始價).

3. Company A proposed to seek a mandate from its shareholders for the acquisition before submitting a bid for the land because the government authority would not accept a bid conditional on shareholders' approval. Except the consideration, all major terms of the transaction had been fixed and disclosed in the tender notice. If Company A won the bid, it would be obliged to acquire the land under these terms. It would be impractical for Company A to seek shareholders' approval for the acquisition after the bid was accepted.

4. Under the proposed mandate, Company A's bid would not exceed a maximum price fixed by it. The maximum price was determined taking into account the location and potential value of the land and a recent valuation of the land by a professional valuer appointed by Company A.

Company B

5. Company B's principal businesses included property investment.

6. Company B intended to sell its entire interest in an investment property located in Hong Kong. The proposed disposal would be a possible major transaction for Company B and the terms of agreement would be subject to shareholders' approval.

7. It proposed to seek a prior mandate from its shareholders to sell the property. Under the proposed mandate:

   - The property would be sold to independent purchaser(s) within a fixed period.

   - The consideration would be above a minimum price fixed by Company B. The minimum price was determined taking into account the then market conditions and a recent valuation of the property by a professional valuer appointed by Company B.

8. Company B considered that it would be unduly burdensome to make an agreement for the disposal conditional on shareholders' approval because of the uncertainty and additional time required to complete the transaction, which might affect the selling price of the property. The proposed mandate, if approved by shareholders, would enable it to seize every opportunity to realise its investment in the property quickly in light of the changing market conditions.

Relevant Listing Rules

9. Rule 14.34 states that:

   As soon as possible after the terms of a share transaction, discloseable transaction, major transaction, very substantial disposal, very substantial acquisition or reverse takeover have been finalised, the listed issuer must in each case:—

   …

   (2) publish an announcement in accordance with rule 2.07C as soon as possible. See also rule 14.37.

10. Rule 14.40 states that:

    a major transaction must be made conditional on approval by shareholders.

11. Rule 14.63(2)(a) states that if voting or shareholder approval is required, a notifiable transaction circular must:

    contain all information necessary to allow the holders of the securities to make a properly informed decision.

Analysis

12. Chapter 14 governs an issuer's transactions, principally acquisitions and disposals having material impacts on its financial position. Depending on the size of the transaction, the Rules require the issuer to disclose the terms of the transaction and/or obtain shareholder approval. Shareholders would vote on the agreement having considered its terms.

13. In these cases, there was no transaction and the requirements of Chapter 14 were not triggered. If an agreement for the acquisition/disposal were signed, it would be subject to shareholders' approval under Rule 14.40. The company's shareholders would vote on the agreement based on its terms.

14. There was a question whether the Exchange would accept a prior mandate in lieu of a shareholders' approval on the terms of the agreement for the acquisition/disposal under Chapter 14.

Company A

15. When considering whether to accept a prior mandate in Company A's case, the Exchange noted the following:

- Company A could acquire the land from the government authority only through the public tender. It would be impossible to seek shareholders' approval except by a prior mandate.

- The government authority had fixed and disclosed the timing and major terms (except the consideration) for the tender, and Company A would set out the maximum consideration for the land in its circular to shareholders. There was sufficient safeguard in the proposed mandate and shareholders would be able to make an informed assessment of the acquisition.

Company B

16. The Exchange considered the reason provided by Company B for the proposed mandate for the disposal of the property and whether in the circumstances, it would accept a prior mandate from shareholders in lieu of shareholders' approval of the sale and purchase agreement. However, it did not consider it unduly burdensome or impractical for Company B to make the disposal conditional on shareholders' approval.

Conclusion

17. The Exchange accepted a prior mandate for Company A's proposed transaction but not Company B's proposed disposal.

Whether the Exchange would accept a listed issuer's proposal to seek a prior approval in advance from its shareholders for a disposal of listed investments which constituted a very substantial disposal

Parties

- **Company A** – a Main Board issuer
- **Target** – another Main Board issuer

Facts

1. Company A held listed shares in the Target (**Shares**) representing approximately 20% of the Target's share capital.

2. It was Company A's intention to realise all its investments in the Target subject to market conditions. The disposals would be, in aggregate, a possible very substantial disposal for Company A and therefore subject to shareholders' approval.

3. Company A proposed to seek a mandate from its shareholders for selling the Shares to independent third parties. It asked the Exchange to accept that the mandate would meet the shareholder approval requirement for the disposals under Chapter 14. Under the proposed mandate:

    - The Shares would be sold within a period after the shareholders approved the mandate.

    - The Shares would be sold (i) in the open market on the Exchange and/or (ii) through block trades by entering into placing agreements with reputable investment banks as placing agents. For any block trade, the terms and conditions of the sale would be negotiated on an arms' length basis.

      Company A submitted that it was a common market practice to sell a large quantity of securities through block trades where investment banks would procure independent buyers and close the deal overnight. In light of the substantial amounts of Shares held by Company A, it would be necessary and appropriate for the proposed mandate to cover block trades.

    - The price for selling the Shares in an open market would be no less than a fixed dollar amount which was determined with reference to the market prices of the Shares in the past 12 months. Where Shares were to be sold through a block trade, the Company proposed a limit for the selling price based on the higher of (i) a fixed dollar amount and (ii) a small discount to the average closing price of the Shares for the 5 trading days immediately before the placing agreement.

    - The proceeds would be used by Company A for general working capital.

4. Company A considered the mandate, if approved by shareholders, would provide its directors with flexibility in selling the Shares and enable them to react promptly to changing market conditions. Whether the Shares were to be sold in an open market or through block trades, the transactions would need to be completed within a very short period. It would be impractical to make any such sales conditional on shareholders' approval.

Relevant Listing Rules

5. Rule 14.34 states that:

   As soon as possible after the terms of a share transaction, discloseable transaction, major transaction, very substantial disposal, very substantial acquisition or reverse takeover have been finalised, the listed issuer must in each case:—

   …

   (2) publish an announcement in accordance with rule 2.07C as soon as possible. See also rule 14.37.

6. Rule 14.49 states that:

   a very substantial disposal … must be made conditional on approval by shareholders in general meeting. …

7. Rule 14.63(2)(a) states that if voting or shareholder approval is required, a notifiable transaction circular must:

   contain all information necessary to allow the holders of the securities to make a properly informed decision.

Analysis

8. Chapter 14 governs an issuer's transactions, principally acquisitions and disposals having material impacts on its financial position. Depending on the size of the transaction, the Rules require the issuer to disclose the terms of the transaction and/or obtain shareholder approval. Shareholders would vote on the agreement having considered its terms.

9. Here, there was no transaction and the requirements of Chapter 14 were not triggered. Company A proposed to seek a prior mandate for selling its investments in listed securities to independent third parties. When considering whether to accept such an arrangement, the Exchange noted the following:

   - Company A proposed to sell the Shares on the Exchange. It would be impractical, if not impossible, to seek shareholders' approval except by a prior mandate.

   - The mandate would also cover block trades which were necessary for selling a large quantity of securities. Under the terms of the mandate, block trades would be conducted through reputable investment banks and the selling price would be determined based on the prevailing market price of the Shares subject to the restrictions approved by shareholders. The mandate would not result in undue risks to shareholders.

- Company A proposed thresholds for the selling price of the Share and specified the time period for the disposal. There was sufficient safeguard in the proposed mandate and information for the shareholders to make an informed assessment.

Conclusion

10. Company A's proposed mandate for selling the Shares would meet the shareholder approval requirement.

Whether a listed issuer was required to seek reapproval from its shareholders for changing the terms of a very substantial acquisition after it had been approved by shareholders

Parties

- **Company A** – a Main Board issuer
- **Vendor** – the vendor of the Target
- **Target** – Company A's acquisition target

Facts

1. Company A was in the gaming business.

2. It agreed with the Vendor to acquire the Target (**Agreement**). The Target's main asset was a profit stream from acting as a gaming promoter. Under the Agreement, the Vendor would provide Company A with profit guarantees.

3. The acquisition was a very substantial acquisition for Company A and had been approved by its shareholders.

4. After obtaining shareholder approval but before completing the Agreement, Company A's directors became aware of the adverse effect of the global financial crisis on the Target's profitability. This effect was not considered when the Agreement was signed or when it was approved by the shareholders. The directors and the Vendor agreed to reduce the consideration and the profit guarantees substantially, and to extend the long stop date. Based on these amendments, the acquisition would remain a very substantial acquisition for Company A.

5. Company A considered that no shareholder approval of the amended Agreement was required because:

    a. The amendments would not change the subject matter of the acquisition (i.e. the Target and its profit stream) or the projected yield in percentage terms.

    b. No reasonable shareholder would object to the amendments which would reduce Company A's investment costs.

    c. Company A would remain contractually obliged to complete the acquisition based on the original Agreement even if the shareholders did not approve the amendments.

Relevant Listing Rules

6. Rule 14.40 states that:

   A major transaction must be made conditional on approval by shareholders.

7. Rule 14.49 states that:

   … a very substantial transaction must be made conditional on approval by shareholders in general meeting …

Analysis

8. For an agreement approved by an issuer's shareholders, the issuer may be required to seek prior shareholder approval of an amendment to the agreement, depending on the nature and materiality of the amendment (see FAQ11.4 – No.1).

9. Company A renegotiated material terms of the Agreement. The Exchange considered the proposed amendments to be material changes to the Agreement and, in substance, a new transaction. The shareholders should be given an opportunity to consider whether, in light of the change in the circumstances (i.e. the financial crisis), the amended Agreement was in the interest of the company as a whole and to vote on it.

Conclusion

10. Company A should seek shareholder approval of the amended Agreement.

Whether a listed issuer was required to seek reapproval from its shareholders for changing the terms of a very substantial acquisition after it had been approved by shareholders

Parties

- **Company A** – a Main Board issuer
- **Target** – a company to be acquired by Company A under a very substantial acquisition

Facts

Background

1. Company A entered into an agreement to acquire the Target from a third party vendor (the **Acquisition**). It would settle the consideration by cash and by issuing consideration shares, convertible bonds and promissory notes to the vendor. The Acquisition was a very substantial acquisition.

2. While the Target had a limited operating history, it had recently developed its own energy saving system for business operations. Company A considered that the Acquisition would allow it to diversify into a new line of business with significant growth potential.

3. Company A disclosed in its circular details of the business plans and working capital requirements for the Target in the coming years. It also disclosed its proposal to conduct a placing of new shares and the minimum dollar amount to be raised (the **Placing**). About 90% of the proceeds would be used to finance the cash consideration for the Acquisition and part of the Target's working capital requirements. Under the Acquisition agreement, completion of the Acquisition was conditional on the completion of the Placing (the **Condition**). The pro forma financial information on the enlarged group reflected the impact of the Acquisition and the Placing.

4. Company A's shareholders approved the Acquisition.

5. Company A then entered into agreements with placing agents for the Placing. While the Placing was approved by the shareholders, it was not completed due to adverse market conditions.

Proposed amendment to the Acquisition agreement

6. Company A proposed to postpone the Placing after completion of the Acquisition in light of the deteriorating market conditions. It would sign a supplemental agreement with the vendor to waive the Condition (the **Proposed Amendment**).

7. Company A considered that the Proposed Amendment would be in the interests of the company and its shareholders as a whole. It would not change the consideration, the asset to be acquired or other key terms of the Acquisition, and should not be regarded as a material change to the terms of the Acquisition agreement.

Relevant Listing Rules

8. Rule 14.36 states that

"Where a transaction previously announced pursuant to this Chapter is terminated or there is any material variation of its terms or material delay in the completion of the agreement, the listed issuer must as soon as practicable announce this fact by means of an announcement published in accordance with rule 2.07C. This requirement is without prejudice to the generality of any other provisions of the Exchange Listing Rules and the listed issuer must, where applicable, also comply with such provisions."

9. Rule 14.49 states that

"A very substantial disposal and a very substantial acquisition must be made conditional on approval by shareholders in general meeting…."

Analysis

10. Rule 14.36 ensures that shareholders are notified by the issuer of any material change to the terms of its notifiable transaction. Under Rules 14.36 and 14.49, if the transaction is classified as a major (or above) transaction, the material change should be subject to shareholders' approval.

11. In this case, the Exchange considered that the Proposed Amendment was a material change to the terms of the Acquisition agreement because:

- The shareholders were informed that the Acquisition was conditional on the completion of the Placing, and the cash consideration and a substantial part of the working capital required for the Target's new business would be funded by the Placing. The circular also disclosed how the Acquisition together with the Placing would affect the financial position of Company A. The financing arrangement was material information for the shareholders to decide on how to vote on the Acquisition.

- The Proposed Amendment would remove the Condition so that Company A could complete the Acquisition without the Placing. This would change the financing arrangement for the Acquisition previously presented in the circular. Shareholders should have the right to reconsider whether it is in the interests of Company A and its shareholders as a whole to complete the Acquisition before raising sufficient funds to finance the Acquisition.

Conclusion

12. The Exchange considered that the Proposed Amendment was a material change to the terms of the Acquisition, and should be made conditional on shareholders' approval at general meeting.

Whether the circular and shareholders' approval requirements applied to a disposal of the listed issuer's business by provisional liquidators

Facts

1. A creditor petitioned to wind-up a Main Board issuer incorporated in Bermuda (**Company X**) for its inability to pay debts. The High Court of Hong Kong appointed provisional liquidators to the company.

2. The provisional liquidators agreed to sell Company X's principal business to an independent investor, and would use the proceeds to pay the debts. The sale would be a very substantial disposal.

3. Under the law, completion of the sale was subject to a court order. The provisional liquidators considered that the sale should not require shareholder approval under Chapter 14 because Company X was insolvent and would not have residual assets for distribution to shareholders. The shareholders therefore had no interest left in the company.

Relevant Listing Rules

4. Rule 14.38A states that:

   … A listed issuer which has entered into a major transaction must send a circular to its shareholders …

5. Rule 14.48 states that:

   In the case of a very substantial disposal …, the listed issuer must comply with the requirements for all transactions for major transactions set out in rules 14.34 to 14.37 and 14.38A.

6. Rule 14.49 states that:

   A very substantial disposal … must be made conditional on approval by shareholders in general meeting. …

Analysis

7. Chapter 14 seeks to protect shareholders' interests by giving them the rights to participate in the decision process for material transactions through voting at shareholders' meetings. It does not specifically provide for the case where the issuer is insolvent and its assets have to be liquidated to repay creditors.

8. In this case, the court appointed the provisional liquidators to take control of Company X and arrange for its restructuring. The sale was part of the restructuring process and would take place under a court order. The proceeds would be used to repay creditors. Under the law, creditors' claims ranked higher than shareholders' equity in terms of distribution by Company X. As Company X had insufficient assets to repay the creditors, its shareholders had no interest left in Company X. In these circumstances, the shareholders' interests would not be prejudiced in the absence of a shareholder meeting to approve the sale under Chapter 14.

Conclusion

9. The requirement to despatch a circular and obtain shareholder approval under Rules 14.48 and 14.49 did not apply to the sale. However, Company X should keep shareholders informed of the progress of the sale under Rule 13.09(1).

Whether two shareholders, who had been partners in a project, constituted a closely allied group of shareholders for the purpose of providing a written shareholders' approval for a major transaction

Facts

1. A listed issuer (**Company A**) entered into a transaction which constituted a major transaction under Rule 14.06(3) of the Listing Rules requiring shareholders' approval.

2. Rule 14.44 provides that such shareholders' approval may be obtained either by convening a general meeting of the issuer or by means of the written approval of the transaction by a shareholder or a closely allied group of shareholders who together hold more than 50% of the voting rights at such general meeting. Rule 14.45 sets out the factors which the Exchange will consider in determining whether or not a group of persons is a "closely allied group of shareholders".

3. Company A obtained a written certificate from each of two shareholders together holding over 50% in nominal value of Company A's issued share capital approving the transaction.

4. The two shareholders had been partners in a project.

Analysis

5. The two shareholders had no established trading/business relationship other than as partners in one project in the past. Furthermore, one of the shareholders had no prior history of voting at any of Company A's shareholders' meetings.

Conclusion

6. The two shareholders did not constitute "a closely allied group of shareholders" and, accordingly, a written certificate from them was not acceptable to the Exchange in lieu of a resolution passed at a shareholders' meeting.

Whether the Exchange would waive the general meeting requirement and accept a written shareholders' approval for a very substantial acquisition

Facts

1. A Main Board listed issuer (**Company A**) proposed to form a joint venture company so that the joint venture company could tender for a sizeable development project. Under the relevant Listing Rules, the formation of the joint venture company (the **JVCo**) would constitute a very substantial acquisition (the **Transaction**).

2. Company A submitted an application for a waiver from strict compliance with Rule 14.49 of the Listing Rules so that it could proceed to form the JVCo before a shareholders meeting was held on the ground that the majority shareholders (holding over 50 percent of the voting rights of Company A) would undertake to vote in favour of the resolutions to approve the formation of the JVCo.

3. In support of its application, Company A submitted that:

   a. the Transaction was classified as a very substantial acquisition purely on technical grounds due to the consideration ratio;

   b. the company was not in control of the tender procedures and had submitted this waiver application as soon as it became aware that it would receive an invitation to submit a tender from the project owner;

   c. previous experience suggested that the project owner could make an award within a period ranging from less than three weeks to as long as a few months after the tender deadline;

   d. if the JVCo were to submit a tender conditional upon approval by shareholders at a shareholders' meeting to be held at a future date, the project owner might consider the JVCo's tender unfavourably;

   e. without a waiver being granted, it would be difficult for Company A to participate in tenders for large projects where it needed to form joint ventures with others to share risks and to pool resources together;

   f. Company A would hold a shareholders' meeting to ratify the formation of the JVCo which would give shareholders the opportunity to exercise their voting rights and to express their views at that meeting and that it would not give written shareholders' approval in lieu of holding a general meeting;

g. the majority shareholders of a Company A would vote in favour of the resolutions to be proposed at the shareholders' meeting (which they would undertake to do so) and the resolutions would be carried;

h. Company A could indicate in its announcement and shareholders' circular the intentions of its majority shareholders;

i. if the majority shareholders had intended to vote against the formation of the JVCo, it would not be possible for directors to recommend to the shareholders that the formation of the JVCo be approved. If such an intention were known it would constitute material information requiring disclosure in a shareholders' circular; and

j. Company A believed that the prior indication of the voting position of its majority shareholders in the shareholders' circular would not discourage minority shareholders from attending the general meeting to express and discuss their views on the formation of the JVCo.

Relevant Listing Rules

4. Listing Rule 14.49 provides as follows:

A very substantial disposal and a very substantial acquisition must be made conditional on approval by shareholders in general meeting. No written shareholders' approval will be accepted in lieu of holding a general meeting. The Exchange will require any shareholder and his associates to abstain from voting at the relevant general meeting on the relevant resolution(s) if such shareholder has a material interest in the transaction. Where any shareholder is required to abstain from voting, any vote of shareholders taken at the general meeting on the relevant resolution(s) must be taken on a poll.

Analysis

5. The Transaction fell within the ambit of Listing Rule 14.49.

The Exchange regards the purpose and ambit of Listing Rule 14.49 to be clear and unambiguous. Listing Rule 14.49 requires that a very substantial acquisition must be made conditional on approval by shareholders in general meeting and that no written shareholders' approval would be accepted in lieu of holding a general meeting. Given the potential significant impact of a very substantial acquisition on the issuer, opportunity should be given to shareholders to express their views at the general meeting and to exercise their voting rights at such meeting. Such rights, which are established under the Listing Rules, should be paid due respect, and that strict application of Listing Rule 14.49 was appropriate.

Conclusion

6. The Exchange determined[1] that the circumstances did not warrant the grant of the waiver requested and prior approval by shareholders in general meeting must be obtained for a very substantial acquisition.

[1] This decision was upheld on review.

Whether certain shareholders of a listed issuer had a material interest in a proposed acquisition

Parties

- **Company A** – a Main Board listed company
- **Vendor** - a company listed on an overseas stock exchange
- **Target Company** – a company in which Company A proposed to acquire an interest from the Vendor
- **Mr X** – a director and substantial shareholder of Company A, and a director and chief executive officer of the Vendor. He held approximately 2 per cent of the issued shares of the Vendor and 0.5 per cent of the issued shares of the Target Company
- **Mr Y** – a director and substantial shareholder of Company A, and a director of the Vendor. He held approximately 0.2 per cent of the issued shares of the Vendor

Facts

1. Company A proposed to acquire about a 60 per cent equity interest in the Target Company from the Vendor (the **Proposed Acquisition**). The Proposed Acquisition would constitute a very substantial acquisition for Company A and was subject to shareholders' approval under the Listing Rules.

2. Mr X and Mr Y were directors and substantial shareholders of Company A. At the relevant time, it was also submitted that:

   - Both Mr X and Mr Y were directors of the Vendor. Mr X was also the chief executive officer of the Vendor.
   - Mr X and Mr Y held approximately 2 per cent and 0.2 per cent of the issued shares of the Vendor respectively.
   - Mr X also held approximately 0.5 per cent of the issued shares of the Target Company. (Mr Y did not hold any shares of the Target Company.)

3. Company A submitted that neither Mr X nor Mr Y had a material interest in the Proposed Acquisition because:

   - Neither of them was a party to the Proposed Acquisition, or an associate of either the Vendor or the Target Company.

- The equity interest held by each of Mr X and Mr Y in the Vendor was minimal (ie approximately 2 per cent and 0.2 per cent respectively).

- The consideration for the Proposed Acquisition (representing less than 5 per cent of the Vendor's annual revenue or 1 per cent of the Vendor's market capitalisation) was so insignificant from the Vendor's perspective that neither Mr X nor Mr Y nor their respective associate(s) could derive any material benefit (monetary or otherwise) from the Proposed Acquisition by reason of their minimal shareholding and/or directorship in the Vendor.

- Mr X only held a 0.5 per cent equity interest in the Target Company, which did not form part of the equity interest in the Target Company to be acquired by Company A under the Proposed Acquisition.

- Both Mr X and Mr Y had made full disclosure of their interest in the Proposed Acquisition to the board of directors of Company A (the Board), and had abstained and would continue to abstain from voting on the relevant resolutions in their capacity as directors of Company A.

- The Board had appointed an executive committee to manage the Proposed Acquisition. Mr X and Mr Y were members of the committee but they did not have any voting rights.

- Neither Mr X nor Mr Y participated in any deliberations or decision of the board of directors of the Vendor, or voted in his capacity as director of the Vendor, in connection with the Proposed Acquisition.

Relevant Listing Rules

4. Rule 2.15 provides that:

   Where a transaction or arrangement of an issuer is subject to shareholders' approval under the provisions of the Exchange Listing Rules, any shareholder that has a material interest in the transaction or arrangement shall abstain from voting on the resolution(s) approving the transaction or arrangement at the general meeting.

   Note: For the avoidance of doubt, any provision in the Exchange Listing Rules requiring any other person to abstain from voting on a transaction or arrangement of an issuer which is subject to shareholders' approval shall be construed as being in addition to the requirement set out in rule 2.15.

5. Rule 2.16 provides that:

   For the purpose of determining whether a shareholder has a material interest, relevant factors include:

   (1) whether the shareholder is a party to the transaction or arrangement or a close associate of such a party; and

   (2) whether the transaction or arrangement confers upon the shareholder or his close associate a benefit (whether economic or otherwise) not available to the other shareholders of the issuer.

There is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms. The materiality of an interest is to be determined on a case by case basis, having regard to all the particular circumstances of the transaction concerned.

Note: The references to "close associate" shall be changed to "associate" where the transaction or arrangement is a connected transaction under Chapter 14A.

6. Rule 14.49 provides that:

… a very substantial acquisition must be conditional on approval by shareholders in general meeting. … The Exchange will require any shareholder and his close associates to abstain from voting at the relevant general meeting on the relevant resolution(s) if such shareholder has a material interest in the transaction.

Analysis

7. Rule 2.16 provides a non-exhaustive list of factors to determine whether a shareholder has a material interest for the purposes of the Listing Rules. The Rule also states that there is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms.

8. When determining the materiality of the interests of Mr X and Mr Y in the Proposed Acquisition, the Exchange considered not only their equity interests in the Vendor and the Target Company but also other circumstances of the Proposed Acquisition.

9. In this case, Mr X and Mr Y were not close associates of the Vendor (the counterparty in the Proposed Acquisition). Nevertheless, Mr X and Mr Y had a conflict of interest in the Proposed Acquisition as a result of their position as directors of both Company A and the Vendor. Mr X was also the chief executive officer of the Vendor.

10. The Exchange did not consider that Company X's submission had satisfactorily addressed the conflict of interest issue. Although Mr X and Mr Y had abstained, and would continue to abstain, from voting on the relevant resolutions in their capacity as directors of Company A, they were appointed by the Board as members of an executive committee which managed the Proposed Acquisition. Although Mr X and Mr Y had no voting rights in the committee, they were in a position to exercise influence over the terms of the Proposed Acquisition. Further, the fact that Mr X and Mr Y had abstained from voting on the relevant Board resolutions suggested that their interest in the Proposed Acquisition was considered to be material.

11. In view of the conflict of interest, Mr X and Mr Y each had an interest in the Proposed Acquisition. The Exchange considered that the interest was material and therefore Mr X and Mr Y were required to abstain from voting on the resolution to approve the Proposed Acquisition at the general meeting of Company A under Rules 2.15 and 14.49.

Conclusion

12. Mr X and Mr Y each had a material interest in the Proposed Acquisition and must abstain from voting on the resolution to approve the Proposed Acquisition at the general meeting of Company A under Rules 2.15 and 14.49.

Whether certain shareholders of a listed issuer had a material interest in the issuer's proposal to privatise a listed subsidiary

Parties

- **Company X** – a Main Board listed company
- **Subsidiary** – a GEM listed company and a subsidiary of Company X
- **Company A** – a substantial shareholder of Company X. It was controlled by Individual A.
- **Company B and Company C** – each a substantial shareholder of Company X. They were controlled by a company listed on the Exchange.
- **Individual D, Individual E** – each a director and a shareholder of Company X
- **Relevant Shareholders** – Company A, Company B, Company C, Individual D and Individual E collectively

Facts

1. Company X and certain companies, including Company A, controlled by Individual A (**Group A**) held approximately 65 per cent and 9.9 per cent of the issued shares of the Subsidiary respectively.

2. Company X proposed to privatise the Subsidiary by a scheme of arrangement.

    - Under the scheme, all shares in the Subsidiary excluding those held by Company X and Group A (**Scheme Shares**) would be cancelled in exchange for cash consideration.

    - Company X would also make an offer to the holders of the outstanding options granted by the Subsidiary according to the Takeovers Code.

3. Upon the scheme becoming effective, all Scheme Shares would be cancelled and any outstanding options not exercised on or before the record date would lapse.

4. The proposal was subject to approval of the independent shareholders of the Subsidiary (ie shareholders other than Company X and parties acting in concert with it) under the Takeovers Code. The Relevant Shareholders were parties acting in concert with Company X in relation to the proposal.

5. Upon completion, Company X's shareholding in the Subsidiary would increase to about 90 per cent. The proposal constituted a major transaction for Company X and was subject to shareholder approval at a general meeting of Company X.

6. As some holders of the Scheme Shares or outstanding options were connected persons of Company X, the transactions with them under the proposal constituted connected transactions for Company X.

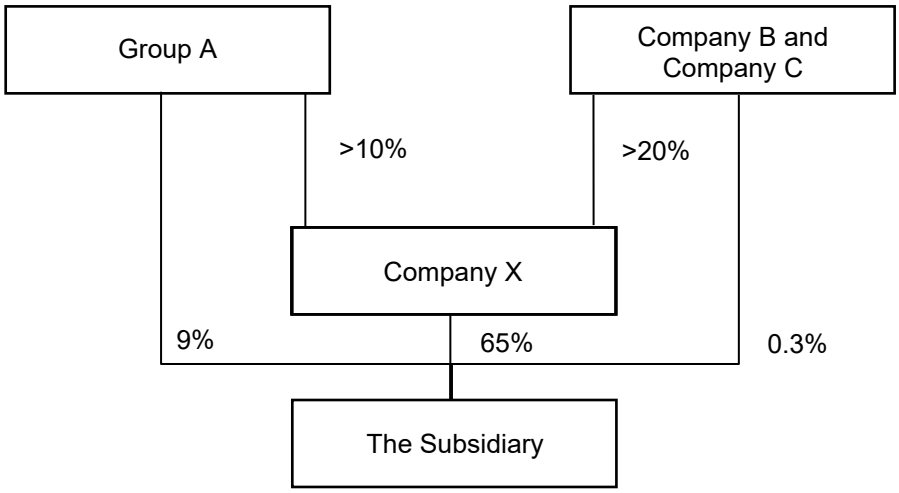
7. Company X would convene a general meeting to seek shareholders' approval of the proposal, which included the transactions with connected persons of Company X. There was a question whether each of the Relevant Shareholders had a material interest in the proposal and was required to abstain from voting on the resolution to approve the proposal at the general meeting of Company X.

Company A, Company B and Company C – substantial shareholders of Company X

8. Company A was wholly owned by Individual A. Group A (which included Company A) held approximately 9.9 per cent of the issued share capital of the Subsidiary (other than those indirect interests in the subsidiary held through Company X). The shares in the Subsidiary held by Group A would not form part of the Scheme Shares and would not be cancelled upon the scheme becoming effective.

9. Company B and Company C were ultimately controlled by a company whose shares were also listed on the Exchange. They together held approximately 0.3 per cent of the issued share capital of the Subsidiary (other than those indirect interests in the Subsidiary held through Company X).

10. The simplified shareholding structure showing the interest of Group A, Company B and Company C in Company X and the Subsidiary before the proposed privatisation is set out below:



Individual D and Individual E – shareholders of Company X

11. Individual D and Individual E were each a director of Company X and the Subsidiary. Individual E was also the chief executive officer of the Subsidiary.

12. Individual D held some shares in the Subsidiary which represented less than 0.0001 per cent of the Subsidiary's issued share capital.

13. Individual E did not hold any shares in the Subsidiary but held a number of outstanding options. The shares to be issued upon exercise of the vested outstanding options represented approximately 2 per cent of the Subsidiary's issued share capital.

Relevant Listing Rules

14. Rule 2.15 provides that:

> Where a transaction or arrangement of an issuer is subject to shareholders' approval under the provisions of the Exchange Listing Rules, any shareholder that has a material interest in the transaction or arrangement shall abstain from voting on the resolution(s) approving the transaction or arrangement at the general meeting.
>
> *Note: For the avoidance of doubt, any provision in the Exchange Listing Rules requiring any other person to abstain from voting on a transaction or arrangement of an issuer which is subject to shareholders' approval shall be construed as being in addition to the requirement set out in rule 2.15.*

15. Rule 2.16 provides that:

> For the purpose of determining whether a shareholder has a material interest, relevant factors include:
>
> (1) whether the shareholder is a party to the transaction or arrangement or a close associate of such a party; and
>
> (2) whether the transaction or arrangement confers upon the shareholder or his close associate a benefit (whether economic or otherwise) not available to the other shareholders of the issuer.
>
> There is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms. The materiality of an interest is to be determined on a case by case basis, having regard to all the particular circumstances of the transaction concerned.

16. Rule 14.40 provides that:

> In the case of a major transaction, the listed issuer must comply with the requirements for all transactions and for discloseable transactions set out in rules 14.34 to 14.39. In addition, a major transaction must be made conditional on approval by shareholders.

17. Rule 14.46 provides that:

> The Exchange will require any shareholder and his associates to abstain from voting at the relevant general meeting on the relevant resolution(s) if such shareholder has a material interest in the transaction. …

18. Rule 14A.36 provides 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.

Analysis

19. Rule 2.16 provides a non-exhaustive list of factors to determine whether a shareholder has a material interest for the purposes of the Listing Rules. The Rule also states that there is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms.

20. When determining the materiality of an interest, the Exchange will need to consider all the circumstances of the proposed transaction.

Company A

21. Company X submitted that Company A as a substantial shareholder of Company X did not have a material interest in the proposal as the 9 per cent shareholding in the Subsidiary directly held by Group A would not form part of the Scheme Shares and Group A would not be entitled to any payment of the cash consideration.

22. The Exchange did not agree. As set out in Rule 2.16, a material interest may not necessarily be defined in monetary or financial terms.

23. Under the proposal, there was a specific arrangement between Company X and Group A that the shares in the Subsidiary held by Group A would be excluded from the scheme and would not be cancelled upon the scheme becoming effective. The Exchange considered that Group A, as a party to this arrangement, had a material interest in the proposal. Accordingly, Company A must abstain from voting at the general meeting of Company X.

Company B and Company C

24. Company B and Company C each held a substantial shareholding in Company X, which owned a 65 per cent interest in the Subsidiary. Although these companies were holders of the Scheme Shares, their direct interest in the Subsidiary (in aggregate about 0.3 per cent) was immaterial compared to that held through Company X. The Exchange accepted that as substantial shareholders of Company X, the interest of Company B and Company C in the proposal was in alignment with the interest of other shareholders of Company X. Therefore, Company B and Company C would not be regarded as having a material interest in the proposal.

25. The Exchange also noted that the connected transactions with Company B and Company C would be exempt from the independent shareholders' approval requirement under the de minimis provisions in Chapter 14A of the Listing Rules.

26. Company B and Company C would not be required to abstain from voting at the relevant general meeting of Company X.

Individual D

27. The Exchange agreed that Individual D did not have a material interest in the proposal because the amount of Scheme Shares he held was insignificant. He had also undertaken to donate his Scheme Shares to a charitable body and there was not any transaction between Company X and him under the proposal. Accordingly, he would not be required to abstain from voting at the relevant general meeting of Company X.

Individual E

28. The proposal involved privatising the Subsidiary. Individual E was then the chief executive officer of the Subsidiary and held a number of outstanding options. His interest in the proposal was different from the other shareholders of Company X and was regarded as material in light of the circumstances.

29. Under the proposal, the transaction between Company X and Individual E constituted a connected transaction that required independent shareholders' approval under Chapter 14A of the Listing Rules. Therefore, when Company X put forward a resolution to seek shareholders' approval of the proposal which included the transaction with Individual E, Individual E must abstain from voting.

Conclusion

30. The Exchange determined that Company A and Individual E had a material interest in the proposal and must abstain from voting on the resolution to approve the proposal at the general meeting of Company X.

Shareholders' approval requirement for notifiable transactions

1. A listed issuer proposes to vary certain terms of a major transaction after it has been approved by its shareholders. Is the listed issuer required to seek reapproval from its shareholders on the revised terms?

If the change in terms of the transaction is material, it would in substance be a new transaction and therefore must be reapproved by shareholders.

MB Rule 14.40
GEM Rule 19.40
First released: November 2008; last updated: May 2024

HKEX Guidance Letter
HKEX-GL116-23

October 2023 (Last updated in June 2024)

Disclosure of the basis of consideration and business valuations in notifiable transactions

I. Background

1. Under current Rules and guidance[1], when an issuer conducts an acquisition or disposal that constitutes a notifiable transaction, it must disclose the basis for determining the consideration and the terms of the transaction. Where the consideration (or other material terms) of the transaction is primarily based on an independent business valuation of the target (**Transaction Target**), details of the valuation must be disclosed in the transaction circular.

Published guidance on directors' duties in corporate transactions

2. In May 2017, the Securities and Futures Commission (**SFC**) issued a Guidance note on directors' duties in the context of valuations in corporate transactions[2] (**SFC Guidance Note**). The SFC Guidance Note advises directors to carry out independent and sufficient investigation and due diligence on the Transaction Targets, and provides guidance on the circumstances where the directors should consider the need to appoint an independent valuer. These include: (i) where the directors do not have sufficient experience or expertise in the target's business or in valuation; (ii) the target's business is new or still in its infancy; (iii) the information provided in respect of the target's business requires professional advice or professional scrutiny in order to properly assess the merits of the proposed transaction; (iv) the size of the target relative to that of, or its significance to, the issuer; (v) the risks involved in the transaction or the complexity or nature of the transaction; or (vi) where any director of the acquiring company has an actual or potential conflict of interest in the proposed transaction.[3]

3. In July 2019, the SFC published a Statement on the Conduct and Duties of Directors when Considering Corporate Acquisitions or Disposals. The statement outlines recurring types of misconduct related to acquisitions and disposals that have given rise to concerns, including corporate transactions where the issuer either did not obtain a valuation of the Transaction Target when the circumstances suggested it would be appropriate, or the issuer relied on a valuation when reliance on the valuation was imprudent.

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1 See Main Board Rule 14.58(5) / GEM Rule 19.58(6) and FAQ11.5 – No.1.

2 Along with the guidance to directors, the SFC also issued circulars to financial advisers and valuers in relation to the expected standard of work on valuations in corporate transactions.

3 The SFC Guidance Note also provides guidance on considerations for engaging a valuer, including assessments on the valuer's independence and qualification, and the scope of the valuer's mandate.

II. Purpose of this guidance letter

4. In our vetting of issuers' transaction circulars, we identified cases where we were concerned that the terms of the transaction (including the consideration) may not be fair and reasonable to the issuer and its shareholders as a whole. Where the consideration was primarily based on an independent valuation, we found that the disclosure about the valuation was insufficient for investors to understand how the valued amount was derived and accordingly, the basis for the consideration. This falls short of the general standard of disclosure, which requires that the information contained in an issuer's circular must be accurate and complete in all material respects and not be misleading or deceptive, and where shareholders' approval is required, the circular should contain all information necessary to allow shareholders to make a properly informed decision[4].

5. This letter provides guidance on recommended disclosure of business valuation which forms a primary factor in the determination of the consideration (see section III(a)). It should be read in conjunction with the SFC guidance materials.

6. This letter also provides guidance on disclosure of the basis of consideration for notifiable transactions, regardless of whether an independent valuation is disclosed (see section III(b)).

III. Guidance

(a) Disclosure of business valuation which forms a primary factor in the determination of the consideration

General

7. An issuer should adequately explain the basis for determining the consideration to enable its shareholders to assess whether the terms of a transaction are fair and reasonable. When it conducts a transaction under the circumstances set out in paragraph 1, its circular should contain the valuation report of the Transaction Target or a summary that fairly presents the views and analysis of the valuer and all material factors contained in the report.

8. In general, the valuation report (or the summary of it) should contain information in line with generally accepted valuation standards (e.g. the International Valuation Standards) and include, among others:

   (i) the valuation approach(es) and method(s) used by the valuer and the reasons for their selection;
   (ii) the scope of work performed by the valuer, any limitation thereon and the reasons for such limitation;
   (iii) the nature and source of information relied upon;
   (iv) the key inputs and assumptions, and how they were determined and translated into the appraised value;
   (v) the appraised value ascribed to the Transaction Target and the principal reasons for the conclusions reached;
   (vi) the effective date of the valuation; and
   (vii) the identity, qualification and independence of the valuer.

[4] Main Board Rules 2.13 and 14.63 / GEM Rules 17.56 and 19.63.

9. In our review, we have noted that disclosure in some issuers' circulars was overly general and simplistic, particularly in disclosure about valuation methods, key inputs and assumptions used in the valuations.

Valuation approaches and methods

10. Issuers may use different valuation approaches to assess the valuations of Transaction Targets. Common valuation approaches include the income approach, market approach, cost approach and asset-based approach. Each of these approaches has different methods of application.

11. The valuation approaches and methods selected by the valuer and the reasons for their selection should be clearly disclosed and discussed in the valuation report. For example:

- When applying the discounted cash flows (**DCF**) method to value a start-up target company, the issuer should explain how the use of the DCF method was appropriate in the absence of a historical track record to substantiate the forecasts.

- When applying the market approach to value a target company engaging in a novel or innovative industry, the issuer should explain how the use of the market approach is appropriate in the absence of similar or comparable companies.

12. If the appraised value is different from the base value computed from the valuation method selected by the valuer, the report should include a reconciliation of such difference[5].

13. Where more than one valuation approach and method is used by the valuer, the report should also include the valuer's process in analysing the values derived from different valuation approaches and methods and how they contribute to the final appraised value.

Key inputs and assumptions

14. To assist shareholders to understand the valuation, the issuer should explain, with detail and in specific terms, the key assumptions and valuation inputs.

Market approach

15. Where the market approach is used, the valuation report should contain sufficient information on the criteria used to select market comparables[6]. This would include:

- the key inputs such as the financial information of the Transaction Target, the pricing multiples (e.g. revenue/ earning/ EBITDA/ book value multiples) used in the computation process and the rationale for using these pricing multiples;

- a list of market comparables and the bases for compiling this list. The report should set out the selection criteria (including quantitative benchmarks) for the comparables and the reasons for using those criteria. If any companies or transactions that meet the selection criteria are excluded, the bases for such exclusion should be justified and clearly stated;

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5 For example, the discount applied to the base value of the Transaction Target for lack of marketability, or the discount for lack of control in an acquisition of a non-controlling interest of the Transaction Target (or conversely, the control premium).

6 They can be publicly-traded comparables or comparable transactions.

- relevant details of the market comparables selected (e.g. the nature and location of their principal businesses and financial information such as revenue, profits, net asset value and market capitalisation/transaction consideration) to reflect that the selection criteria were consistently applied and the market comparables are appropriate and exhaustive; and

- any adjustments made for differences between the Transaction Target and the market comparables and how they were determined.

16. Set out below are some examples of cases reviewed where the disclosure was inadequate and could not demonstrate that the selection bases were appropriate:

- The description of the selection criteria was generic. For example, the report disclosed that comparable companies were selected on the basis that they are "mostly" or "mainly" engaged in certain businesses without providing any quantitative benchmark such as the percentage of revenue or profits attributable to the relevant business segment.

- There was limited explanation as to why certain companies that met the selection criteria were considered as outliers and excluded from the list of market comparables. For example, the report simply disclosed that certain companies were excluded as their price earnings multiples were "significantly higher or lower than" the other comparables. There was no disclosure of the identities and price earnings multiples of those companies to support the basis for excluding them from the list of market comparables.

Income approach

17. For a DCF valuation, the Rules specifically require, among others, disclosure of all the principal assumptions upon which the underlying cash flow forecast is based.[7] As a general principle, the assumptions must be specific rather than general, and they should draw the shareholders' attention to, and where possible quantify, those uncertain factors which could materially disturb the ultimate achievement of the forecast. It would not be acceptable to make assumptions about the general accuracy of the estimates made in the profit forecast, or matters which the directors, by virtue of their particular knowledge and experience in the business, are best able to take a view in or are able to exercise control over.[8]

18. In some cases reviewed, the valuation report disclosed the definition of the DCF method and the formulae used, and generic assumptions made for the financial projections. There was limited information about the key quantitative inputs such as the discount rate and the terminal growth rate (if a terminal value is applied to the cash flows beyond the forecast period), and the specific assumptions in respect of the Transaction Target. As a result, shareholders cannot properly assess the fairness and reasonableness of the terms of the transaction.

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7 Under Main Board Rule 14.61 / GEM Rule 19.61, any valuation of assets (except for property interests or businesses) acquired by an issuer based on discounted cashflows or projections of profits, earnings or cashflows is regarded as a "profit forecast". Main Board Rules 14.60A, 14.66(2) and Paragraph 29(2) of Appendix D1B / GEM Rules 19.60A, 19.66(10) and Paragraph 29(2) of Appendix D1B require (i) a report from the issuer's auditors or reporting accountants on their review of the accounting policies and calculations for the profit forecast; and (ii) a confirmation from the directors or the financial advisers that the forecast has been made by the directors after due and careful enquiry.

8 Main Board Rule 11.19 / GEM Rule 14.31

19. We consider that the disclosure should include, among others:

- the key, specific assumptions underlying the financial projections, in particular quantitative assumptions (including, without limitation, revenue growth rates, the gross profit or EBITDA margins, changes in major expenses of the Transaction Target during the forecast period and its plan for capital expenditure) and the supporting rationale. It would not be sufficient to include merely qualitative or narrative statements without specific quantitative disclosures of the relevant figures;

- the key inputs (e.g. the discount rate and terminal growth rate) to the valuation and how they were determined;

- a narrative of the DCF model that describes how the key inputs are applied to the financial projections to arrive at the base value of the Transaction Target. Where the final appraised value is different from the base value, the report should also include a reconciliation of such difference;

- where appropriate (for example, where the Transaction Target's income statement items are projected to be significantly improved compared to its historical trend or the Transaction Target's projected profit margin is significantly higher than that of the industry peers), the Exchange has the discretion to request the issuer to explain the rationale behind the assumptions with basis and disclose the key projected figures such as projected revenues, operating costs and profits. The issuer should also disclose the computation process showing how the financial projections and the key inputs are translated into the base value of the Transaction Target; and

- a sensitivity analysis if changes in any key assumptions or inputs are likely to materially affect the valuation.

Cost approach

20. We identified insufficient disclosure about key valuation inputs in some cases reviewed. We consider that the report should contain: (i) the quantitative inputs used to determine the gross current replacement or reproduction cost (i.e. costs that would be required to replace or reproduce the assets of equivalent utility e.g. material and labour costs, and other associated costs such as transportation and installation costs); (ii) the amount of depreciation adjustment made to the gross current replacement or reproduction cost to account for the physical and economic obsolescence and any technical deficiency, and (iii) the computation process for the final depreciated replacement or reproduction cost.

Asset-based approach

21. Where the asset-based approach is used, the valuation report sets out the appraised value for each asset and liability of the Transaction Target, their book values and the differences between the two. The report should disclose the key quantitative inputs and assumptions used in the calculations of these appraised values and the computation process, and where applicable, it should provide separate valuation reports for these assets. Where there are material differences between the book values and appraised values, the report should also explain the differences.

(b) Disclosure of the basis of determining the consideration regardless of whether an independent valuation is obtained

22. An issuer should provide an adequate explanation of the basis for determining the consideration by disclosing in the transaction announcement sufficient and objective information with quantitative inputs and analysis to substantiate how the consideration was arrived at. For instance, where the consideration is not primarily based on an independent valuation, it would not be sufficient if the issuer simply disclosed that the consideration is determined with reference to the historical performance and future prospects of the Transaction Target. The issuer should provide adequate and relevant disclosure (both quantitative and qualitative) of the factors that are key to the determination of the consideration. Examples include the historical and expected financial and operational performance of the Transaction Target such as its revenue growth rate, gross profit/ EBITDA margin, sale volume, market share and production capacity and efficiency.

23. Further, the explanation should also include disclosure of quantitative inputs and assumptions referencing, where applicable, our guidance in part (a) above. For example:

- where the consideration of a transaction is determined with reference to, among others, pricing multiples derived from market comparables, the issuer should make adequate disclosure on the relevant pricing multiples, why such pricing multiples were relevant and the selection criteria for the market comparables (see paragraphs 15 and 16); or

- if an issuer discloses a forecast on the Transaction Target's net profits or losses to support the basis for the consideration or other terms of the transaction, it should disclose, with detail and in specific terms, the key assumptions (including quantitative assumptions) for the forecast[9] and the supporting rationale (see paragraphs 17 to 19).

IV. Glossary

"appraised value" – an opinion of the value of an asset or a business at a specified date given by a valuer

"asset based approach" – a valuation approach which estimates the value of a business as its adjusted net asset value, i.e. after adjusting each asset and liability of the business to their respective appraised values

"base value" – the value of an asset or a business directly computed from a valuation method. A valuer would apply valuation premiums, discounts and/or other adjustments (where appropriate) to the base value to arrive at the appraised value

"cost approach" – a valuation approach which estimates the value of an asset or a business by calculating its gross current replacement or reproduction cost and subtracting the estimated depreciation to reflect its physical deterioration and other forms of obsolescence

"discount rate" – the rate at which the financial projections are discounted to their present values. It should reflect the time value of money and the risks associated with the financial projections and future operations of the asset or business

[9] Main Board Rules 14.60A, 14.66(2) and Paragraph 29(2) of Appendix D1B / GEM Rules 19.60A, 19.66(10) and Paragraph 29(2) of Appendix D1B also require (i) a report from the issuer's auditors or reporting accountants on their review of the accounting policies and calculations for the profit forecast; and (ii) a confirmation from the directors or the financial advisers that the forecast has been made by the directors after due and careful enquiry.

"income approach" – a valuation approach which estimates the value of an asset or a business by reference to the value of income, cash flows or cost savings generated by the asset or business based on discounting future cash flows to present value

"market approach" – a valuation approach which estimates the value of an asset or a business by comparing it with comparable assets or companies for which price information is available

"terminal value" – where an asset or a business is expected to generate cash flows beyond the forecast period, the value of the asset or business at the end of that period, i.e. the sum of present values of its expected future cash flows beyond the forecast period, valued at the end of the forecast period

"valuation approach and method" – a valuation approach generally refers to the manner in which the valuation task is undertaken in order to determine the value of an asset or a business, while a valuation method generally refers to the particular procedure of technique applied or used

Whether the Exchange would waive the profit forecast requirements in respect of a valuation report on the disposal target disclosed in the listed issuer's announcement and circular for the disposal

Parties

- **Company A** – a PRC issuer listed on the Main Board
- **Purchaser** – a company listed on a PRC exchange
- **Parent** – the ultimate controlling shareholder of each of Company A and the Purchaser
- **Target** – a subsidiary of Company A proposed to be sold to the Purchaser

Facts

1. Company A proposed to sell the Target to the Purchaser in return for new A shares to be issued by the Purchaser (**Transaction**). This was a major and connected transaction for Company A.

2. Since the Transaction involved a transfer of state-owned assets, the PRC regulations required the Purchaser to engage an appraiser to prepare a valuation report on the Target to determine the consideration. The valuation was partly based on the projections of the Target's earnings. A subsidiary of the Parent (but not Company A) would indemnify the Purchaser for any shortfall in the Target's profits compared to the forecasted profits in the valuation report.

3. Company A would disclose the Target's valuation prepared by the appraiser and the basis for determining the consideration in its announcement and circular for the Transaction.

4. As the valuation was based on projections of the Target's earnings, Company A would need to comply with the disclosure and reporting requirements on profit forecasts under the Rules. It requested the Exchange to waive these requirements because:

    a. It was the Purchaser, and not Company A, which was obliged to prepare the valuation report.

    b. Company A was not involved in preparing the report, except for providing the Purchaser with historical financial information. The accounting principles and policies used by the appraiser differed from those used by Company A.

c. While the consideration was based on the valuation report under PRC regulations, Company A's board had considered other factors when assessing the Transaction, including the historical earnings and dividend distributions of the Target and Company A.

d. The Target would cease to be part of Company A after the Transaction so the profit forecast was irrelevant to its future financial position.

e. Therefore, it would be unduly burdensome for Company A to comply with the requirements.

Relevant Listing Rules

5. Rule 14.61 defines a "profit forecast" to mean:

> … any forecast of profits or losses, however worded, and includes any statement which explicitly or implicitly quantifies the anticipated level of future profits or losses, either expressly or by reference to previous profits or losses or any other benchmark or point of reference. It also includes any profit estimate, being any estimate of profits or losses for a financial period which has expired but for which the results have not yet been published. Any valuation of assets (other than land and buildings) or businesses acquired by a listed issuer based on discounted cash flows or projections of profits, earnings or cash flows will also be regarded as a profit forecast.

6. Rule 14.62 states that if an announcement contains a profit forecast for the issuer or a company which is or is proposed to become its subsidiary, the issuer must provide the Exchange with the following no later than the publication of the announcement:

(1) details of the principal assumptions, including commercial assumptions, upon which the forecast is based;

(2) a letter from the listed issuer's auditors or reporting accountants confirming that they have reviewed the accounting policies and calculations for the forecast and containing their report; and

(3) a report from the listed issuer's financial advisers confirming that they are satisfied that the forecast has been made by the directors after due and careful enquiry. If no financial advisers have been appointed in connection with the transaction, the listed issuer must provide a letter from the board of directors confirming they have made the forecast after due and careful enquiry.

7. Rules 14.66(2) and 14A.70(13) state that a circular relating to a major transaction/ connected transaction must contain information in paragraph 29(2) of Appendix 1B if there is a profit forecast.

8. Rule 14A.68(7) states that a connected transaction announcement must contain the information set out in rule 14.62 if the announcement contains a profit forecast of the listed issuer's group or a company which is, or will become, the listed issuer's subsidiary.

9. Paragraph 29(2) of Appendix 1B states that

> … Where a profit forecast appears in any listing document, it must be clear, unambiguous and presented in an explicit manner and the principal assumptions, including commercial assumptions, upon which it is based, must be stated. The accounting policies and calculations for the forecast must be examined and reported on by the reporting accountants or auditors, as appropriate, and their report must be set out. The financial adviser must report in addition that they have satisfied themselves that the forecast has been stated by the directors after due and careful enquiry, and such report must be set out. …

Analysis

10. The reason for preparing the Target's valuation was to comply with the PRC regulations. Company A was not involved in preparing the valuation report. This was different from the circumstances contemplated under Rules 14.62 and 14A.68(7) which assume that the issuer's directors made the forecast. Company A had practical difficulty in complying with the requirements.

Conclusion

11. The Exchange waived the requirements.

Whether the Exchange would waive the circular requirement for a major transaction

Parties

- **Company A** – a Main Board issuer
- **Company B** – another Main Board issuer and a non-wholly owned subsidiary of Company A

Facts

1. Company A recently announced a disposal of its interests in Company B (**Disposal**). The Disposal did not require shareholders' approval, and would be completed when the parties obtained the necessary regulatory approvals. Upon completion, Company B would cease to be a subsidiary of Company A.

2. Company B now proposed to acquire a target company (**Acquisition**) from certain independent third parties, which would be a very substantial acquisition for Company B. It would also be a major transaction for Company A as Company B was still a subsidiary of Company A.

3. Company A submitted that the Disposal and the Acquisition were separate transactions. Completion of the Disposal was expected to take place before Company B issued its circular and the notice of general meeting for the approval of the Acquisition.

4. Company A requested a waiver from the circular requirement for the Acquisition because:

   - Company B would no longer be Company A's subsidiary upon completion of the Disposal. Information about the Acquisition and the target company would be irrelevant to Company A and its shareholders.

   - Company A would not convene a general meeting for the approval of the Acquisition as its parent company would provide a written approval of the transaction according to Rule 14.44. The circular, if required, would be issued to Company A's shareholders for information only.

Relevant Listing Rules

5. Rule 14.38A requires that:-

   "… a listed issuer which has entered into a major transaction must send a circular to its shareholders and the Exchange and arrange for its publication in accordance with the provisions of Chapter 2 of the Exchange Listing Rules."

Analysis

6. Under Chapter 14, an issuer proposing a material transaction must issue a circular containing all information that is necessary for its shareholders to make an informed assessment of the assets to be acquired or disposed of and the impact of the transaction on the issuer.

7. Having considered the circumstances of this case, the Exchange agreed that it would be unduly burdensome to require Company A to issue a circular for the Acquisition as required under the Rules if at that time Company B was no longer a subsidiary of Company A.

Conclusion

8. The Exchange agreed to grant the waiver to Company A on the basis that the Disposal would be completed before Company B issued its circular for the Acquisition.

Whether the Exchange would waive the requirements for disclosing certain information of the counterparties and the assets to be acquired under a discloseable transaction

Parties

- **Company A** – a Main Board listed issuer
- **Vendors –** third parties independent from Company A

Facts

1. Company A was principally engaged in hotel investment and operation. It intended to acquire a building situated in Hong Kong (the **Target Property**) for redevelopment into a hotel property. The Target Property comprised a number of residential and commercial units owned by various Vendors.

2. Company A submitted that it had entered into provisional sale and purchase agreements with some of the Vendors for acquiring their units in the Target Property (the **Acquisitions**), which in aggregate constituted a discloseable transaction.

3. Rules 14.58(2), 14.60(1) and 14.60(2) requires an announcement for a notifiable transaction to contain, among other things, a description of the principal business activities of the counterparty if it is a company or entity, the general nature of the transaction, and brief details of the assets being acquired including the name of any company or business or the actual assets or properties where relevant.

4. Company A applied for a waiver from the above Rules so that it would not be required to disclose the following information (the **Relevant Information**) in its announcement for the Acquisitions:

    - the principal business activities of the Vendors which are companies;
    - the name and address of the Target Property and the units subject to the Acquisitions;
    - the conditions precedents for completion of the Acquisitions.

5. It proposed to make the following alternative disclosure in the announcement:

    - the Vendors are individuals and companies which are independent of Company A and its connected persons;
    - the district where the Target Property is located and the gross area of the units it proposed to acquire; and

- a statement that completion of the Acquisitions is subject to the satisfaction of a number of conditions.

6. Company A submitted that the terms of each Acquisition were determined after arm's length negotiation between Company A and the Vendor. As it was uncertain whether the Acquisitions could proceed to completion and Company A was still negotiating with other Vendors for acquiring the remaining units in the Target Property, the Relevant Information was commercially sensitive. Disclosure of the information at this stage would be prejudicial to the interests of Company A and would affect the on-going negotiations with other Vendors.

7. Company A considered that with the alternative disclosure, the announcement would provide sufficient information for investors to appraise the Acquisitions. It would also publish a further announcement to disclose the Relevant Information upon completion of the Acquisitions.

Relevant Listing Rules

8. Rule 14.58 provides that:

"The announcement for a share transaction, discloseable transaction… must contain at least the following information:

(1) ...

(2) a description of the principal business activities carried on by the listed issuer and a general description of the principal business activities of the counterparty, if the counterparty is a company or entity; …"

9. Rule 14.60 provides that:

"In addition to the information set out in rule 14.58, the announcement for a discloseable transaction… must contain at least brief details of the following:

(1) the general nature of the transaction …

(2) brief details of the asset(s) being acquired or disposed of, including the name of any company or business or the actual assets or properties where relevant …"

Analysis

10. Chapter 14 governs an issuer's transactions, principally acquisitions and disposals having material impacts on its financial position. Depending on the size of the transaction, the Rules require the issuer to disclose the terms of the transaction and/or obtain shareholder approval.

11. When deciding whether to grant a waiver, the Exchange will take into account the circumstances and reasons outlined in the waiver application and all other relevant information supplied by the issuer.

12. The Exchange considered that concerns about commercial sensitivity of the details of a transaction should not override the disclosure obligations of the issuer where the information was material to investors. When assessing Company A's waiver application, the Exchange took into account the following factors:

a. The Acquisitions constituted a discloseable transaction only and was not significant to Company A.

b. The alternative disclosure would allow investors to understand the nature of the Acquisitions. The waiver would not result in an omission of material information in the initial announcement for the Acquisitions.

c. Disclosure of the Relevant Information at this stage might be prejudicial to the interests of Company A.

Conclusion

13. The Exchange granted the waiver to Company A.

Note: With effect from 1 October 2019, Rule 14.58(2) also requires the announcement of a notifiable transaction to disclose the identity of the counterparty.

Whether the Exchange would waive the requirement for disclosing the consideration for certain technology and patent to be acquired by the listed issuer under a discloseable transaction

Parties

- **Company A** – a Main Board listed company
- **Company B** – a third party independent of and not connected with Company A or any of its connected persons

Facts

1. Company A was principally engaged in providing semiconductor fabrication services and solutions to customers.

2. In addition to its internal research and development team to develop new process technologies, Company A also relied on other technology partners to advance its portfolio of process technologies. In the past, it had entered into agreements with third parties to acquire technology, patents and licences to enable it to manufacture advanced wafers for customers.

3. Company B's principal activity was to supply hardware, software and information technology services and to develop and implement e-business solutions.

4. Company A and Company B proposed to enter into a technology licensing agreement under which Company B agreed to license certain specific semiconductor technology (**Technology**) to Company A for its wafer foundry service.

5. The total consideration for the Technology (**Consideration**) under the Agreement would be funded by Company A's internal resources. The Technology would be recorded as an acquired intangible asset in Company A's accounts.

6. The Transaction constituted a discloseable transaction for Company A.

7. Under Rule 14.58(4), the issuer must disclose the consideration for the transaction in its announcement. Company A applied for a waiver from disclosing the Consideration in the announcement for the following reasons:

   - It was a normal business practice in the semiconductor wafer foundry industry not to disclose the consideration for technology licensing arrangements.

   - The Technology was one of the most advanced technologies of its kind globally. Based on Company A's information, Company B was the only source of such advanced technology available for commercial production and licensing to Company A. Company B had explicitly required that the Consideration, being an extremely commercially sensitive piece of information for Company B, must not be disclosed.

   - Disclosure of the Consideration would result in the loss of significant potential licensing opportunities for Company A and hence would have a significant adverse impact on its future business development and would not be in the interests of Company A and its shareholders as a whole.

   - The Consideration was arrived at after arm's length negotiation between Company A and Company B, and the agreement was negotiated and entered into by the parties in accordance with customary business practice. Company A had considered a number of factors, including the type and degree of development of the Technology, the supply of and market demand for it, whether the Consideration would achieve competitive pricing of wafers produced using the Technology and the overall long term profitability for Company A as a result of using it. Company A's directors, including independent non-executive directors, were of the opinion that the terms of the Agreement were fair and reasonable and were in the interests of its shareholders as a whole.

8. Company A proposed to include the following alternative disclosure in the announcement instead of the value of the Consideration:

   - The unaudited net change in the gross value of Company A's acquired intangible assets in the relevant financial year which indicated the aggregate value of intangible assets (including the Technology) acquired by it in that year.

   - The Transaction constituted a discloseable transaction (i.e. a transaction where any percentage ratio under Rule 14.07 was 5% or more, but less than 25%). Company A would disclose its latest published consolidated total assets and its total market capitalisation as at the date of the Agreement. The information would give an indication of the range of values for the Consideration by reference to the asset ratio and the consideration ratio.

Relevant Listing Rules

9. Rule 14.58 provides that:

> The announcement for a share transaction, discloseable transaction, major transaction, very substantial disposal, very substantial acquisition or reverse takeover must contain at least the following information:
>
> (1) …
>
> (4) the aggregate value of the consideration, how it is being or is to be satisfied and details of the terms of any arrangements for payment on a deferred basis. If the consideration includes securities for which listing will be sought, the listed issuer must also include the amounts and details of the securities being issued;
>
> (5) …
>
> …
>
> (Rule 14.58 was amended on 1 October 2019 and 11 June 2024 respectively. See Note below.)

Analysis

10. Rules 14.58 to 14.60 set out the minimum disclosure requirements for announcements of different types of notifiable transactions. Notwithstanding this, an issuer must observe the general principle under Rule 2.13 that the information contained in its announcement must be accurate and complete in all material respects and not be misleading or deceptive.

11. Issuers are expected to exercise all reasonable care to ensure full compliance with the Listing Rules. The Exchange will not grant waivers to issuers, except where the Listing Rules already contemplate granting waivers under certain circumstances or where the Exchange is satisfied that there are exceptional circumstances warranting a waiver. The "Guide on Applications for Waivers and Modifications of the Listing Rules" available on the HKEx website sets out a non-exhaustive list of factors that the Exchange will generally consider when assessing the merits of a waiver application.

12. When deciding whether to grant a waiver, the Exchange will take into account the circumstances and reasons outlined in the waiver/modification request and all other relevant information supplied by the listed issuer.

13. Company A applied for specific disclosure relief in respect of the value of the Consideration due to the commercial sensitivity of the information in the semiconductor wafer foundry industry.

14. The Exchange considered that concerns about commercial sensitivity of the terms of a transaction should not override the disclosure obligations of the issuer where the information was material to investors. When assessing Company A's waiver application, the Exchange also took into account:

    - Company A's submission that there was a limited number of suppliers for the technologies in the specialised industry, and Company B was the only source of the Technology available for commercial production and licensing to Company A.

    - The Transaction constituted a discloseable transaction only and was not significant to Company A. The unaudited gross value of intangible assets acquired by Company A in the relevant financial year, which included the Technology, represented less than 5% of the latest published consolidated total assets of Company A.

    - The alternative disclosure included: (i) the aggregate value of the Technology and other similar intangible assets acquired by Company A during the year; and (ii) information indicating the range of values of the Consideration. This information would facilitate investors' assessment of the impact of the transaction on Company A's financial position.

    The specific circumstances suggested that strict compliance with the disclosure requirements might be impractical and prejudicial to the interests of Company A. Having regard to the materiality of the Transaction and the alternative disclosure, the Exchange accepted that non-disclosure of the value of the Consideration in the announcement was not likely to mislead investors or influence their assessment of Company A's position.

Conclusion

15. The Exchange granted Company A a waiver from disclosing the Consideration in the announcement.

Note: With effect from 1 October 2019, Rule 14.58 also applies to the announcement for an extreme transaction. With effect from 11 June 2024, Rule 14.58(4) also requires the announcement of a notifiable transaction to disclose the amounts and details of treasury shares to be transferred if the consideration for the transaction includes treasury shares.

Whether the Exchange would impose additional requirements on a proposed distribution in specie of interests in an overseas listed subsidiary by a listed issuer

Parties

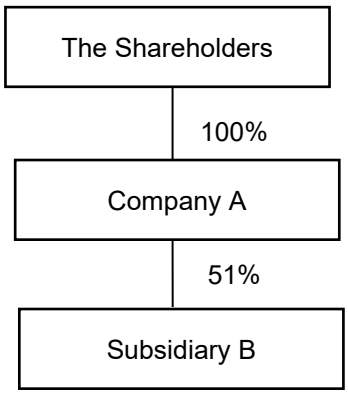
- **Company A** – a Main Board issuer
- **Subsidiary B** – Company A's non-wholly owned subsidiary, incorporated and listed overseas
- **Shareholders** – Company A's shareholders

Facts

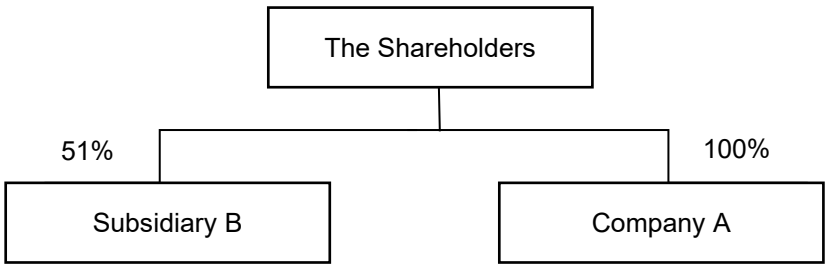
1. Company A was engaged in a number of businesses including (i) retail services through department stores; and (ii) information technology services through Subsidiary B.

2. To streamline its business activities and develop a more focused line of business, Company A proposed a group reorganisation through distribution in specie of all its equity interest in Subsidiary B (the Shares) to its Shareholders. After the distribution, Company A would cease to have any interest in Subsidiary B. The simplified shareholding structures before and after the distribution are below:

Before the distribution



After the distribution



3. The distribution required shareholder approval under Company A's articles of association and applicable laws. Company A submitted that the distribution would be in the Shareholders' interest and that all the Shareholders would be treated fairly and equally because:

   a. The Shares would be distributed to the Shareholders pro rata to their respective shareholding in Company A. Therefore the distribution would not dilute their interest in Subsidiary B.

   b. There was an adequate market in the Shares, which were listed on a stock exchange in Subsidiary B's place of incorporation. As supported by a legal opinion, the Shares could be freely owned and transferred by the Shareholders as foreigners and their transferability would not be unreasonably restricted. Any transfer of the Shares and/or dividend payment would be subject to reasonable tax.

   c. Company A would bear all the costs and duties payable by the Shareholders upon the transfer of the Shares to them, and would arrange for brokers to provide each Shareholder with custodian services free of account opening and monthly holding charges for two years or until all his Shares were disposed of, whichever was earlier.

Applicable listing rules or principles

4. Rule 2.03 states that:

   The Exchange Listing Rules reflect currently acceptable standards in the market place and 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) 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; ...

5. Rule 2.04 states that

   … the Exchange Listing Rules are not exhaustive and that the Exchange may impose additional requirements or make listing subject to special conditions whenever it considers it appropriate. …

6. Rules 14.04(1) and 14A.24 provide guidance on the scope of "transactions" subject to the notifiable transaction rules and connected transaction rules.

Analysis

7. The Exchange will normally consider a dividend distribution to shareholders as falling outside Chapters 14 and 14A. However, in the case of a distribution in specie, the Exchange may be concerned about whether the distribution is fair to all shareholders, particularly where unlisted assets are being distributed and there will be no liquid market for minority shareholders to realise a value from the distribution. The Exchange may impose additional requirements under Rule 2.04 to ensure compliance with Rule 2.03.

8. Here, the Shares were not listed on the Exchange and the proposal did not provide a cash alternative to the Shareholders. Nevertheless, the Exchange considered the following factors:

   a. The Shares were listed on an overseas exchange and could be freely owned and transferred by the Shareholders and there would be a liquid market for the Shareholders to realise a value from the distribution.

   b. Company A had made appropriate arrangements to facilitate the Shareholders' owning and holding of the Shares.

   c. The distribution was subject to shareholder approval.

Conclusion

9. The Exchange did not impose additional requirements under Rule 2.04 on the proposed distribution.

Note: With effect from 1 October 2019, Rule 14.94 applies to a distribution in specie of assets (other than securities listed on the Exchange) by a listed issuer where the size of the assets would amount to a very substantial disposal based on the percentage ratio calculations. The issuer must comply with the requirements:

(1) The issuer must obtain prior approval of the distribution by independent shareholders in a general meeting. The issuer's controlling shareholders (or if there is no controlling shareholder, the directors (other than the independent non-executive directors) and chief executive of the issuer) and their respective associates must abstain from voting in favour of the resolution. Further, the shareholders' approval for the distribution must be given by at least 75% of the votes attaching to any class of listed securities held by holders of voting either in person or by proxy at the meeting, and the number of votes cast against the resolution is not more than 10% of the votes attaching to any class of listed securities held by holders permitted to vote in person or by proxy at the meeting.

(2) The issuer's shareholders (other than the directors (excluding independent non-executive directors), chief executive and controlling shareholders) should be offered a reasonable cash alternative or other reasonable alternative for the distributed assets.

Where the assets proposed to be distributed are securities listed in other jurisdictions, the Exchange may waive the requirements in set out in (2) above if the issuer can demonstrate that there is a liquid market for the securities, the shareholders may readily dispose of those securities, and where appropriate, the issuer will make arrangements to facilitate the shareholders to hold or dispose of those securities.

Disclosure and other requirements for notifiable transactions

Profit forecast

1. A listed issuer proposes to acquire a company which constitutes a notifiable transaction. The listed issuer has prepared a valuation of the company using the discounted cash flow method. Is the listed issuer required to disclose the valuation in its announcement and circular for the notifiable transaction?

The listed issuer must observe the general disclosure principle under MB Rule 2.13 / GEM Rule 17.56. Where the valuation of the target company is a primary factor in forming the basis for the consideration or other material terms of the transaction, the valuation should be disclosed in the announcement and circular. See also our guidance letter HKEX-GL116-23 Disclosure of the basis of consideration and business valuations in notifiable transactions.

Where the valuation is prepared using the discounted cash flow method, it is a profit forecast and the listed issuer should comply with the MB Rule 14.60A / GEM Rule 19.60A and Paragraph 29(2) of Appendix D1B to the MB Rules and GEM Rules (as the case may be).

MB Rules 2.13, 14.60A, 14.66(2), App D1B – 29(2)
GEM Rules 17.56, 19.60A, 19.66(3), App D1B – 29(2)
First released: November 2008; last updated: May 2024

2. A listed issuer proposes to acquire a revenue generating asset. Do the profit forecast Rules apply if the announcement contains a profit forecast of the asset?

Yes. While MB Rule 14.60A / GEM Rule 19.60A does not make reference to an acquisition of assets, the reporting requirements should apply if the announcement contains profit forecast of the asset to be acquired. This follows the general principle of MB Rule 2.13 / GEM Rule 17.56.

MB Rules 2.13, 14.60A, 14.66(2), AppD1B – 29(2)
GEM Rules 17.56, 19.60A, 19.66(3), AppD1B – 29(2)
First released: November 2008; last updated: May 2024

3. Where a profit forecast is disclosed in a notifiable transaction circular, Paragraph 29(2) of Appendix D1B to the MB Rules and GEM Rules requires the financial advisers to report that they have satisfied themselves that the forecast has been made by the directors after due and careful enquiry and such report must be set out in the circular.

Can the directors of the listed issuer provide this confirmation if the listed issuer has not appointed a financial adviser in connection with the notifiable transaction?

MB Rule 14.60A(3) / GEM Rule 19.60A(3) provides that where a notifiable transaction announcement contains a profit forecast and no financial advisers have been appointed in connection with the transaction, the listed issuer may provide a letter from the board of directors confirming they have made the forecast after due and careful enquiry.

We may apply the principle of MB Rule 14.60A(3) / GEM Rule 19.60A(3) to the circular and accept the board of directors' confirmation for the purpose of Paragraph 29(2) of Appendix D1B to the Main Board Rules and GEM Rules. The listed issuer should consult the Exchange in advance in such circumstances.

MB Rules 14.66(2) and App D1B – 29(2)
GEM Rules 19.66(3) and App D1B – 29(2)
First released: November 2008; last updated: May 2024

4. Will valuations of Natural Resource assets (i.e. Reserves) based on discounted cash flows (DCF) be regarded as profit forecasts under MB Rules 14.60A and 14.61 / GEM Rules 19.60A and 19.61 which is required to be reviewed by the reporting accountants?

No, if the valuation meets the requirements of MB Chapter 18 / GEM Chapter 18A.

MB Rule 11.17, 14.60A, 14.61, 18.34, AppD1A(34)(2) and AppD1B (29)(2)
GEM Rule 14.29, 18A.34, 19.60A, 19.61, AppD1A(34)(2) and AppD1B(29)(2)
First released: March 2013; last updated: May 2024

Counterparty to a transaction

5. Is a listed issuer required to disclose the identity of the ultimate beneficial owner (UBO) of the counterparty in the announcement of a notifiable transaction?

MB Rule 14.58(2) / GEM Rule 19.58(3) requires disclosure of the identity of the counterparty to a notifiable transaction. This is normally the identity of the person with whom the listed issuer negotiated the transaction (and not the investment holding company that is the legal buyer or seller). As a general practice, listed issuers should disclose the UBO. This provides the investing public with information of the party who would exert influence on the transaction.

A UBO would normally be a natural person, subject to the following:

(a) For a company – natural persons who control, directly or indirectly, one-third or more of the counterparty. If the counterparty has a diverse shareholder base, the listed issuer should disclose as a minimum the UBO of the single largest shareholder;

(b) For a trust – the trustee and beneficiaries of the trust;

(c) For an investment fund – the licensed investment manager and / or the general partner (which may be a corporate) of a registered investment fund with a wide investor base. For other investment funds (e.g. a fund established for a single purpose or with few investors), the identity of the investors should also be disclosed; or

(d) For partnerships – the same principle for an investment fund applies.

In some situations, the counterparty or its intermediate owner may be the party that negotiated the transaction and its disclosure would provide sufficient information for investors. This may include:

(a) a listed issuer;
(b) a private company which has a substantive business and is generally known to the public;
(c) a governmental body or a state-owned company; or
(d) where the transaction involves the provision or subscription of services in the listed issuer's ordinary and usual course of business, the customer or service provider (e.g. construction services, operating leases).

In addition to disclosing the UBO of the counterparty, the UBOs of other parties which the listed issuer may have a continuing relationship with may also be material information requiring disclosure, for example, the UBOs of other shareholders of a target company acquired by the listed issuer who may exert influence on the target company.

MB Rules 14.58(2) and 14.58(3)
GEM Rules 19.58(3) and 19.58(4)
First released: November 2008; last updated: May 2024

Financial information of acquisition or disposal targets

6. Where a listed issuer acquires an equity interest in a company, what should it disclose to meet MB Rule 14.58(6) / GEM Rule 19.58(7), which requires disclosure of the book value of the assets to be acquired?

The listed issuer may disclose the net asset value shown in the target company's latest accounts.

MB Rule 14.58(6)
GEM Rule 19.58(7)
First released: November 2008; last updated: May 2024

7. A listed issuer proposes to acquire a company that reports under different accounting standards from those of the listed issuer. Can the listed issuer disclose the target company's financial information reported under its accounting standards in the notifiable transaction announcement?

Yes. In addition, the listed issuer should also disclose the accounting standards adopted by the target company and where applicable, an explanation on any principal differences between the accounting standards adopted by the listed issuer and the target company which may have a material impact on the financial information of the target company.

MB Rules 14.07, 14.58(6) and 14.58(7)
GEM Rules 19.07, 19.58(7) and 19.58(8)
First released: November 2008; last updated: May 2024

8. MB Rule 14.58(7) / GEM Rule 19.58(8) requires disclosure of the net profit attributable to the assets which are the subject of the transaction in the announcement. For an acquisition or disposal of a property held for rental purpose, what information should be disclosed to meet the Rule?

The net rental income generated from the subject property before and after taxation taking into account all related disbursements e.g. expenses for managing the property and allowances to maintain it in a condition to command its rent should be disclosed.

MB Rule 14.58(7)
GEM Rule 19.58(8)
First released: November 2008; last updated: May 2024

9. Does a major transaction circular need to include a recommendation from the directors as to the voting action that shareholders should take if the listed issuer has already obtained written approval from its major shareholders?

No.

MB Rule 14.63(2)(c)
GEM Rule 19.63(2)(c)
First released: November 2008; last updated: May 2024

10. A listed issuer is preparing a major transaction circular involving acquisition of revenue-generating assets. Does the circular need to include:

(i) a profit and loss statement?

Yes.

(ii) a valuation in respect of the assets to be acquired?

Yes, if such valuation is available.

MB Rule 14.67(6)(b)(i)
GEM Rule 19.67(6)(b)(i)
First released: November 2008; last updated: May 2024

11. MB Rule 14.68(2)(a)(i) / GEM Rule 19.68(2)(a)(i) requires the financial information of the disposal target or the listed issuer's group to include the balance sheet, the cash flow statement and the statement on changes in equity. What should be included in these statements?

They should include, at a minimum, each of the line items presented in the listed issuer's latest published annual accounts.

MB Rule 14.68(2)(a)(i)
GEM Rule 19.68(2)(a)(i)
First released: May 2010; last updated: May 2024

12. Which standard should auditors or reporting accountants adopt for the review of the financial information of the disposal target or the listed issuer's group to be reported in the circular?

The review should be conducted according to the relevant Hong Kong Institute of Certified Public Accountants or International Auditing and Assurance Standards Board standards. Currently, the applicable standard for a review engagement is Hong Kong Standard on Review Engagements 2400 / 2410 or International Standard on Review Engagements 2400 / 2410.

MB Rule 14.68(2)(a)(i)
GEM Rule 19.68(2)(a)(i)
First released: May 2010; last updated: May 2024

13. If the disposal target was acquired by the listed issuer two years ago, can the listed issuer include, in the circular, the disposal target's financial information from the acquisition date?

No. The circular should contain the disposal target's financial information for the three financial years immediately preceding the issue of the circular and where applicable a stub period.

MB Rules 14.68(2)(a)(i), Note to 4.06(1)(a)
GEM Rules 19.68(2)(a)(i), Note to 7.05(1)(a)
First released: May 2010; last updated: May 2024

14. If a listed issuer discloses the listed issuer group's financial information with separate disclosure on the disposal target (i.e. option (B) in MB Rule 14.68(2)(a)(i) / GEM Rule 19.68(2)(a)(i)), what financial information about the disposal target should be disclosed?

There should be a separate note with information on the disposal target's financial information. Normally this includes the target's income statement, balance sheet, cash flow statement and statement of changes in equity.

MB Rule 14.68(2)(a)(i)
GEM Rule 19.68(2)(a)(i)
First released: May 2010; last updated: May 2024

15. MB Rule 14.68(3) / GEM Rule 19.68(3) requires a very substantial disposal circular to include the management discussion and analysis and other information on the remaining group as set out in Paragraph 32 of Appendix D2 to the MB Rules/ GEM Rule 18.41. What period should such information cover?

It should cover (i) the same period as the financial information of the listed issuer group disclosed in the very substantial disposal circular under Option (B) of MB Rule 14.68(2)(a)(i) / GEM Rule 19.68(2)(a)(i); or (ii) the latest three financial years and where applicable, the most recent interim period for which the listed issuer group's financial information has been published.

MB Rules 14.68(2)(a)(i) and 14.68(3)
GEM Rules 19.68(2)(a)(i) and 19.68(3)
First released: November 2008; last updated: May 2024

16. If a listed issuer incorporates financial information for the last three financial years in a circular by reference to another published document, what should be disclosed?

In addition to identifying the information to be incorporated by reference, the listed issuer should identify the published document with the document name and date, the relevant pages, and where shareholders can access the document (for example, the website address).

MB Rules 14.67(4) and App D1B - 31(3)
GEM Rules 19.67(4) and App D1B - 31(3)
First released: May 2010; last updated: May 2024

Valuation of properties

17. MB Rule 5.01(1) / GEM Rule 8.01(1) provides that the acquisition cost should be used as the carrying amount of an asset if the acquisition is made after the latest consolidated audited accounts. How should the acquisition cost be determined?

The acquisition cost should be determined based on the appropriate accounting treatment used by the acquiror in preparing the financial statements.

MB Rule 5.01(1)
GEM Rule 8.01(1)
First released: October 2011; last updated: May 2024

Indebtedness statement

18. Are there any requirements on the reporting date of the indebtedness statement?

The Exchange ordinarily requires the indebtedness statement to be dated not more than eight weeks before the circular is issued.

MB Rules 14.66(10) and App D1B – 28
GEM Rules 19.66(11) and App D1B – 28
First released: November 2008; last updated: May 2024

19. Does the indebtedness statement need to be reviewed by professional accountants or advisers?

The Listing Rules do not specifically require a review of the indebtedness statement by professional accountants or advisers. It is up to the listed issuer to decide whether such a review is necessary.

MB Rules 14.66(10) and App D1B – 28
GEM Rules 19.66(11) and App D1B – 28
First released: December 2009; last updated: May 2024

20. If the target company will become a subsidiary of the listed issuer upon completion of the acquisition, should the indebtedness statement of the listed issuer's group and the target company be prepared (a) on a combined basis; or (b) separately?

Both presentation bases are acceptable.

MB Rules 14.66(10), App D1B – 28 and Note 2
GEM Rules 19.66(11), App D1B – 28 and Note 2
First released: May 2010; last updated: May 2024

Working capital sufficiency statement

21. MB Rules 14.66(10), 14.66(12) and Paragraph 30 of Appendix D1B to the MB Rules / GEM Rules 19.66(11), 19.66(13) and Paragraph 30 of Appendix D1B to the GEM Rules require the listed issuer's financial advisers or auditors to provide a comfort letter on the working capital sufficiency statement. Can the comfort letter be provided by the reporting accountants?

Yes.

MB Rules 14.66(10), 14.66(12) and App D1B – 30
GEM Rules 19.66(11), 19.66(13) and App D1B – 30
First released: December 2009; last updated: May 2024

22. For a very substantial disposal of a subsidiary, can the working capital sufficiency statement of the group exclude that subsidiary?

No. Paragraph 30 of Appendix D1B to the MB Rules and GEM Rules requires the listed issuer to prepare a working capital sufficiency statement on the group, this includes the subsidiary to be disposed of.

MB Rules 14.66(10), 14.66(12) and App D1B – 30
GEM Rules 19.66(11), 19.66(13) and App D1B – 30
First released: November 2008; last updated: May 2024

Online display of documents

1. Where and for how long should documents on display be published online? How will these documents be removed from the relevant websites after the expiry of the prescribed display period?

Listed issuers should publish documents on display on both the HKEX website (through EPS under the headline category "Documents on Display") and the listed issuer's website for the time period prescribed by the Listing Rules (which is the same as what the Listing Rules originally require for physical display of such documents).

After the expiry of any relevant display period prescribed by the Listing Rules, listed issuers should remove the documents on display manually from the HKEX website through EPS and their own website.

They should not do so before the expiry of the relevant display period.

MB Rules 4.14, 5.01B(1)(b), 5.02B(2)(b), 14.66(10), 14.67A(2)(b)(viii), 14A.70(13), 15A.21(4), 17.02(2), 19.10(5)(e) and (6), 19A.27(4), 29.09, 29.10, 36.08(3), App D1A - 53, App D1B - 43, App D1C - 54, App D1D - 27, App D1E - 76, App D1F - 66, App A2 - 9(b), App E5 - 5 and 15 / GEM Rules 7.18, 8.01B(1)(b), 8.02B(2)(b), 19.66(11), 19.67A(2), 20.68(13), 23.02(2), 24.09(2), (3), (5)(a), (5)(e) and (6), 25.20(4), 32.05(3), 35.10, 35.11, App D1A - 52, App D1B - 42, App D1C - 53, App A2 - 9
First released: June 2021; last updated: May 2024

2. Are listed issuers allowed to redact sensitive information in documents on display?

If listed issuers do not wish certain information contained in documents on display to be disclosed, they may apply to the Exchange for specific disclosure relief.

The Exchange will consider redaction waiver on a case-by-case basis and with reference to the Guide on Applications for Waivers and Modifications of the Listing Rules. A waiver may be granted to allow the redaction of information that is not material to the assessment of the subject transaction if a listed issuer can demonstrate to the Exchange's satisfaction that disclosure of such information would breach the Personal Data (Privacy) Ordinance or cause competitive harm to the listed issuer (e.g. the information is a trade secret).

MB Rule 2.04
GEM Rule 2.07
First released: June 2021; last updated: May 2024

3. What are "contracts pertaining to the transaction" in the case of a notifiable transaction or connected transaction circular? Are material contracts entered into two years ago in relation to earlier phases of the subject transaction considered as "contracts pertaining to the transaction"?

Contracts pertaining to the transaction are contracts which are related to the transaction and relevant to shareholders' assessment of the transaction before they vote at the meeting. Material contracts in relation to earlier phases of the project referred to in the circular but that are not otherwise related to the subject transaction will generally not be considered as "contracts pertaining to the transaction".

MB Rules App D1B - 43(2)(c), App D1F - 66(2)(c)
GEM Rules App D1B - 39, 41 and 42(2)
First released: June 2021; last updated: May 2024

PRC's filing requirements for overseas listings and securities offerings by Mainland companies

1. The China Securities Regulatory Commission (CSRC) introduced a new filing regime on 31 March 2023 to require all Mainland companies to register their direct or indirect overseas listings and securities offerings with the CSRC by filing materials on key compliance issues (PRC Filing Requirements). They apply to both PRC issuers and Hong Kong/overseas-incorporated issuers with principal operations in the Mainland. Would the implementation of the PRC Filing Requirements have any impact on the issuance of securities by issuers listed on the Exchange?

As a general principle, listed issuers must comply with applicable laws and regulations at all times. Accordingly, where a listed issuer's proposed issuance of securities falls within the PRC new filing regime, its directors should ensure that the listed issuer has completed the filing with the CSRC in accordance with the PRC Filing Requirements.

The Exchange may require listed issuers to confirm compliance with the PRC Filing Requirements or other laws and regulations applicable to their material transactions as part of its vetting process of transaction circulars. It may withhold the listing approval for the proposed issue of securities if the PRC Filing Requirements are not fulfilled.

MB Rules 2.03 and 8.01
GEM Rule 2.06 and 11.01
First released: February 2023; last updated May 2024

12

Connected transactions

12.1 Definition of connected persons and deeming provisions

Listing decision – Whether a fund manager was a core connected person or a connected person of the listed issuer when the manager held shares in a listed issuer on behalf of its clients	LD22-2011	12.1 – 1
Listing decision – Whether the Exchange would deem a third party service provider as a connected person of the listed issuer by virtue of its close association with the controlling shareholder of the listed issuer	LD111-2017	12.1 – 4
Listing decision – Whether the Exchange would deem an investor as a connected person of the listed issuer upon completion of a proposed transaction where the investor would acquire 29.9 percent interest in a subsidiary of the issuer with a special arrangement to restrict the investor's voting power at general meetings of the subsidiary to below 10 per cent	LD63-1	12.1 – 7
Listing decision – Whether substantial shareholders of the holding company of a listed issuer were connected persons of the listed issuer, and if not, whether the Exchange would deem these parties as connected persons	LD63-2	12.1 – 11
Listing decision – Whether the Exchange would deem a party as a connected person of the listed issuer in respect of a proposed transaction that involved such party acquiring from both the listed issuer and its controlling shareholder their respective interests in the same property	LD63-3	12.1 – 16

Listing decision – Whether the Exchange would deem a REIT as a connected person of the listed issuer in respect of a proposed transaction that involved the listed issuer and its controlling shareholder injecting their assets into the REIT and subscribing units issued by the REIT	LD63-5	12.1 – 19
Frequently asked questions – Definition of connected persons	FAQ12.1 – No.1	12.1 – 22

12.2 Definition of connected transactions and calculation of percentage ratios

Listing decision – Whether the provision of guarantee by a listed issuer for a bank loan granted to a subsidiary of an associated company was a connected transaction if the substantial shareholder of the issuer directly held a 10 per cent interest in the associated company	LD78-2014	12.2 – 1
Listing decision – Whether the placing of deposits by a listed issuer with banks, being subsidiaries of a substantial shareholder of the issuer, was a connected transaction	LD76-1	12.2 – 4
Listing decision – Whether the provision of management services by a listed issuer for a residential complex was a connected transaction if its substantial shareholder owned a majority of the undivided shares in the complex	LD76-2	12.2 – 8
Listing decision – Whether the proposed amendments to a non-competition undertaking given by the controlling shareholder to the listed issuer constituted a connected transaction	LD79-2014	12.2 – 12
Listing decision – Whether the Exchange would disregard the revenue ratio for a disposal of a target company whose business was different from the principal businesses of the listed issuer	LD62-4	12.2 – 15
Listing decision – Whether the Exchange would accept the alternative revenue ratio proposed by a listed issuer due to a change in its accounting policy for jointly controlled entities	LD61-2013	12.2 – 18

Listing decision – In respect of a placing and top-up subscription proposed by a listed subsidiary, whether the listed parent was allowed to calculate the percentage ratios for its disposal and acquisition of interests in the subsidiary on a net basis, and if not, a waiver from the major transaction requirements would be granted	LD75-3	12.2 – 21
Listing decision – Whether the Exchange would accept the alternative revenue ratio for certain continuing connected transactions between a newly acquired subsidiary and the substantial shareholder of the listed issuer	LD60-2013	12.2 – 25
Frequently asked questions – Definition of connected transactions and calculation of percentage ratios	FAQ12.2 – No.1-12	12.2 – 28

12.3 Continuing connected transactions

Guidance letter – Guidance on pricing policies for continuing connected transactions and their disclosure	GL73-14	12.3 – 1
Listing decision – Whether the Exchange would waive the annual review and reporting requirements for a continuing connected transaction between the listed issuer and its independent non-executive director	LD63-2013	12.3 – 6
Listing decision – Whether the Exchange would waive the written agreement requirement for continuing connected transactions between a subsidiary of the listed issuer and other substantial shareholders of the subsidiary	LD82-1	12.3 – 8
Frequently asked questions – Continuing connected transactions	FAQ12.3 – No.1-11	12.3 – 11

12.4 Aggregation of transactions

Listing decision – Whether a listed issuer was required to aggregate its purchase of products of the same nature from associates of a connected person	LD64-3	12.4 – 1
Listing decision – Whether a listed issuer would be required to aggregate its continuing connected transactions with its controlling shareholder which involved both revenue and expenditure items	LD64-4	12.4 – 4

Listing decision – Whether a listed issuer was required to aggregate its transactions in relation to the lease and license of properties in the same building to two directors who were associates of each other	LD76-3	12.4 – 7
Listing decision – Whether a listed issuer was required to aggregate its construction contracts for different parts of a railway line with associates of a connected person	LD13-2011	12.4 – 10
Listing decision – Whether a listed issuer was required to aggregate its transactions with its parent company involving (i) the parent company contracting out certain works to the listed issuer; and (ii) the listed issuer sub-contracting some of the works back to the parent group	LD14-2011	12.4 – 12
Frequently asked questions – Aggregation of transactions	FAQ12.4 – No.1-3	12.4 – 15

12.5 Shareholders' approval requirement

Listing decision – Whether certain shareholders of a listed issuer had a material interest in the issuer's proposal to privatise a listed subsidiary	LD73-2	12.5 – 1
Listing decision – Whether a substantial shareholder of a listed issuer had a material interest in the proposed acquisition of interests in a target company	LD81-1	12.5 – 6
Listing decision – Whether a substantial shareholder of a listed issuer had a material interest in the proposed acquisitions of interests in a target company	LD81-2	12.5 – 9
Frequently asked questions – Shareholders' approval requirement for connected transactions	FAQ12.5 – No.1	12.5 – 13

12.6 Exemptions from the connected transaction requirements

Frequently asked questions – Exemptions from the connected transaction requirements	FAQ12.6 – No.1-16	12.6 – 1

12.7 Disclosure and other requirements

Listing decision – Whether the Exchange would waive the profit forecast requirements in respect of a valuation report on the disposal target disclosed in the listed issuer's announcement and circular for the disposal	LD93-3	12.7 – 1
Frequently asked questions – Disclosure and other requirements for connected transactions	FAQ12.7 – No.1	12.7 – 4

Whether a fund manager was a core connected person or connected person of the listed issuer when the manager held shares in a listed issuer on behalf of its clients

Parties

- **Company A** – a Main Board issuer

- **Manager** – an international asset management group and a shareholder of Company A

Facts

1. The Manager managed funds and assets for institutional and private clients around the world. It held about 12 per cent of Company A's shares (the **Shares**) for two categories of clients:

   - 8 per cent were held under certain funds managed by the Manager (collectively, the **Pooled Funds**). These funds had defined investment objectives and mandates to invest in a wide range of companies. Investors of the funds were required to effectively delegate, without recourse, the investment decisions and voting powers of the Shares to the Manager.

   - 4 per cent were held on behalf of a number of clients under segregated investment accounts and closed-end funds (collectively, the **Segregated Funds**). These clients retained the power to instruct the Manager on how to handle their investments, including investment decisions and voting powers of the underlying securities.

     The mandate given by each client to the Manager contained a proxy arrangement under which the Manager was authorised to vote on behalf of the client according to the client's instruction, and in the absence of a specific voting instruction, the Manager might exercise the voting rights in accordance with its proxy voting policy endorsed by the client. The policy sought to assure that proxies were voted in the best interest of each client.

2. The Manager had no other connection with Company A. It did not have any board seats in Company A or special rights to influence its management.

3. Company A submitted the 4 per cent Shares held under the Segregated Funds should be excluded when assessing whether the Manager was a substantial shareholder of Company A because the voting rights of these Shares rested with the clients. It sought the Exchange's confirmation that the Manager was not Company A's core connected person or connected person.

Relevant Listing Rules

4. Rule 1.01 defines a "substantial shareholder" in relation to a company as:

   a person who is entitled to exercise, or control the exercise of, 10 per cent or more of the voting power at any general meeting of the company.

5. Rule 1.01 states that a "core connected person" in relation to a company includes:

   … a director, chief executive or substantial shareholder of the company …

6. Rule 14A.07 states that a "connected person" includes:

   (1) a director, chief executive or substantial shareholder of the listed issuer…
   …

7. Rule 8.24 states that:

   The Exchange will not regard any core connected person of the issuer as a member of the "public" or shares held by a core connected person as being "in public hands". …

Analysis

8. Under the Rules, a core connected person or connected person includes an issuer's substantial shareholder for the purpose of the public float and connected transaction requirements. These requirements seek to (i) ensure a sufficient amount of listed securities in public hands to maintain an open market for trading; and (ii) safeguard against connected persons taking advantage of their positions to the detriment of the issuer's minority shareholders.

9. In this case, the Exchange noted that:

   - The Manager had control over 8 per cent of the Shares which were held under the Pooled Funds.
   - The 4 per cent of the Shares held under the Segregated Funds could be distinguished from other Shares held by the Manager:
     - The clients of the Segregated Funds were the beneficial owners of the underlying Shares. They had control over the investment portfolios including the purchase and sale of these Shares.
     - The exercise of the voting rights attached to the Shares held under the Segregated Funds was always subject to the clients' specific instructions. Although the Manager could exercise the voting rights in the absence of any specific instructions, it must vote in the best interest of the clients, and not itself, under the proxy voting policy endorsed by the clients.

10. As the Manager did not have control over 10 per cent or more of the shares, it was not a substantial shareholder of Company A.

Conclusion

11. The Manager was not Company A's core connected person or connected person.

Whether the Exchange would deem a third party service provider as a connected person of the listed issuer by virtue of its close association with the controlling shareholder of the listed issuer

Parties

- **Company A** – a Main Board issuer
- **Company B** – a company engaged in the provision of payment services
- **Parent Company** – Company A's controlling shareholder holding a majority of Company A's issued shares

Facts

1. Company A proposed to engage Company B to provide certain payment processing services for Company A's online sale of products (**Transactions**).

2. Company A submitted that Company B was not an associate of the Parent Company under Chapter 14A.

3. Nevertheless, there were certain relationships between Company B and the Parent Company:

   (a) Company B was initially established by the Parent Company to operate its payment service business. In light of the subsequent changes in the relevant business licensing regulations in the PRC, the Parent Company divested all its interest in and control over Company B to PRC nationals and restructured Company B as a PRC domestic company to facilitate its application for the PRC regulatory approvals. As part of the divestment, the Parent Company also entered into various agreements with Company B and other relevant parties to govern the Parent Company's continuing financial and commercial relationship with Company B in the future.

   (b) At the time of the proposed Transactions, the Parent Company still maintained various arrangements with Company B to secure long-term economic participation in Company B, including that:

      (i) the Parent Company would receive royalty streams and a service fee amounting to the sum of an expense reimbursement plus a profit sharing of 38% of the consolidated pre-tax income of Company B (**Profit Sharing Arrangement**) for the license of certain intellectual properties and provision of software technology services; and

(ii) where Company B applies for, and receives, certain PRC regulatory approvals in the future and subject to certain conditions, it would issue new shares to the Parent Company for up to 33% of its equity capital.

4. The issue was whether the Exchange would exercise its power to deem Company B as a connected person of Company A such that the Transactions would become connected transactions of Company A.

5. Company A submitted that Company B should not be deemed as its connected person because:

(a) The deeming power under Rule 14A.19 should only be exercised by the Exchange with reference to Rule 14A.20 which, in this case, did not apply because the Profit Sharing Arrangement was executed before (and thus not "with respect to") the Transactions.

(b) The Transactions would be conducted in the ordinary course of Company A's business on an arm's length basis under normal commercial terms. The Parent Company was not able to influence the terms of the Transactions.

(c) Neither the Parent Company nor Company A had an intention to circumvent the connected transaction Rules. As the Parent Company holds over 50% of the equity interest in Company A, but shares only 38% of the profit of Company B, there would be no incentive to manipulate the rates paid by Company A - the Parent Company would bear over 50% of any cost increase of Company A which would exceed the additional 38% profit it shares through the Profit Sharing Arrangement.

Relevant Listing Rules

6. Main Board Listing Rule 14A.19 provides that:

"The Exchange has the power to deem any person to be a connected person."

7. Main Board Listing Rule 14A.20 provides that:

"A deemed connected person includes a person:

(1) who has entered, or proposes to enter, into:

(a) a transaction with the listed issuer's group; and

(b) an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with a connected person described in rule 14A.07(1), (2) or (3) with respect to the transaction; and

(2) who, in the Exchange's opinion, should be considered as a connected person."

Analysis

8. The purpose of the connected transaction Rules is to guard against the transfer of benefits by persons who are able to exercise significant influence over the issuer. Rule 14A.19 provides that the Exchange has the specific power to deem a person to be connected. When applying the deeming provision, the Exchange considers all relevant facts and circumstances surrounding the transaction and has particular regard to the substance and not the form of the arrangement.

9. In the present case, the Exchange noted that there was a close association between the Parent Company and Company B (see paragraph 3 above). The Exchange considered it appropriate to deem Company B as a connected person of Company A under Rule 14A.19 because:

   (a) The Parent Company, as a controlling shareholder of Company A, was in a position to exercise significant influence over Company A's transactions with Company B.

   (b) The Profit Sharing Arrangement would enable the Parent Company to stand to benefit from Company A's transactions with Company B and could effect a transfer of benefits from Company A to the Parent Company.

10. The Exchange disagreed with Company A's view because:

   (a) Under Rule 14A.19, the Exchange may deem any person to be a connected person. Rules 14A.20 and 14A.21 set out certain specific circumstances where the Exchange may apply the deeming provision, which are not meant to be exhaustive.

   (b) The Profit Sharing Arrangement was part of the arrangements for the Parent Company to secure long-term economic participation in Company B. As the Parent Company was in a position to exercise significant influence over Company A and its transactions with Company B, there was a conflict of interests of Company A with those of the Parent Company. The Exchange's decision to apply the deeming provision was consistent with the policy intent of the connected transaction Rules, i.e. to guard against the transfer of benefits by persons with significant influence over a listed issuer.

   (c) Intention of circumvention and incentive for rates manipulation were not the tests in the present case; neither were they the only circumstances where a deeming provision should be invoked. Company A's argument that the Transactions were negotiated on an arm's length basis was also not the relevant test in the present case. Because of the concerns mentioned in paragraph 9 above, to deem Company B as a connected person of Company A would appropriately increase the transparency and oversight of the Transactions within the regulatory ambit of the connected transaction Rules.

Conclusion

11. The Exchange determined that Company B should be deemed as a connected person of Company A under Rule 14A.19. Accordingly, the Transactions would constitute connected transactions of Company A.

Whether the Exchange would deem an investor as a connected person of the listed issuer upon completion of a proposed transaction where the investor would acquire 29.9 per cent interest in a subsidiary of the issuer with a special arrangement to restrict the investor's voting power at general meetings of the subsidiary to below 10 per cent

Parties

- **Company A –** a Main Board listed company
- **Company X** and **Company Y** – wholly-owned subsidiaries of Company A
- **Project Company** – a property development company and a subsidiary of Company A
- **Purchaser** – an independent third party company proposing to acquire from Company A a 29.99% equity interest in the Project Company

Facts

1. Company A, through Company X and Company Y, held a 70.01% equity interest and a 29.99% equity interest in the Project Company respectively.

2. The Purchaser was a company owned by certain funds (**Funds**) managed by a fund management company.

3. Company A and the Purchaser entered into an agreement (**Agreement**) under which the Purchaser would acquire from Company A the entire interest in Company Y and hence an indirect 29.99% equity interest in the Project Company (**Transaction**). Upon completion of the Transaction, Company A (through Company X) would continue to hold a 70.01% equity interest in the Project Company which would be a non-wholly owned subsidiary of Company A. The Purchaser (through Company Y) would hold the remaining 29.99% equity interest in the Project Company.

4. It was also agreed that upon completion of the Transaction, Company Y would reduce its voting power at the general meetings of the Project Company (**General Meetings**) to 9.98% and the remaining 90.02% of the voting power would be exercisable by Company X. Company X and Company Y would have the right to appoint 10 directors and 1 director to the board of the Project Company (**Board**) respectively.

5. Notwithstanding the arrangements mentioned in paragraph 4 above, the joint venture contract and the articles of association of the Project Company would provide that:

a. if the Funds (or the Purchaser) dispose of their indirect interest in the Project Company to a potential purchaser, the potential purchaser's voting power in the General Meetings, and rights to appoint directors to the Board will be restored to the same extent as the equity interest acquired by the potential purchaser. This term, Company A submitted, catered for a potential purchaser who might have an expectation different from those of the Funds and might want to retain control of the Project Company proportionate to its equity interest in the Project Company; and

b. Company Y has veto rights in respect of certain matters concerning the Project Company (the **Reserved Matters**) covering a wide range of matters. The Reserved Matters include but are not limited to the following matters:

- winding up of the Project Company
- amendment to constitutional documents
- change in share capital, or issue or redemption of securities
- amendment to shareholders' rights
- distribution of reserve
- development of new business or material change in the nature or scope of business
- any capital and operating budget or business plan or any material amendment thereto
- any material contact outside the normal course of business
- any contract other than on arm's length market terms
- any acquisition, sale, lease or disposal of any property other than in the ordinary course of business
- any material transaction outside the ordinary course of the business

6. Company A submitted that

- the Funds were primarily interested in the economic return on their investment in the Project Company, and did not intend to participate in the management of the Project Company's business. The reduction in Company Y's voting power in the General Meetings, which the Funds did not commercially require, would exclude Company Y and therefore the Purchaser from the definition of "substantial shareholder" of the Project Company and therefore a connected person of Company A; and

- subjecting certain matters of a joint venture company to the special approval of minority shareholders was necessary for the protection of the minority shareholders and was customary in property joint ventures. Since the Reserved Matters were restricted to material matters outside the ordinary course of business of the Project Company and the respective veto right was meant to be a defensive measure for protection of minority interest rather than a means to acquire control, the Project Company would still be able to manage its business in its ordinary course without interference from Company Y. Accordingly, Company Y should not be considered to be in a position to have an influence over the Project Company to such an extent that it should be treated as a connected person.

Relevant Listing Rules

7. Main Board Listing Rule 1.01 defines "substantial shareholder" and "connected person" as follows:

"substantial shareholder"	in relation to a company means a person … who is entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of the company.
"connected person"	has the meaning in rule 14A.06(7) …

8. Main Board Listing Rule 2.04 provides that:

> It is emphasised that the Exchange Listing Rules are not exhaustive and that the Exchange may impose additional requirements or make listing subject to specific conditions whenever it considers it appropriate. Conversely, the Exchange may waive, modify or not require compliance with the Exchange Listing Rules in individual cases (to suit the circumstances of a particular case), as a variety of circumstances may exist which require it to make ad hoc decisions. …

9. Main Board Listing Rule 14A.07(1) provides that the definition of "connected person" includes:

> a … substantial shareholder of the listed issuer or any of its subsdiaries

Analysis

10. The connected transaction rules seek to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as the listed issuer's directors, chief executives or substantial shareholders or their associates) taking advantage of their positions to the detriment of minority shareholders of an issuer.

11. For the purposes of the connected transaction rules, the definition of "connected person" is set out in Rules 14A.07 to 14A.22.

12. Rule 2.04 provides that the Listing Rules are not exhaustive and that the Exchange has discretion to, among others, modify the existing requirements under the Listing Rules and impose additional requirements as it considers appropriate. The Exchange will have regard to all of the relevant facts and circumstances of the case in its determination of whether to exercise its discretion under Rule 2.04. In circumstances where the definition of "connected person" is technically inapplicable to a particular person/entity due to certain specific arrangements, the Exchange will look at the substance of the arrangements and consider whether they have been structured to circumvent the spirit and intent of the rules. In such circumstances, it may be appropriate to "deem" such person/entity as connected under Rule 2.04.

13. In the present case, given the special voting arrangement established for the Project Company, Company Y would not be entitled to exercise or control the exercise of 10% or more of the voting power at any general meetings of the Project Company. It did not meet the definition of a substantial shareholder of the Project Company. Accordingly, Company Y and hence the Purchaser would not be connected persons of Company A pursuant to Rule 14A.07(1).

14. Having considered the relevant facts and circumstances of this case, the Exchange considered it necessary to deem the Purchaser as a connected person of Company A pursuant to Rule 2.04. Principal factors taken into account by the Exchange are set out below.

- It was apparent from the facts that the special voting arrangement in respect of the Project Company was structured in the way to circumvent the connected transaction rules. The Exchange was not satisfied that there was any genuine commercial reason for Company Y to restrict its voting power in the General Meetings to just below 10% (being the threshold for determining a substantial shareholder under the Listing Rules).

- Despite the restriction on Company Y's voting power in the General Meetings, Company Y would have the veto rights in respect of the Reserved Matters. While veto rights given to minority shareholders on certain material matters were not uncommon in property joint venture companies, the Reserved Matters in this case covered a wide range of matters some of which should normally be within the powers vested in shareholders at general meetings. The considerable influence of Company Y over these significant matters of the Project Company through its veto rights should be recognised.

Conclusion

15. Based on the above analysis, the Exchange determined that the Purchaser should be deemed as a connected person of Company A under Rule 2.04.

Whether substantial shareholders of the holding company of a listed issuer were connected persons of the listed issuer, and if not, whether the Exchange would deem these parties as connected persons

Parties

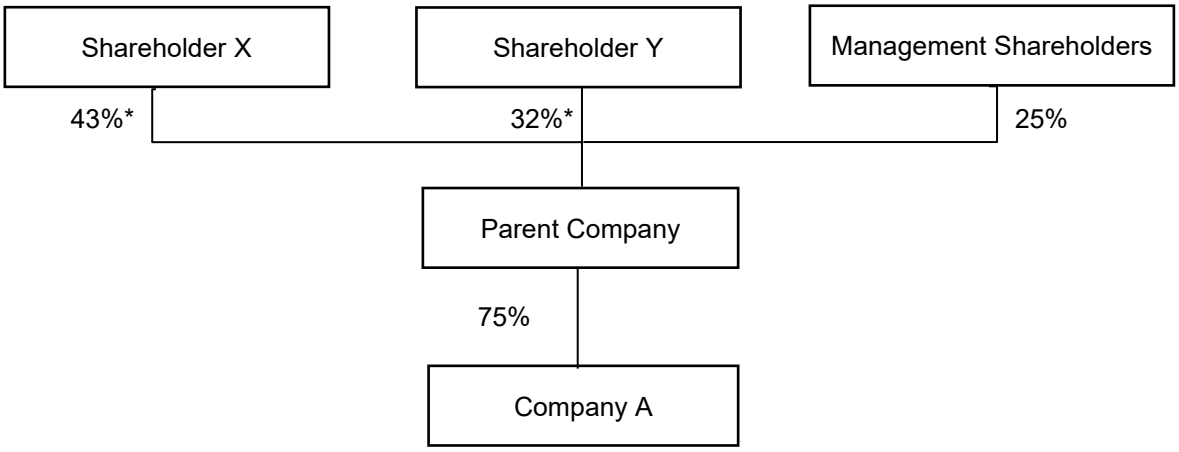
- **Company A** – a Main Board listed issuer
- **Parent Company** – the holding company of Company A
- **Parent Shareholders** – shareholders of Parent Company, including Shareholder X, Shareholder Y and the Management Shareholders

Facts

1. Company A was a subsidiary of Parent Company. Parent Company held approximately 75% of the issued share capital of Company A at the time of new listing.

2. Parent Company engaged in other business activities in addition to its investment in Company A.

3. Parent Company was owned by three shareholder groups, including Shareholder X, Shareholder Y and the Management Shareholders (as referred in paragraph 5 below). The simplified shareholding structure of Company A and Parent Company was as follows:



** including interest held by wholly owned subsidiaries of Shareholder X/Y*

4. Shareholder X and Shareholder Y were the major corporate shareholders of Parent Company. Each of Shareholder X and Shareholder Y was a separate entity with its own business activities and its securities were listed on an overseas stock exchange.

5. The Management Shareholders comprised 4 individuals (including Mr. A and Mr. B) who were founders and members of the management of Parent Company. Mr. A and Mr. B were also directors of Company A.

6. The Parent Shareholders had entered into a shareholders' agreement (the **Shareholders' Agreement**) before listing of Company A which governed relationship of these shareholders in respect of Parent Company.

7. Based on the shareholding structure of Parent Company and the terms of the Shareholders' Agreement, each of the three groups of Parent Shareholders was in a position to exert influence over Parent Company through approval/veto rights on significant matters relating to Parent Company and its subsidiaries, but none of them had control over Parent Company.

8. As Company A was not a party to the Shareholders' Agreement, the arrangements among the Parent Shareholders in terms of approval/veto rights on significant matters relating to Company A (being a subsidiary of Parent Company) under the Shareholders' Agreement were not binding on Company A and its board. Neither Company A nor its board had any obligation to ensure the implementation of the Shareholders' Agreement.

Relevant Listing Rules

9. Main Board Listing Rule 1.01 defines, among others, the terms "close associate", "substantial shareholder" and "core connected person" as follows:

"close associate"	(b) in relation to a company means: … (i) its subsidiary or holding company or a fellow subsidiary of its holding company; … (iv) any other company in the equity capital of which the company, its subsidiary or holding company, a fellow subsidiary of its holding company, … taken together are directly or indirectly interested so as to exercise or control the exercise of 30% (or any amount be specified in the Takeovers Code as the level for triggering a mandatory general offer) or more of the voting power at general meetings, or to control the composition of a majority of the board of directors and any subsidiary of this other company; …
"substantial shareholder"	in relation to a company means a person … who is entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of the Company …

"core connected person"	(a)	for a company …, means a director, chief executive or substantial shareholder of the company or any of its subsidiaries or a close associate of any of them, and

10. Main Board Listing Rule 14A.07 provides that a "connected person" is:

(1) a director, chief executive or substantial shareholder of the listed issuer or any of its subsidiaries;

…

(4) an associate of any of the above persons…

Analysis

11. The general definition of "core connected person" is contained in Rule 1.01. For the purposes of the connected transaction rules, the definition of "connected person" is set out in Rules 14A.07 to 14A.22.

12. In the present case, Parent Company was a substantial shareholder, and therefore a core connected person and a connected person, of Company A under Rules 1.01 and 14A.07 by virtue of its 75% equity interest in Company A.

Whether the Parent Shareholders were connected persons of Company A under the Listing Rules by virtue their substantial interests in Parent Company

13. When determining whether the Parent Shareholders were core connected persons or connected persons of Company A under Rules 1.01 and 14A.07 by virtue of their substantial interests in Parent Company, the Exchange had considered whether the Parent Shareholders were (i) substantial shareholders of Company A or (ii) associates of Parent Company under the Listing Rules. In this regard, the facts of the case indicated that:

- None of the Parent Shareholders had control over Parent Company. Accordingly, no individual Parent Shareholder was able to exercise or control the exercise of 10% or more of the voting power at any general meeting of Company A even though such person's indirect interest in Company A through Parent Company was more than 10%. The Parent Shareholders did not fall under the definition of "substantial shareholder" set out in Rule 1.01 in respect of Company A.

- None of the Parent Shareholders were close associates or associates of Parent Company under Rules 1.01 and 14A.12 to 14A.15. In particular, there was no evidence suggesting that Parent Company was a subsidiary of any Parent Shareholder.

Based on the facts presented, none of the Parent Shareholders were connected persons of Company A under Rules 1.01 and 14A.07by virtue of their substantial interests in Parent Company.

14. Notwithstanding the above and for the avoidance of doubt, Mr. A and Mr. B were core connected persons or connected persons of Company A under Rules 1.01 and 14A.07 by virtue of their positions as directors of Company A.

Whether the Exchange would deem the Parent Shareholders to be connected persons of Company A because of their substantial interests in Parent Company

15. Rule 2.04 provides that the Listing Rules are not exhaustive and that the Exchange has discretion to, among others, modify the existing requirements under the Listing Rules and impose additional requirements as it considers appropriate. The Exchange will have regard to all of the relevant facts and circumstances of the case in its determination of whether to exercise its discretion under Rule 2.04. In circumstances where the definition of "connected person" is technically inapplicable to a particular person/entity due to certain specific arrangements, the Exchange will look at the substance of the arrangements and consider whether thy have been structured to circumvent the spirit and intent of the rules. In such circumstances, it may be appropriate to "deem" such person/entity as connected person under Rule 2.04.

16. In the present case, should the Parent Shareholders hold shares in Company A directly instead of through Parent Company, Shareholder X and Shareholder Y would be substantial shareholders of Company A under Rule 1.01. There was a question of whether the structure of Parent Company was a means to circumvent the Listing Rules, and if yes, it would be necessary to "look through" the structure of Parent Company and deem the Parent Shareholders as connected persons of Company A. In making the determination, the Exchange had taken into account the following factors:

- Parent Company had a number of business activities and it was not a single purpose undertaking established for the sole and dominant purpose of holding its investment in Company A.

- Other than their interests in Parent Company, the three groups of Parent Shareholders were independent from each other. The Shareholders' Agreement governed the relationship of the Parent Shareholders in respect of Parent Company and the approval/veto rights of the Parent Shareholders on certain significant matters concerning the Parent Company and its subsidiaries (including Company A). While each group of Parent Shareholders was able to exert influence over the Parent Company through its approval/veto rights under the Shareholders' Agreement, there was no evidence indicating that the Parent Shareholders must act together or in the same direction in respect of matters relating to Company A.

17. Based on the facts of the case, there were no suggestions that the structure of Parent Company and the Shareholders' Agreement were designed to circumvent the Listing Rules. The Exchange considered that the then relationship among the Parent Shareholders was not sufficient to warrant the Exchange exercising its power to deem the Parent Shareholders as connected persons of Company A.

18. Notwithstanding the above, the Exchange noted that minority shareholders of Company A could be potentially disadvantaged if the Parent Shareholders were to act together and cause Company A to enter into transactions with either one of them which minority shareholders might have been minded to vote against if they had the right to do so. The Exchange therefore reminded Company A that in future, subject to the specific facts and circumstances of a particular transaction, the Exchange might exercise its power to regard the Parent Shareholders or any of them as connected person(s).

Conclusion

19. The Exchange determined that none of the Parent Shareholders were core connected persons or connected person of Company A under Rules 1.01 and 14A.07 by virtue of their substantial interests in Parent Company.

20. The Exchange reminded Company A that in future, subject to the specific facts and circumstances of a particular transaction, the Exchange might exercise its power to regard the Parent Shareholders or any of them as connected person(s).

Whether the Exchange would deem a party as a connected person of the listed issuer in respect of a proposed transaction that involved such party acquiring from both the listed issuer and its controlling shareholder their respective interests in the same property

Parties

- **Company A** – a Main Board listed company
- **Mr. X** – the Chairman and controlling shareholder of Company A
- **Purchaser** – an independent third party

Facts

1. Company A was the beneficial owner of the whole block of Building Z, except for the ground floor which was beneficially owned by Mr. X.

2. The Purchaser entered into two agreements (the **Agreements**) with Company A and Mr. X separately for the acquisitions of their respective interests in Building Z (**Transaction A** and **Transaction X** respectively) on the same day with the intention to redevelop Building Z.

3. Company A submitted that the Purchaser was introduced by a real estate agent to Company A and Mr. X separately. At the request of the Purchaser, the Agreements were inter-conditional and were scheduled to complete simultaneously.

4. Mr. X was not personally involved in the negotiation process for the agreement between Company A and the Purchaser (the **Company Agreement**). Other members of Company A's management team represented Company A during the negotiation process and, thereafter, presented a draft of the Company Agreement to the board of Company A for consideration and approval. Mr. X attended the relevant board meeting at which the Company Agreement was approved. Before the board voted for the resolution approving the Company Agreement, Mr. X had declared his interest in Transaction X and that he had no material interest in the Company Agreement.

5. In respect of Transaction X, Company A submitted that Mr. X entered into the relevant agreement after his negotiation with the real estate agent and the Purchaser without involving any other members of the board or management team of Company A.

Relevant Listing Rules

6. Main Board Listing Rule 14A.20 provides that:

   A deemed connected person includes a person:

   (1) who has entered, or proposes to enter, into:

      (a) a transaction with the listed issuer's group; and

      (b) an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with a connected person described in rule 14A.07(1), (2) or (3) with respect to the transaction; and

   (2) who, in the Exchange's opinion, should be considered as a connected person.

7. Main Board Listing Rule 14A.25 provides that:

   Any transaction between a listed issuer's group and a connected person is a connected transaction.

Analysis

8. The connected transaction rules seek to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as the listed issuer's directors, chief executives or substantial shareholders or their associates) taking advantage of their positions to the detriment of minority shareholders of an issuer.

9. Rule 14A.19 provides that the Exchange has the specific power to deem a person to be connected. The power is usually exercised by the Exchange in respect of a particular transaction. In making the determination, the Exchange will consider all relevant facts and circumstances surrounding the transaction and whether the interests of shareholders as a whole are taken into account by the listed issuer when it enters into the transaction. Particular regard would be given to the substance rather than the form of the transaction and any arrangements that are designed to circumvent the spirit and intent of the connected transaction rules.

10. Rules 14A.20 and 14A.21 set out certain specific circumstances where the Exchange may exercise its power to deem a person to be connected. Rule 14A.20 is intended to cover situations where the connected person may be in a position to exercise significant influence in a transaction between the listed issuer and a third party and/or where the connected person stands to benefit from the transaction because the connected person has entered, or proposes to enter, into any arrangement with that third party with respect to that transaction.

11. The Exchange decided to exercise its power to deem the Purchaser as a connected person in respect of Transaction A under Rule 14A.20. In making the determination, the Exchange had taken into accounts the following factors:

- The case involved Company A and Mr. X (being a connected person) entering into agreements with the same person for disposing of their respective interests in the same building. Transaction A and Transaction X were related to each other and fell under the circumstances described in Rule 14A.20. In particular, the inter-conditionality of the Agreements represented an arrangement between the Purchaser and Mr. X described in Rule 14A.20.

- Mr. X took part in Company A's decision making process of, and approved, the Company Agreement. Mr. X also negotiated with, and entered into Transaction X with the Purchaser. The Company Agreement and the agreement in respect of Transaction X could not be viewed separately and the circumstances suggested that it was possible for Mr. X to influence the terms of Transaction A in a way to obtain an advantage in Transaction X.

12. Company A submitted that (i) there were commercial reasons for the Purchaser to enter into transactions with both Company A and Mr. X and require the Agreements to be inter-conditional; (ii) Transaction A and Transaction X were negotiated separately; (iii) Mr. X was not involved in the negotiation between Company A and the Purchaser/estate agent in respect of Transaction A; (iv) Mr. X had declared his interest at the relevant board meeting before the board voted for the resolution to approve Transaction A; and (v) the consideration receivable by Company A under Transaction A was higher than the market value of its interests in Building Z as valued by an independent valuer. However, the Exchange did not consider these mitigating factors be sufficient to warrant the Exchange to reach a different conclusion.

Conclusion

13. Based on the above analysis, the Exchange determined that the Purchaser should be deemed as a connected person of Company A in respect of Transaction A under Rule 14A.20. Accordingly, Transaction A constituted a connected transaction of Company A under Rule 14A.25.

Whether the Exchange would deem a REIT as a connected person of the listed issuer in respect of a proposed transaction that involved the listed issuer and its controlling shareholder injecting their assets into the REIT and subscribing units issued by the REIT

Parties

- **Company A** – a Main Board listed issuer
- **Parent Shareholder** – a substantial shareholder of Company A
- **REIT** – a real estate investment trust and prospective new applicant for listing on the Exchange

Facts

1. Company A and its subsidiaries (the **Group**) were principally engaged in property development, investment and management.

2. A majority of the shareholding interest in Company A was owned by the Parent Shareholder.

3. The REIT was proposed to be constituted as a unit trust and its units (the **Units**) would be listed on the Exchange through an initial public offering (the **Offering**).

4. The trustee of the REIT (the **Trustee**) was proposed to be a professional trustee company which would hold the assets of the REIT for the benefit of the Unit holders and would have the power to, among others, acquire properties as investments and enter into agreements on behalf of the REIT.

5. The manager of the REIT (the **Manager**) would be a wholly-owned subsidiary of Company A. The Manager would be responsible for managing and investing the REIT's assets (including acquiring and disposing of assets by the REIT) for the benefit of the Unit holders.

6. For the purposes of the listing of the Units, it was proposed that:

    - the REIT's initial property portfolio would comprise properties to be acquired from the Group and the Parent Shareholder and the REIT would enter into separate agreements with the Group and with the Parent Shareholder in respect of each acquisition. Completion of each acquisition would be conditional on the Offering.

- each of the Group and the Parent Shareholder would also enter into a subscription agreement with the REIT for the subscription of certain Units for cash which was also conditional on the Offering. Immediately after the Offering, the Units to be held by the Group and the Parent Shareholder would be, in aggregate, less than 30% of the total Units then in issue.

The disposal of the Group's property interests to the REIT and the subscription of the Units by the Group are referred as the **Company Transactions**. The disposal of the Parent Shareholder's property interests to the REIT and the subscription of Units by the Parent Shareholder are referred as the **Parent Transactions**. The Company Transactions and the Parent Transactions are collectively referred as the **Transactions**.

Relevant Listing Rules

7. Main Board Listing Rule 14A.19 provides that:

   The Exchange has the power to deem any person to be a connected person.

8. Main Board Listing Rule 14A.20 provides that:

   A deemed connected person includes a person:

   (1) who has entered, or proposes to enter, into:

      (a) a transaction with the listed issuer's group; and

      (b) an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with a connected person described in rule 14A.07(1), (2) or (3) with respect to the transaction; and

   (2) who, in the Exchange's opinion, should be considered as a connected person.

Analysis

9. The connected transaction rules seek to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as the listed issuer's directors, chief executives or substantial shareholders or their associates) taking advantage of their positions to the detriment of minority shareholders of an issuer.

10. Rule 14A.19 provides that the Exchange has the specific power to deem a person to be connected. This power is usually exercised by the Exchange in respect of a particular transaction. In making the determination, the Exchange will consider all relevant facts and circumstances surrounding the transaction and whether the interests of shareholders as a whole are taken into account by the listed issuer when it enters into the transaction. Particular regard would be given to the substance rather than the form of the transaction and any arrangements that are designed to circumvent the spirit and intent of the connected transaction rules.

11. Rules 14A.20 and 14A.21 set out certain specific circumstances where the Exchange may exercise its power to deem a person to be connected. Rule 14A.20 is intended to cover situations where the connected person may be in a position to exercise significant influence in a transaction between the listed issuer and a third party and/or where the connected person stands to benefit from the transaction because the connected person has entered, or proposes to enter, into any arrangement with that third party with respect to that transaction.

12. In considering whether the REIT should be deemed as a connected person of Company A in respect of the Company Transactions under Rule 14A.20, the Exchange had taken into account the proposed REIT structure, the relationship of the Manager with Company A and the Parent Shareholder, and the series of Transactions the REIT proposed to enter into with the Group and the Parent Shareholder leading to the establishment of the REIT and the Offering.

13. The present case involved the Group and the Parent Shareholder (being a connected person) entering into agreements with the same entity for disposing of their respective property interests to, and subscribing the Units issued by, such entity at the same time. The completion of each Transaction and the Offering would be inter-conditional. It was apparent that the Transactions were related to each other and fell under the circumstances described in Rule 14A.20.

14. The Manager, being a subsidiary of Company A, was ultimately controlled by the Parent Shareholder. Under the proposed REIT structure, the Manager would have the general power of management over the REIT's assets, including any acquisition or disposal of assets by the REIT. The Manager would negotiate with both the Group and the Parent Shareholder on behalf the REIT in respect of the Transactions. The proposed REIT structure and the series of Transactions suggested that it was possible for the Parent Shareholder to influence the Manager and the terms of the Company Transactions in a way to obtain an advantage through the Parent Transactions.

15. Company A had submitted that there would be various safeguards against any conflict of interest arising from the role of the Manager and its relationship with the Parent Shareholder. The Code of Real Estate Investment Trusts required independent valuation of the properties to be acquired from the Group and the Parent Shareholder which was necessary to enable investors in the Units to make an informed assessment of assets to be held by the REIT. Furthermore, the Manager would be subject to the oversight of the Trustee which was a professional trustee company. However, the Exchange considered that such safeguards would primarily serve to protect the interests of the Unit holders but not the sellers of the properties and their minority shareholders. Specifically, the safeguards would not address the potential for a shift of benefits between the Company Transactions and the Parent Transactions by virtue of the Parent Shareholder being in a position to exercise influence over the Company Transactions.

Conclusion

16. Based on the above analysis, the Exchange determined that the REIT should be deemed as a connected person of Company A in respect of the Company Transactions under Rule 14A.20, and that the Company Transactions would constitute connected transactions of Company A under Rule 14A.25.

Definition of connected persons

1. The definitions of "close associate" and "associate" include the trustees, acting in their capacity as trustees, of any trust of which a director, chief executive or substantial shareholder or any of his family / immediate family members is a beneficiary (the beneficiaries). Do the definitions include a scenario where the beneficiaries' interests are held through a company controlled by any of the beneficiaries?

Yes. The definitions cover interests held directly or indirectly by the beneficiaries.

MB Rules 1.01, 14A.12(1)(b), 14A.13(2) and 19A.04
GEM Rules 1.01, 20.10(1)(b), 20.11(2) and 25.04
First released: March 2004; last updated: May 2024

Whether the provision of guarantee by a listed issuer for a bank loan granted to a subsidiary of an associated company was a connected transaction if the substantial shareholder of the issuer directly held a 10 per cent interest in the associated company

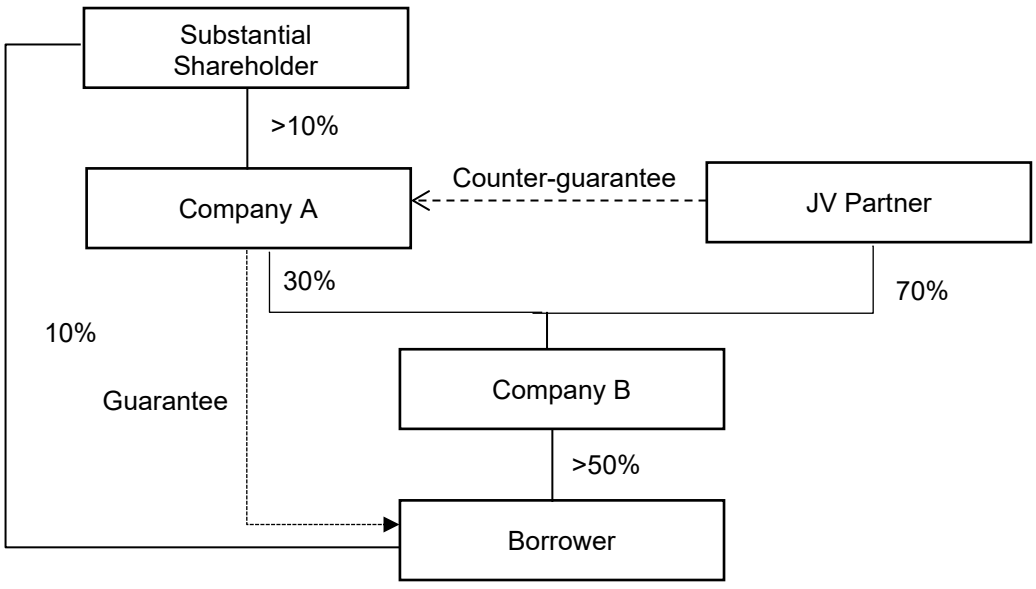
Parties

- **Company A** – a Main Board issuer
- **Company B –** a 30%-owned associated company of Company A
- **Borrower** – a non-wholly subsidiary of Company B
- **Substantial Shareholder** – a substantial shareholder of each of Company A and the Borrower
- **JV Partner** – an independent third party holding a 70% interest in Company B

Facts

1. Company A proposed to provide a guarantee in favour of a bank for a loan facility to be granted to the Borrower (**Proposed Guarantee**). The JV Partner would provide a counter-guarantee in favour of Company A against all its liabilities arising out of the Proposed Guarantee.

2. The simplified shareholding structure is set out below:



3. Company B and the Borrower were associated companies of Company A. Company B was an investment holding company and did not have any operating subsidiaries other than the Borrower.

4. Company A enquired whether the Proposed Guarantee would be subject to the connected transaction requirements under Chapter 14A. It submitted that:

   - the Borrower was not a connected person of Company A; and
   - the Borrower was not a "commonly held entity" falling under Rule14A.27. While the Substantial Shareholder owned 10% interest in the Borrower, neither Company A nor any of its subsidiaries was a shareholder of the Borrower. Company A only had an indirect interest in the Borrower through Company B.

Relevant Listing Rules

5. Rule 14A.19 states that:

   "The Exchange has the power to deem any person to be a connected person."

6. Rule 14A.26 states that:

   "Financial assistance provided by a listed issuer's group to, or received by a listed issuer's group from, a commonly held entity is a connected transaction."

7. Rule 14A.27 states that:

   "A "commonly held entity" is a company whose shareholders include:

   (1) a member of the listed issuer's group; and

   (2) any connected person(s) at the issuer level who, individually or together, can exercise or control the exercise of 10% or more of the voting power at the company's general meeting. This 10% excludes any indirect interest held by the person(s) through the listed issuer."

8. Rule 14A.89 states that:

   "Financial assistance provided by a listed issuer's group to a connected person or commonly held entity is fully exempt if it is conducted:

   (1) on normal commercial terms or better; and

   (2) in proportion to the equity interest directly held by the listed issuer or its subsidiary in the connected person or the commonly held entity.

   Any guarantee given by the listed issuer's group must be on a several (and not a joint and several) basis.
   …"

Analysis

9. The connected transaction Rules seek to safeguard against connected persons taking advantage of their positions to the detriment of the issuer's minority shareholders. Under the Rules, the Exchange may deem a person to be connected in respect of a particular transaction. When applying the deeming provision, the Exchange considers all relevant facts and circumstances surrounding the transaction and has particular regard to the substance and not the form of the transaction and any arrangements designed to circumvent the spirit and intent of the connected transaction Rules.

10. In this case, the Exchange considered that the Proposed Guarantee should be subject to the connected transaction requirements because:

- An issuer providing financial assistance to a commonly held entity is a connected transaction. A commonly held entity is a company whose shareholders include (i) the issuer or any of its subsidiaries; and (ii) any connected person(s) at the issuer level who can, individually or together, control the exercise of 10% or more of the voting power at the company's general meeting.

- The Borrower was held as to 10% by the Substantial Shareholder and over 50% by Company A and the JV Partner through Company B. As Company B was mainly a vehicle for holding shares in the Borrower, the Exchange considered it necessary to "see through" the structure of Company B and deem the Borrower as a commonly held entity.

- Company A would guarantee the entire loan facility to be granted to the Borrower. This would confer a benefit on the Substantial Shareholder through its substantial interest in the Borrower.

Conclusion

11. The Proposed Guarantee was subject to the connected transaction requirements under Chapter 14A.

Whether the placing of deposits by a listed issuer with banks, being subsidiaries of a substantial shareholder of the issuer, was a connected transaction

Parties

- **Company A** – a Main Board listed company
- **Banks** – subsidiaries of a substantial shareholder of Company A

Facts

1. Company A and its subsidiaries (**Group**) were principally engaged in a variety of businesses including property development and investment, hospitality and leisure, and asset management and investment.

2. In its ordinary and usual course of business, the Group from time to time maintained term deposits and bank balances with various financial institutions on normal commercial terms for treasury management purposes.

3. Company A submitted that the Banks were financial institutions licensed to carry on banking business in Hong Kong and certain overseas jurisdictions under the legislation or authority in the respective jurisdictions. As part of its treasury activities, the Group would place deposits with the Banks (**Transactions**) in a manner similar to comparable transactions which the Group entered into with other independent financial institutions. The Transactions would be conducted on an arm's length basis and on normal commercial terms.

4. The Banks were subsidiaries of a substantial shareholder of Company A and hence connected persons of Company A.

5. Company A sought the Exchange's view on whether the Transactions would be exempt from the connected transaction requirements for the following reasons:

   (a) According to Listing Decision LD53-2, legitimate treasury activities should be treated as bona fide transactions to utilise surplus cash reserves, and the Exchange considered that Rule 14.04(1)(g) should be interpreted to exempt treasury activities where the issuer has a clearly stated and established treasury policy and transactions are conducted in accordance with the treasury policy.

Company A submitted that it had established a treasury policy to utilise the Group's surplus cash reserves. The placing of deposits by the Group with various licensed banks, including the Banks, had been and would continue to be conducted according to the established treasury policy. Following the guidance set out in Listing Decision LD53-2, the Transactions would form part of the legitimate treasury activities of the Group and be exempt from the notifiable transaction requirements under Rule 14.04(1)(g).

There was a question whether the Transactions would also be excluded under Chapter 14A and therefore exempt from the connected transaction requirements on the basis that they were regarded as bona fide transactions in the ordinary and usual course of business of the Group.

(b) Alternatively, Company A considered that the exemption under Rule 14A.87(1) applied to the Transactions.

Under Rule 14A.87(1), financial assistance provided by a banking company in its ordinary and usual course of business to a connected person on normal commercial terms was exempt from the reporting, announcement and independent shareholders' approval requirements under Chapter 14A.

In this case, the Transactions involved the Group placing deposits with connected persons and were regarded as provision of financial assistance by the Group to the connected persons under Chapter 14A. Although Company A and its subsidiaries were not banking companies, Company A considered that Rule 14A.87(1) should provide relief given that the Transactions formed part of the treasury activities of the Group in its ordinary and usual course of business. The Transactions were also in the ordinary and usual course of business of the respective Banks which were "banking companies" as defined in Rule 14A.88.

Relevant Listing Rules

6. Rule 14.04(1) states that for the purposes of Chapter 14, any reference to a "transaction" by a listed issuer:

(a) includes the acquisition or disposal of assets, including deemed disposals as referred to in rule 14.29.

…

(g) to the extent not expressly provided in rules 14.04(1)(a) to (f), excludes any transaction of a revenue nature in the ordinary and usual course of business (as referred to in rule 14.04(8)) of the listed issuer.

7. Rule 14A.06 provides the meaning of the following terms:

…

(17) "financial assistance" has the meaning in rule 14A.24(4);

…

(26) "normal commercial terms or better" are terms which a party could obtain if the transaction were on an arm's length basis or terms no less favourable to the listed issuer's group than terms available to or from independent third parties;

…

(28) "ordinary and usual course of business" of an entity means the entity's existing principal activities or an activity wholly necessary for its principal activities; …

…

(38) a "transaction" has the meaning in rule 14A.24

…

8. Rule 14A.24 provides that:

"Transactions" include both capital and revenue nature transactions, whether or not conducted in the ordinary and usual course of business of the listed issuer's group. This includes the following types of transactions:

(1) …

…

(4) granting an indemnity or providing or receiving financial assistance. "Financial assistance" includes granting credit, lending money, or providing an indemnity against obligations under a loan, or guaranteeing or providing security for a loan; …

9. Rule 14A.25 provides that:

Any transaction between a listed issuer's group and a connected person is a connected transaction.

10. Rule 14A.87 provides that:

For any financial assistance provided by a banking company in its ordinary and usual course of business to a connected person or a commonly held entity:

(1) the transaction is fully exempt if it is conducted on normal commercial terms or better;

…

11. Rule 14A.88 provides that:

A "banking company" is a listed issuer or its subsidiary which is a bank, a restricted licence bank or a deposit taking company as defined in the Banking Ordinance, or a bank constituted under appropriate overseas legislation or authority.

12. Listing Decision LD53-2 provides that:

> The Exchange takes the view that legitimate short-term investments for treasury management purposes are not intended to fall within the ambit of the Chapter 14 rules. The Exchange also notes that given this position transactions could be devised to appear to be for treasury purposes in an attempt to defeat or circumvent the purpose of the notification and shareholder approval requirements in Chapter 14. Therefore an analysis would be required on a case by case basis to differentiate transactions and arrangements caught by the scope of Chapter 14 of the Listing Rules from those exempt.
>
> The Exchange considered that legitimate treasury activities should be treated as bona fide transactions for the purpose of utilizing surplus cash reserves. In general, investments for treasury purposes should be in liquid stocks and short-term in nature. Listing Rule 14.04(1)(g) excludes any transaction of a revenue nature in the ordinary and usual course of business from the scope of Chapter 14 of the Listing Rules. The Exchange considered that Listing Rule 14.04(1)(g) should be interpreted to exempt treasury activities where the listed issuer has a clearly stated and established a treasury policy and transactions contemplated are conducted in accordance with such treasury policy.

Analysis

13. Each of Chapter 14 and Chapter 14A provides specific guidance on the "transactions" subject to the notifiable transaction rules and connected transaction rules respectively. Unlike Chapter 14, Chapter 14A includes transactions of a revenue nature in the ordinary and usual course of business. This difference in the definition of "transactions" is clearly stated in Rule 14A.24.

14. In this case, the Transactions would be entered into between the Group and the Banks which were connected persons of Company A. The Transactions therefore constituted connected transactions for Company A. Under Rule 14A.24, whether or not the Transactions were of a revenue nature in the ordinary and usual course of business is irrelevant to the applicability of Chapter 14A to the Transactions. Company A had to comply with the connected transaction rules in Chapter 14A.

15. Under Rules 14A.87(1) and 14A.88, financial assistance provided by a banking company in its ordinary and usual course of business to a connected person on normal commercial terms is exempt from the connected transaction requirements. The exemption caters for a banking company whose principal business is subject to prudential supervision by a regulatory body. The Transactions did not fall into the exemption as Company A and its subsidiaries were not banking companies.

Conclusion

16. The Transactions were connected transactions subject to Chapter 14A of the Listing Rules.

Note: The Listing Decision LD53-2 (as referred to in paragraph 5(a) above) was withdrawn after the amendments to Rule 14.04(1)(g) with effect from 1 October 2019.

Whether the provision of management services by a listed issuer for a residential complex was a connected transaction if its substantial shareholder owned a majority of the undivided shares in the complex

Parties

- **Company A** – a listed company
- **Shareholder X** – the substantial shareholder of Company A
- **Body of Owners** – an unincorporated entity which comprised all owners of the undivided shares in the Complex
- **Company Y** – one of the owners of the undivided shares in the Complex, and a company controlled by Shareholder X
- **Management Company** – the building manager of the Complex, and a company controlled by Shareholder X

Facts

1. The principal activities of Company A and its subsidiaries (the **Group**) included providing hotel and clubhouse management services.

2. The Body of Owners was an unincorporated entity which comprised all owners of the undivided shares in a residential complex (the **Complex**). It was organised to manage the common areas of the Complex and consider matters of common interest to the owners, and it did not carry on a trade or business.

3. The Management Company was a building management company appointed under the Deed of Mutual Covenants (the **DMC**) of the Complex to act as agent for the Body of Owners.

4. Company Y was one of the owners of the Complex, and was interested in approximately 60% of the undivided shares in the Complex.

5. Company A submitted that the Group was awarded a contract for management of the Complex clubhouse by tender. The Group would enter into the management contract with the Management Company (as an agent for the Body of Owners) for the provision of management services to the clubhouse of the Complex at a fixed monthly fee for two years (the **Transaction**).

6. While the Management Company and Company Y were associates of Shareholder X and therefore connected persons of Company A, Company A argued that the Transaction did not constitute a connected transaction for Company A because:

   - The Management Company only acted as an agent of the Body of Owners in respect of the Transaction.

   - The case involved a transaction between the Group and the Body of Owners. Notwithstanding Company Y's 60% interest in the undivided shares in the Complex, the Body of Owners was not an "associate" of Shareholder X because it was neither a "company" nor a "subsidiary" under the definition of associates in the Listing Rules.

   - Further, an owners' committee had been established to represent the Body of Owners under the DMC. In respect of the Management Contract, the Management Company had provided the tenders from various service providers to the owners' committee for consideration, and the owners' committee resolved to award the Management Contract to the Group. At the relevant time, members representing Company Y did not form a majority of the members of the owners' committee, and Company Y did not control the decision of the owners' committee.

7. It was also noted from the information provided by Company A that the management of the Complex was mainly carried out by the owners' committee (the members of which were elected by the owners of the Complex) or the Management Company (as the building manager appointed under the DMC) according to the relevant statutory requirements and the DMC. Important matters were considered and resolved at general meetings of the Body of Owners. At the general meetings, each owner had one vote in respect of each undivided share that he owned, and resolutions were passed by a majority of votes.

Relevant Listing Rules

8. Rule 14A.13 provides that an "associate" of a connected person which is a company includes:

   (1) …
   …

   (3) a 30%-controlled company held, directly or indirectly, by the company…

9. Rule 14A.06(1) defines "30%-controlled company" to mean:

   a company held by a person who can:

   (a) exercise or control the exercise of 30% …or more of the voting power at general meetings; or…

10. Rule 1.01 defines "company" to mean:

    a body corporate wherever incorporated or otherwise established.

11. Rule 14A.07 defines "connected person" to mean:

(1) a director, chief executive or substantial shareholder of the listed issuer or any of its subsidiaries;

…

(4) an associate of any of the above persons;…

12. Rule 14A.25 provides that:

Any transaction between a listed issuer's group and a connected person is a connected transaction.

Analysis

14. The connected transaction rules seek to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as directors, chief executives or substantial shareholders or their associates) taking advantage of their positions to the detriment of the minority shareholders.

15. In this case, Shareholder X was a substantial shareholder of Company A and a transaction between the Group and Shareholder X or any of his associates constituted a connected transaction for Company A under the Listing Rules.

16. The Exchange noted Company A's view that the Body of Owners would not fall under the definition of associates in Rule 14A.13 as it was not a "company" had taken a narrow and strict legalistic approach to the application of the Listing Rules.

17. Under Rule 14A.13, associates of Shareholder X would include any *company* in the equity capital of which Shareholder X was directly or indirectly interested so as to exercise or control the exercise of 30% or more of the voting power at general meetings, or to control the composition of a majority of the board of directors. The Exchange noted that while the Body of Owners, being an unincorporated entity, was not a company, Shareholder X (through his interest in Company Y which held 60% of the undivided shares in the Complex) was able to control the exercise of 60% of the voting power at the general meetings of the Body of Owners as well as the composition of a majority of the owners' committee of the Complex. The Transaction was analogous to a transaction between the Group and a company controlled by Shareholder X where the connected person was in a position to take advantage to the detriment of the minority shareholders. The Exchange considered it appropriate to take a purposive approach in this case to ensure that the spirit and intent of the Listing Rules were adhered to. Accordingly, the Body of Owners was treated as an associate of Shareholder X in respect of the Transaction.

18. Given that the Management Contract was entered into between the Group and the Management Company (as an agent for the Body of Owners), and both the Body of Owners and the Management Company were associates of Shareholder X and therefore connected persons of Company A, the Transaction constituted a connected transaction for Company A.

Conclusion

19. The Transaction constituted a connected transaction for Company A.

Whether the proposed amendments to a non-competition undertaking given by the controlling shareholder to the listed issuer constituted a connected transaction

Parties

- **Company A** – a Main Board listed issuer
- **Newco** – a subsidiary of Company A before the proposed spin-off
- **Holding Company** – the controlling shareholder of Company A

Facts

1. Company A proposed to spin-off Newco for a separate listing on the Exchange. The proposal would involve Company A distributing all its interest in Newco in specie to the existing shareholders. Upon completion of the proposal, Company A would no longer hold any interest in Newco. Newco would become a connected person of Company A as the Holding Company would hold more than 50% interest in it.

2. Newco was principally engaged in the manufacturing and sale of certain products (the **Newco Business**).

3. At the time of Company A's new listing on the Exchange, the Holding Company and Company A had entered into a non-competition deed (the **Original Non-Competition Deed**), under which the Holding Company had undertaken to Company A not to, directly and indirectly, carry on or be engaged or interested in the principal businesses of Company A including the Newco Business.

4. In order to delineate the businesses of the Holding Company, Company A and Newco upon completion of the proposed spin-off, the parties would enter into the following non-competition arrangement (the **Revised Non-Competition Arrangement**):

    - the Holding Company and Company A would amend the Original Non-Competition Deed to exclude the Newco Business from the deed; and

    - the Holding Company would undertake to Newco not to, directly and indirectly, carry on or be engaged or interested in the Newco Business. While Company A would not be a party to such undertaking, the Holding Company would exercise its influence on Company A so as to cause Company A to comply with the undertaking.

5. There was an issue whether the Revised Non-Competition Arrangement would constitute a connected transaction for Company A, and if so, whether the de minimis exemption would apply as Company A considered that the arrangement was made on normal commercial terms and no consideration would be paid or received by it.

Relevant Listing Rules

6. Rule 14A.01 states that:

"This Chapter applies to connected transactions entered into by a listed issuer or its subsidiaries. The connected transaction rules ensure that the interests of shareholders as a whole are taken into account by the listed issuer when the listed issuer's group enters into a connected transaction."

7. Rule 14A.25 states that:

"Any transaction between a listed issuer's group and a connected person is a connected transaction."

8. Rule 14A.36 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."

9. Rule 14A.76 states that:

"This exemption applies to a connected transaction (other than an issue of new securities by the listed issuer) conducted on normal commercial terms or better as follows:

(1) The transaction is fully exempt if all the percentage ratios (other than the profits ratio) are:

(a) less than 0.1%;

(b) …; or

(c) less than 5% and the total consideration…is less than HK$3,000,000.

(2) The transaction is exempt from the circular (including independent financial advice) and shareholders' approval requirements if all the percentage ratios (other than the profits ratio) are:

(a) less than 5%; or

(b) less than 25% and the total consideration…is less than HK$10,000,000."

(Rule 14A.76 was amended on 11 June 2024. See Note below.)

Analysis

10. In this case, Company A and the Holding Company proposed to enter into the Revised Non-Competition Arrangement which would confer a benefit on the Holding Company and its associates. It was a connected transaction for Company A.

11. The Revised Non-Competition Arrangement would restrict Company A from engaging in certain businesses, and the value of the transaction could not be quantified in monetary terms. The Exchange did not agree that the transaction would qualify for the de minimis exemption.

Conclusion

12. The Revised Non-Competition Arrangement required independent shareholders' approval under Chapter 14A.

Note: Rule 14A.76 was amended on 11 June 2024 to clarify that the de minimis exemption does not apply to a sale or transfer of treasury shares by a listed issuer. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would disregard the revenue ratio for a disposal of a target company whose business was different from the principal businesses of the listed issuer

Parties

- **Company A** – a Main Board issuer
- **Holding Company** – the holding company of Company A

Facts

1. Company A was principally engaged in the provision of banking and financial services.

2. In addition to Company A, the Holding Company was also the holding company of a group of companies engaged in insurance businesses.

3. In year 2005, Company A had acquired from a third party vendor (the **Vendor**) the entire equity interest in Target X (which was principally engaged in the provision of banking and financial services) together with about 95% of the equity interest in Target Y (which was principally engaged in insurance businesses) (the **Acquisition**).

4. At the time of the Acquisition, Company A had stated its intention to transfer the interest in Target Y to the Holding Company following the completion of the Acquisition. Nevertheless, Company A and the Holding Company had not entered into any contractual or binding arrangements in respect of the transfer of interest in Target Y to the Holding Company.

5. In year 2006, Company A proposed to enter into an agreement with the Holding Company for the transfer of its 95% equity interest in Target Y to the Holding Company (the **Transaction**).

6. In respect of the proposed Transaction, the assets ratio and profits ratio were less than 1%. The consideration ratio was about 2.1% and the revenue ratio was about 10%.

7. Company A submitted the following information to support its request to disregard the revenue ratio in respect of the Transaction under Rules 14.20 and 14A.80:

    - The calculation of the revenue ratio produced an anomalous result given that the revenue ratio was approximately 10% but the other percentage ratios were all below 2.5%.

    - The revenue ratio was not appropriate to the sphere of activity of Company A because of the difference in what constituted “revenue” for a banking company and an insurance company. It was not meaningful to compare the interest income of a bank with the premium income of an insurance company.

- The Acquisition and the proposed Transaction formed part of a single transaction. Company A's intention to transfer Target Y to the Holding Company was supported by the following facts:

  - the financial results of Target Y were not consolidated in Company A's accounts for the year 2005 given Company A's intention to transfer Target Y to the Holding Company; and

  - under the proposed Transaction, Target Y would be transferred to the Holding Company at cost plus interest payment determined with reference to the one-month HIBOR for the period during which the interest in Target Y was held by Company A.

8. Company A submitted some alternative size tests to the Exchange which compared (i) the premium income of Target Y with the interest earning loans of Company A or new deposits collected by Company A; (ii) the number of employees; or (iii) the net asset values.

Relevant Listing Rules

9. Main Board Listing Rule 14.07(3) provides that a "revenue ratio" refers to:

   the revenue attributable to the assets which are the subject of the transaction divided by the revenue of the listed issuer ….

10. Main Board Listing 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.:

11. Main Board Listing 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

12. Rule 14.07 sets out five percentage ratios for assessing the impact of a transaction on the listed issuer from different perspectives. The revenue ratio serves to assess the impact of a transaction on the listed issuer by measuring the relative level of activity of the target being acquired or disposed of against that of the listed issuer.

13. The percentage ratio calculation forms 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. A connected transaction on normal commercial term is exempt from shareholders' approval requirements if each of the percentage ratios (other than the profits ratio) is less than 2.5% (Note 1) .

14. When considering Company A's request to disregard the revenue ratio in respect of the proposed Transaction, the Exchange had taken into account the following factors:

- The revenue ratio indicated that the Transaction was of a material size that required independent shareholders' approval under Chapter 14A. This was not out of line with the results of other percentage ratios. In particular, the Exchange noted that the consideration ratio was close to the 2.5% (Note 1) threshold requiring independent shareholders' approval. The Exchange did not consider the result of the revenue ratio to be anomalous.

- The revenue ratio measured the impact of the Transaction on Company A by comparing the revenue generated from the principal activity of each of Target Y and Company A. While Target Y was engaging in a line of business different from Company A's principal activity, it did not mean that the calculation of the revenue ratio would be inappropriate in the sphere of activity of Company A. It was not uncommon for listed issuers to acquire or dispose of businesses that were not in line with the issuers' principal activities. The Exchange did not consider that Company A had provided compelling grounds to substantiate its case and declined to exercise its power under Rules 14.20 and 14A.80 to modify the percentage ratio calculation.

- At the time of the Acquisition, Company A and the Holding Company had not entered into any contractual or binding arrangements in respect of the transfer of interest in Target Y to the Holding Company. Although Company A had stated its intention to effect the transfer following the Acquisition, the proposed Transaction could not be viewed as part of the Acquisition in which Company A had complied with the Rule requirements. Accordingly, when Company A entered into the Transaction, it was required to comply with the Rule requirements which were assessed based on the terms of that transaction. The Exchange did not consider the circumstances of this case be exceptional that warranted the Exchange to disregard any percentage ratios.

15. The Exchange was not satisfied with the alternative tests submitted by Company A as they could not provide a meaningful measure of the relative level of activity of Target Y against that of Company A.

Conclusion

16. Based on the above analysis, the Exchange determined that it was inappropriate to disregard the revenue ratio in respect of the Transaction under Rules 14.20 and 14A.80.

Notes:

1. *Effective from 3 June 2010, the threshold for exempting a connected transaction from the independent shareholder approval requirement has been increased from 2.5% to 5%.*

2. *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.

Whether the Exchange would accept the alternative revenue ratio proposed by a listed issuer due to a change in its accounting policy for jointly controlled entities

Parties

- **Company A** – a Main Board listed issuer
- **JCEs** – entities under the joint control of Company A and other venturers

Facts

1. Company A manufactured and sold automobiles in the Mainland through various JCEs. At the time of new listing of Company A, the Exchange imposed certain post-listing conditions on it with a view to regulating the JCEs (including new JCEs established after listing) in a manner consistent with regulating subsidiaries under the Rules.

2. In the last financial year, Company A changed its accounting policy and accounted for the JCEs using the equity method of accounting. Before the change, Company A had recognized its investments in the JCEs using the proportionate consolidation method (that is, the group combined its share of the JCEs' individual income and expenses, assets and liabilities and cash flows on a line-by-line basis).

3. As a result of the change in accounting policy, the revenue shown in Company A's latest published consolidated accounts (**Published Revenue**) no longer included its share of the JCEs' revenue.

4. Company A submitted that as it operated its business under a jointly controlled entity structure, using the Published Revenue as the denominator for calculating the revenue ratio would produce anomalous results and would not properly reflect the materiality of a transaction to Company A.

5. It therefore proposed to adopt an alternative revenue ratio for classifying its transactions where the denominator would be the sum of the Published Revenue and its share of the JCEs' revenue, with adjustments to eliminate the revenue from transactions between the JCEs and Company A (or its subsidiaries) (**Alternate Revenue**). This would assimilate the group's revenue as if the JCEs were still accounted for using the proportionate consolidation method. The figures used to calculate the Alternative Revenue would be disclosed in Company A's published accounts.

Relevant Listing Rules

6. Main Board Rule 14.04(9) states that:

   "percentage ratios" means the percentage ratios set out in rule 14.07, and "assets ratio", "profits ratio", "revenue ratio", "consideration ratio" and "equity capital ratio" shall bear the respective meanings set out in rule 14.07;

7. Main Board Rule 14.07(3) states that:

   Revenue ratio — the revenue attributable to the assets which are the subject of the transaction divided by the revenue of the listed issuer (see in particular rules 14.14 and 14.17);

8. Main Board Rule 14.14 states that:

   "Revenue" normally means revenue arising from the principal activities of a company and does not include those items of revenue and gains that arise incidentally. In the case of any acquisition or disposal of assets (other than equity capital) through a non wholly owned subsidiary, the revenue attributable to the assets being acquired or realised (and not the listed issuer's proportionate interest in such revenue) will form the numerator for the purpose of the revenue ratio (See also rule 14.17).

9. Main Board Rule 14.17 states that:

   The profits (see rule 14.13) and revenue (see rule 14.14) figures to be used by a listed issuer for the basis of the profits ratio and revenue ratio must be the figures shown in its accounts…

10. Main Board Rule 14.20 states 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.

11. Main Board 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.

12. Main Board Rule 14A.06(30) states that:

    "percentage ratios" has the meaning set out in rule 14.04(9);

Analysis

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

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

15. Here the substantial decrease in revenue as shown in Company A's consolidated accounts was due to the change in accounting policy. There was no change in its principal business or operating model.

16. Company A's business was mainly carried out under a jointly control entity structure, and the JCEs were treated and regulated as if they were Company A's subsidiaries for the purpose of the Rules. When assessing the materiality of a transaction using the revenue ratio, it would be reasonable to take into account the group's share of the JCEs' revenue.

Conclusion

17. The Exchange accepted Company A's proposal to use the Alternative Revenue in place of the Published Revenue when calculating the revenue ratio.

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 result 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.

In respect of a placing and top-up subscription proposed by a listed subsidiary, whether the listed parent was allowed to calculate the percentage ratios for its disposal and acquisition of interests in the subsidiary on a net basis, and if not, whether a waiver from the major transaction requirements would be granted

Parties

- **Company X** – a Main Board listed company**,** and the controlling shareholder of Company Y
- **Company Y** – another Main Board listed company

Facts

1. Company X, Company Y and a placing agent entered into a placing and subscription agreement (the **Agreement**) under which Company X agreed to place a certain number of its existing shares in Company Y to independent investors at a fixed price (the **Placing**) and to subscribe for the same number of new shares to be issued by Company Y at the placing price (the **Top-up Subscription**).

2. The Placing was unconditional. Completion of the Placing would take place a few days after the execution of the Agreement.

3. Completion of the Top-up Subscription was subject to various conditions, including completion of the Placing, Exchange approval for listing the new shares to be issued by Company Y under the Top-up Subscription, and a whitewash waiver being granted to Company X by the Executive Director of the Corporate Finance Division of the Securities and Futures Commission (**SFC**) under the Takeovers Code.

4. The Top-up Subscription constituted a connected transaction for Company Y under Chapter 14A. The Top-up Subscription would be exempt from all connected transaction requirements under Rule 14A.92(4) if it could be completed within 14 days after the execution of the Agreement.

5. Company X's shareholding in Company Y would decrease from 46% to 36% as a result of the Placing, but would be increased to 42% upon completion of the Top- up Subscription. When applying the percentage ratios to each of the Placing and Top-up Subscription, the transaction would constitute a major transaction for Company X under Chapter 14.

6. Company X submitted that the purpose of the Placing was to facilitate Company Y's funding raising, and Company Y would issue its new shares to Company X shortly after the Placing. When considering the Placing and the Top-up Subscription as a whole, there would be a net disposal of a 4% interest in Company Y. Company X was of the view that the net effect of the Placing and the Top-up Subscription should be considered in applying the percentage ratios for transaction classification.

7. Company X also requested that, if the Exchange disagreed with its view on the application of the classification rules, the Exchange grant a waiver from the major transaction requirements in respect of the Placing and the Top-up Subscription.

Relevant Listing Rules

8. Rule 14.04 provides that for the purposes of Chapter 14:

   (1) any reference to a "transaction" by a listed issuer:

      (a) includes the acquisition or disposal of assets, including deemed disposals as referred to in rule 14.29;

      …

9. Rule 14A.92 provides that:

   An issue of new securities by a listed issuer or its subsidiary to a connected person is fully exempt if:

   …

   (4) the securities are issued under a "top-up placing and subscription" that meets the following conditions:

      (a) the new securities are issued to the connected person:

         (i) after it has reduced its holding in the same class of securities by placing them to third parties who are not its associates under a placing agreement; and

         (ii) within 14 days from the date of the placing agreement;

      (b) the number of new securities issued to the connected person does not exceed the number of securities placed by it; and

      (c) the new securities are issued at a price not less than the placing price. The placing price may be adjusted for the expenses of the placing.

   …

Analysis

10. Under the notifiable transaction rules, when an issuer proposes a transaction, it must consider whether it falls into one of the classifications in the rules. A transaction includes an acquisition or disposal of assets.

11. In this case, although the fund raising by Company Y through a placing and top- up subscription would, if completed, have the same effect upon Company X as a straight placing by Company Y, it was necessary to have regard to the terms of the Placing and the Top-up Subscription in applying the notifiable transaction rules.

12. The Placing was unconditional while the Top-up Subscription was subject to certain conditions. One possible scenario was that after Company X's disposal of its 10% equity interest in Company Y under the Placing, the Top-up Subscription could not be completed. As the Placing and the Top-up Subscription were two transactions for Company X, being a disposal of existing shares in Company Y to third parties followed by a subscription of new shares in the same company, the Listing Rules required Company X to apply the percentage ratios to each of the Placing and the Top-up Subscription to determine the transaction classification.

13. In considering Company X's waiver application, the Exchange took into account the following factors:

    - The Placing had not been completed when the waiver application was being considered by the Exchange.

    - The parties to the Agreement had taken reasonable steps to ensure completion of the Top-up Subscription. In particular, before completion of the Placing, details of the placees had been submitted to the Exchange as required and Company X had applied to the SFC for, and had been granted, a whitewash waiver under the Takeovers Code. The only outstanding conditions precedent to the completion of the Top-up Subscription were (i) completion of the Placing and (ii) the Exchange's approval of the listing of shares in Company Y to be issued under the Top-up Subscription. Accordingly, the Exchange was satisfied that the concern about the Top-up Subscription failing to complete after the Placing had been addressed.

    - If both the Placing and the Top-up Subscription were completed, there would be a net disposal of a 4% equity interest in Company Y and its impact on Company X would not be material. The size of the net disposal would not trigger the notifiable transaction requirements.

    - Company X would disclose information relating to the Agreement in a joint announcement with Company Y.

14. Given the steps taken by the parties to the Agreement, it was unlikely that the Top-up Subscription would fail to complete after the Placing. The Exchange accepted that it would be unduly burdensome for Company X to comply with the major transaction requirements having regard to the overall impact on it. Granting the waiver would be unlikely to result in undue risks to Company X's shareholders.

Conclusion

15. Each of the Placing and the Top-up Subscription was a transaction for Company X. Company X should apply the percentage ratios to each transaction to determine the transaction classification under Chapter 14.

16. The Exchange granted a waiver to Company X from the major transaction requirements in respect of the Placing and the Top-up Subscription.

Whether the Exchange would accept the alternative revenue ratio for certain continuing connected transactions between a newly acquired subsidiary and the substantial shareholder of the listed issuer

Parties

- **Company A** – a Main Board listed issuer
- **Target** – a subsidiary of Company A
- **Company B** – a substantial shareholder of certain subsidiaries of the Target

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.

Relevant 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 result 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.

Definition of connected transactions and calculation of percentage ratios

Provision of financial assistance

1. Is a cash deposit made to a connected person (a finance company approved by regulatory authorities) a notifiable and connected transaction?

Yes. It is a provision of financial assistance by the listed issuer to the connected person.

MB Rules 14.04(1)(e) and 14A.24(4)
GEM Rules 19.04(1)(e) and 20.22(4)
First released: February 2013; last updated: May 2024

2. Is an acquisition of a convertible note from an independent third party a connected transaction if the note is issued by a connected person of the listed issuer?

Yes. Although the counterparty is an independent third party, the acquisition would in substance be providing financial assistance to the listed issuer's connected person.

MB Rules 14A.24(4) and 14A.25
GEM Rules 20.22(4) and 20.23
First released: December 2009; last updated: May 2024

3. A listed issuer proposes to fully guarantee a bank loan obtained by its 90% owned subsidiary. Given that the guarantee indirectly benefits the 10% shareholder of the subsidiary which is a connected person at the subsidiary level, will the provision of the guarantee by the listed issuer be regarded as a connected transaction?

No.

MB Rules 14A.24(4) and 14A.25
GEM Rules 20.24(4) and 20.23
First released: March 2014; last updated: May 2024

4. A listed issuer proposes to grant a loan to its substantial shareholder who has also provided a loan to the listed issuer. Can the loans to and from the substantial shareholder be netted off when calculating the percentage ratios for the financial assistance?

No. The proposed loan should be classified on a standalone basis.

MB Rules 14.07 and 14A.87
GEM Rules 19.07 and 20.87
First released: May 2021; last updated: May 2024

Options

5. A listed issuer holds a call option granted by a third party whom became a connected person subsequent to the grant. Will the exercise of the call option by the listed issuer constitute a connected transaction?

Yes.

MB Rules 14A.24(2)(a), 14A.25 and 14A.79(3)
GEM Rules 20.22(2)(a), 20.23 and 20.77(3)
First released: November 2008; last updated: May 2024

6. If the listed issuer has been granted a right of first refusal to acquire certain assets from the controlling shareholder at a price and on terms to be negotiated between the parties, will the right of first refusal be regarded as an option under MB Rule 14A.06(27) / GEM Rule 20.06(27) and non-exercise of such be subject to the connected transaction requirements?

Given that the terms of the acquisition are subject to further negotiation between the parties, the right of first refusal does not constitute an option under MB Rule 14A.06(27) / GEM Rule 20.06(27). Therefore, the non-exercise of the right of first refusal by the listed issuer does not constitute a non-exercise of an option.

MB Rules 14A.06(27), 14A.24(2)(a) and 14A.61(2)
GEM Rules 20.06(27), 20.22(2)(a) and 20.59(2)
First released: 21 March 2014; last updated: May 2024

Leases where the listed issuer is the lessee

7. A listed issuer recognises a lease with fixed lease payments as a right-of-use asset under HKFRS/IFRS 16.

(i) How should the listed issuer classify the lease under the definition of transaction under the Listing Rules?

The lease should be classified as an acquisition of asset (being the right to use the underlying lease asset).

(ii) How should the listed issuer calculate the percentage ratios?

The assets and consideration ratios apply. The numerator will be the value of the right-of-use asset recognised by the listed issuer (which includes the present value of lease payments) according to HKFRS/IFRS 16.

(iii) If the lessor is a connected person, how should the listed issuer classify the lease under the connected transaction rules?

A fixed term lease is a one-off connected transaction (i.e. an acquisition of capital assets).

MB Rules 14.04(1)(a), 14.04(1)(c), 14.04(1)(d), 14.04(1)(g), 14.07, 14.22, 14.23, 14A.24(1), 14A.24(3) and 14A.31
GEM Rules 19.04(1)(a), 19.04(1)(c), 19.04(1)(d), 19.04(1)(g), 19.07, 19.22, 19.23, 20.22(1), 20.22(3) and 20.29
First released: September 2018; last updated: May 2024

8. The lease payments include (i) a fixed dollar amount (fixed lease payments); and (ii) a variable amount determined as a percentage of the listed issuer's annual sales generated from the leased properties (variable lease payments).

Under HKFRS/IFRS 16, the listed issuer will recognise a right-of-use asset taking into account the fixed lease payments. The actual variable lease payments linked to sales will be recognised as expenses in the listed issuer's profit or loss accounts over the lease term.

(i) How should the listed issuer calculate the percentage ratios for the lease?

The value of the right-of-use asset based on the fixed lease payments should be used as numerator of the assets and consideration ratios. The variable lease payments linked to sales will be expenses incurred by the listed issuer in its ordinary and usual course of business and will not form part of the percentage ratios calculation.

(ii) If the lessor is a connected person, how should the listed issuer classify the lease under the connected transaction rules?

If the lessor is a connected person:

(a) The recognition of a right-of-use asset will constitute a one-off connected acquisition.

(b) The variable lease payments linked to sales will be treated as a continuing connected transaction. The listed issuer is required to set annual caps on the variable lease payments, and calculate the revenue, assets and consideration ratios using the annual cap as the numerator.

The lease will be classified under the connected transaction rules by reference to the largest percentage ratio.

(Note: There are other types of variable lease payments (e.g. variable lease payments depending on an index or rate) that are included in the initial measurement of right-of-use asset under HKFRS/IFRS 16. The treatment would be the same as fixed lease payments for the purpose of the Listing Rules).

MB Rules 14.04(1)(a), 14.07, 14A.24(1) and 14A.31
GEM Rules 19.04(1)(a), 19.07, 20.22(1) and 20.29

First released: December 2018; last updated: May 2024

9. A listed issuer enters into a framework agreement with a connected person to cover a number of lease agreements to be entered into over a period of time (say 3 years). Will the leases under the framework agreement be treated as continuing connected transactions? If yes, how should the listed issuer set the annual caps?

Yes. The annual caps would be set based on the expected total value of the right-of-use assets for leases to be entered into in each year under the framework agreement. Where the leases have variable lease payments linked to sales, the listed issuer must also set annual caps based on the variable lease payments it expects to make each year. The framework agreement will be classified under by reference to the largest percentage ratio.

MB Rules 14A.31 and 14A.53
GEM Rules 20.29 and 20.51
First released: December 2018; last updated: May 2024

Leases where the listed issuer is the lessor

10. Will an operating lease with a connected person be treated as a one-off connected transaction or continuing connected transaction? How should the percentage ratios for the lease be calculated?

The operating lease will be a continuing connected transaction for the listed issuer. The listed issuer should calculate each of the assets, revenue and consideration ratios using the annual cap on the rental income (or the actual annual rental income) as the numerator.

MB Rules 14A.24(3) and 14A.31
GEM Rules 20.22(3) and 20.29
First released: December 2018; last updated: May 2024

Capital contribution into a connected subsidiary

11. Is a capital contribution into a joint venture (a connected subsidiary of the listed issuer) made in proportion to the respective interests into the joint venture a connected transaction?

The capital contribution made by the joint venturer into the connected subsidiary is fully exempt under MB Rule 14A.92(1)/ GEM Rule 20.90(1). However, the capital contribution by the listed issuer into the connected subsidiary is a transaction with a connected person (i.e. the connected subsidiary) subject to the connected transaction requirements.

MB Rules 14A.16(1), 14A.25 and 14A.92(1)
GEM Rules 20.14(1), 20.23 and 20.90(1)
First released: November 2008; last updated: May 2024

Share scheme of subsidiaries (other than principal subsidiaries)

12. Is a listed issuer required to comply with the disclosure and/or shareholders' approval requirements under MB Chapter 14A/ GEM Chapter 20 for each grant of options or awards to a connected person under a subsidiary's scheme?

Yes, if the grants to such person over a 12-month period exceeds the de minimis thresholds under MB Rule 14A.76/ GEM Rule 20.76.

In addition, grants of options or awards by a subsidiary to connected persons at the subsidiary level are exempt from the independent shareholders' approval requirement if the conditions set out in MB Rule 14A.101/ GEM Rule 20.101 are met.

MB Rules 14A.76 and 14A.101
GEM Rules 20.76 and 20.101
First released: July 2022; last updated: May 2024

Guidance on pricing policies for continuing connected transactions and their disclosure

A. Purpose

1. This letter gives guidance on the pricing policies in agreements for continuing connected transactions and their disclosure. Continuing connected transactions are transactions with connected persons carried out on a continuing or recurring basis and are expected to extend over a period of time.

B. Relevant Listing Rules

2. Main Board Rules 14A.51 to 14A.59 (GEM Rules 20.49 to 20.57) set out the requirements that apply to continuing connected transactions, including, among others:

   (i) issuers must enter into a written agreement that sets out the terms of the transactions, which must contain the basis for calculating the payments to be made and reflect normal commercial terms;

   (ii) the period of the agreement must be fixed and reflect normal commercial terms. It must not exceed 3 years, except in special circumstances;

   (iii) there must be an annual cap which is determined by reference to previous transactions, the basis of which must be disclosed;

   (iv) where the annual cap exceeds the relevant de minimis threshold, the agreement and the annual cap must be approved by independent shareholders;

   (v) the transactions should be in the issuer's ordinary and usual course of business, on normal commercial terms (or terms no less favourable to the issuer than terms available to or from independent third parties), the terms must be fair and reasonable and in the interest of shareholders as a whole; and

   (vi) the transactions must be carried out in accordance with the issuer's pricing policies, in accordance with the agreement, and approved by the board of directors.

3. Main Board Rules 14A.55, 14A.56, 14A.71 and 14A.72 (GEM Rules 20.53, 20.54, 20.69 and 20.70) set out the annual reporting and review requirements, including:

   (i) disclosure in the annual report details of the transactions, including the total consideration and terms, a brief description of the transactions and their purposes, the parties to the transactions and descriptions of their relationships;

   (ii) annual review of the continuing connected transactions by the independent non-executive directors (**INEDs**) and confirmation in the annual report that the transactions have been conducted in accordance with paragraph 2(v) above; and

(iii) annual negative confirmation by the auditors of matters set out in paragraph 2(vi) above and that the transactions did not exceed the annual cap.

4. The Listing Rules provide a framework for the conduct of continuing connecting transactions, recognizing the practical difficulty if issuers have to comply with the connected transaction Rules each time a transaction is proposed. It provides safeguards against potential abuse through the following:

- the terms of the agreement, including the basis for calculating the payments, should provide a framework for the negotiation of individual transactions under the agreement. This information is disclosed to shareholders for their assessment whether to approve the agreement;
- imposing an annual cap on the aggregate size of the transaction, set by reference to historical transactions and adjusted by the issuer's projections; and
- annual review by the INEDs and auditors, and confirmation in the issuer's annual report, which provides a check and balance to ensure that the transactions under the agreement were conducted in accordance with the criteria set out in paragraphs 2(v) and (vi) above.

C. Guidance

5. Under the current Listing Rules, the shareholders in effect give an issuer a mandate to conduct transactions with connected persons, subject to i) the terms of the agreement which provide a framework for negotiating each transaction, and ii) the annual cap which limits the aggregate size of the transactions. It is important that the terms of the agreement are specific and measurable, and that there are adequate internal controls in place to ensure that the individual transactions are indeed conducted within the framework of the agreement.

a) Pricing policies

6. The Exchange notes that market practice regarding disclosure about the terms of the agreements vary significantly. In many instances, pricing policy is set out in general terms with no indication of the expected quantum or percentage[1]. Without a specific pricing mechanism shareholders cannot properly assess whether to approve the framework agreement, and INEDs and auditors do not have a framework to review the transactions.

7. When entering into agreement with connected persons, issuers should agree on specific pricing terms, such as fixed monetary consideration, a pre-determined formula, or fixed per unit consideration. Examples include:

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[1] Examples of such disclosure include:
- *the transactions will be conducted on normal commercial terms. The consideration will be based on arms' length negotiation with reference to the prevailing market prices.* There is no explanation on how to define/ determine "normal commercial terms" or "prevailing market prices".
- *The transaction will be agreed between the issuer and the connected person on a "cost plus" mechanism.* There is no indication of the "plus" in percentage or fixed amount.
- *The transaction shall be priced in accordance with the following terms: (i) government-prescribed price; (ii) where there is no government-prescribed price, the government-guidance price; (iii) where there is neither a government-prescribed price nor a government-guidance price, the relevant market price; (iv) where none of the above is available or applicable, the price to be agreed between the parties which shall be determined on the basis of reasonable cost plus reasonable profit margin and by reference to the historical price.* Some of the above pricing methods (e.g. the government-prescribed price) do not apply to the subject transactions in practice.

- provision of management services charged at a fixed sum or a percentage of the issuer's sales or asset value;

- interest rate to be charged on a revolving loan facility and the maximum loan amount; and

- sales or purchase of goods at a fixed unit price, or some reference price published from time to time (e.g. government prescribed price, or commodity prices quoted on an exchange). If the pricing of the goods is determined based on a reference price, the issuer should disclose the relevant details, for example, the name of government authority or organization publishing the price, and how and where the price is disclosed or determined, and the frequency of update to the reference price.

8. If the agreement covers transactions of different nature, the issuer should clearly set out the pricing policy for each type of transactions. It should avoid using generic "boilerplate" pricing mechanism where some of the pricing methods are not applicable to certain categories of transactions (see 3rd point of the example in footnote 1).

9. There may be situations where it is not commercially practical for the issuer to agree with the connected person on specific unit price or contract sum, as it is normal in that industry for the individual transactions to be subject to the pricing conditions at the time each transaction is conducted. In these cases, the issuer would normally conduct the transactions in accordance with its pricing policy and guidelines, which apply to transactions with independent customers as well as connected persons. The following guidelines should be observed when negotiating the terms of the agreement:

   (i) It would not be sufficient to describe pricing policies in generic terms, such as "prevailing market price" or "prices based on arm's length negotiations" or "prices on normal commercial terms".

   (ii) The Listing Rules require that the transactions must be conducted on normal commercial terms, or on terms no less favourable than terms available to independent parties. To demonstrate this, the issuer should disclose the methods and procedures the management will follow to determine the price and terms of the transactions. Examples include:

   - For sales of off-the-shelf products or standard services, an indicative range of prices for goods/services, or the minimum/maximum mark-up rate for transactions that are charged on a cost-plus basis, and the procedures for reviewing and approving these price lists or guidelines from time to time;

   - For sales of proprietary goods or services, the process for estimating and approving the selling prices for the goods or services, and the procedures to ensure that these prices are no less favourable to the issuer than those offered to, or quoted by, independent customers; and

   - For purchases of goods or services, the procedures for obtaining quotations or tenders from the connected persons and a sufficient number of independent suppliers, the assessment criteria and the approval process. For example, the management would solicit at least two other contemporaneous transactions with unrelated third parties for products in similar quantities to determine if the price and terms offered by a connected person are fair and reasonable and comparable to those offered by unrelated third parties.

(iii) The issuer should explain why its directors consider that the methods and procedures can ensure that the transactions will be conducted on normal commercial terms and not prejudicial to the interests of the issuer and its minority shareholders.

b) Disclosure of information

10. The issuer should disclose in its announcement and circular (if any) the specific pricing terms or formula set out in the agreement and material information about pricing policies and guidelines (see paragraphs 7 to 9 above).

11. The issuer should also disclose in its annual report whether it has followed these policies and guidelines when determining the price and terms of the transactions conducted during the year.

c) Internal controls

12. As explained, an important safeguard involves the annual review by auditors and INEDs, and the annual confirmations that the individual transactions are indeed conducted in accordance with the terms of the agreement, on normal commercial terms (or terms more favourable than terms available to independent parties), and in accordance with the pricing policy of the issuer. It is important for the issuer to ensure that it has an adequate system of controls to safeguard the transactions, and to provide information for the INEDs and auditors to properly review the transactions annually.

d) INED role

13. Under the Rules, the INEDs are obliged to confirm that the terms of the agreement are fair and reasonable at the time the agreement is announced, and make annual confirmations about the transactions entered under the agreement as set out in paragraph 2(v).

14. The INEDs should ensure that:

(i) the pricing mechanism and the terms of the transactions set out in the agreement are clear and specific;

(ii) the annual caps are reasonable taking into account historical transactions and management projections;

(iii) the methods and procedures established by the issuer are sufficient to ensure that the transactions will be conducted on normal commercial terms and not prejudicial to the interests of the issuer and its minority shareholders;

(iv) appropriate internal control procedures are in place, and its internal audit would need to review these transactions; and

(v) they are provided by the management with sufficient information for the discharge of their duties.

e) Annual review by auditors

15. Under the Listing Rules, the issuer must engage its auditors to report on the continuing connected transactions every year. The auditors may refer to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants for guidance as to their responsibilities and procedures when undertaking the annual review.

Whether the Exchange would waive the annual review and reporting requirements for a continuing connected transaction between the listed issuer and its independent non-executive director

Parties

- **Company A** – a Main Board listed issuer
- **Mr. X** – an independent non-executive director of Company A
- **Company B** – a company indirectly owned as to 30% by Mr. X

Facts

1. Company A proposed to enter into an agreement with Company B to supply certain goods to Company B for a three-year period (the **Transaction**). As Company B was an associate of Mr. X, the Transaction was a continuing connected transaction for Company A and subject to the announcement and annual review and reporting requirements.

2. Company A applied for a waiver from the annual review and reporting requirements for the Transaction under Rule 14A.103 because:

   - the Transaction was connected only because of Mr. X's interests in Company B;
   - Mr. X was only an independent non-executive director of Company A. He did not control Company A and his principal business interests were not related to Company A;
   - the Transaction would be conducted on normal commercial terms and in the ordinary and usual course of business of both Company A and Company B;
   - the size of the Transaction was not significant to Company A with the highest percentage ratio slightly over 0.1%. It would be unduly burdensome to require the independent non-executive directors and the auditors to review the immaterial Transaction annually.

3. It would disclose the Transaction and the waiver, if granted, by way of an announcement.

Relevant Listing Rules

4. Rule 14A.103 states that:

> The Exchange may waive all or some of the connected transaction requirements for a connected transaction with a non-executive director of the listed issuer or its subsidiaries if:
>
> (1) a transaction is connected only because of the interest of a nonexecutive director; and
>
> (2) the director does not control the listed issuer's group, and his principal business interest is not the listed issuer's group.
>
> Where a waiver is granted from the shareholders' approval requirement under this rule, the Exchange may require the listed issuer's auditor or an acceptable financial adviser to give the opinion that the transaction is fair and reasonable to the shareholders as a whole. "

Analysis

5. The connected transaction Rules seek to safeguard against connected persons taking advantage of their positions to the detriment of the issuer's minority shareholders.

6. To reduce issuers' compliance burden, exemptions and waivers from all or some of the connected transaction requirements are available for transactions that are immaterial or specific circumstances where the risk of abuse by connected persons is low.

7. Here Mr. X was only an independent non-executive director and the Transaction met all waiver conditions set out in Rule 14A.103. It was unlikely that Mr. X could exert undue influence over Company A to obtain a benefit through the Transaction. In light of the remote relationship and the immaterial size of the Transaction, the Exchange agreed to waive the annual review and reporting requirements.

Conclusion

8. The Exchange granted the waiver to Company A.

Whether the Exchange would waive the written agreement requirement for continuing connected transactions between a subsidiary of the listed issuer and other substantial shareholders of the subsidiary

Parties

- **Company X** – a Main Board listed company
- **Partners** – certain multinational corporations who would set up joint ventures with Company X

Facts

1. Group X was principally engaged in design, manufacturing and sale of machinery and equipment in some technology intensive industries.

2. Company X would set up joint ventures with the Partners to enhance its competitiveness. As these joint ventures would be Company X's subsidiaries and each Partner would hold more than 10% interest in one or more of the joint ventures, the Partners would be connected persons of Company X.

3. Under the joint venture arrangements, Company X and/or its subsidiaries would enter into various types of transactions with the Partners (the **Transactions**), including transfer of technology for production to the group, and sale and purchase of components and products to and from the group. The Transactions would be continuing connected transactions for Company X.

4. Company X proposed to seek independent shareholder approval of the Transactions and their annual caps for the next 3 years. Company X sought a waiver from Rule 14A.51 so that it would not be required to enter into framework agreements for the Transactions with the Partners for the following reasons:

    a. Compliance with the Rule would be unduly burdensome. All Partners were well-known multinational enterprises operating independently of Company X. Company X had undergone lengthy negotiation with the Partners and experienced great difficulty in getting the Partners to sign the framework agreements for the Transactions.

    b. The Transactions would form an integral part of the business alliance between Company X and the Partners, and were important to Company X's business. If Company X were unable to enter into the Transactions because of the Partners' refusal to sign the framework agreements, this would be detrimental to Company X's interests.

c. The Partners were connected persons of Company X only because of their substantial shareholding in the joint ventures. The business relationship between each Partner and Company X was of an arm's length nature. Given this, there was no concern of the Partners unduly influencing Company X's action to the detriment of its minority shareholders.

d. The circular would contain details of the Transactions including the identities of the counterparties, the nature of the Transactions, the basis for determining the consideration and the annual caps. Company X would re-comply with the connected transaction rules for any transactions with the Partners outside the established framework set out in the circular.

e. There would be a written agreement between Company X (or its subsidiary) and the relevant Partner for each Transaction which would be on normal commercial terms and in the interest of Company X's shareholders as a whole.

f. Company X would comply with all other applicable connected transaction rules for the Transactions.

5. Company X would seek independent shareholder approval of this waiver application together with the Transactions and their annual caps at the general meeting. Details of the waiver application would be disclosed in the circular for the Transactions.

Relevant Listing Rules

6. Rule 14A.51 provides that:

A written agreement for a continuing connected transaction must contain the basis for calculating the payments to be made. Examples include sharing of costs incurred by the parties, unit prices for goods or services provided, annual rental for leasing a property, or management fees based on a percentage of the total construction cost.

7. Rule 14A.52 provides that:

The period for the agreement must be fixed and reflect normal commercial terms or better. It must not exceed three years except in special circumstances where the nature of the transaction requires a longer period. In this case, the listed issuer must appoint an independent financial adviser to explain why the agreement requires a longer period and to confirm that it is normal business practice for agreements of this type to be of such duration.

8. Rule 14A.53 provides that:

The listed issuer must set an annual cap (the "cap") for the continuing connected transaction. The cap must be:

(1) expressed in monetary terms;

(2) determined by reference to previous transactions and figures in the published information of the listed issuer's group. If there were no previous transactions, the cap must be set based on reasonable assumptions; and

(3) approved by shareholders if the transaction requires shareholders' approval.

9. Rule 14A.54 provides that:

   The listed issuer must re-comply with the announcement and shareholders' approval requirements before:

   (1) the cap is exceeded; or

   (2) it proposes to renew the agreement or to effect a material change to its terms.

   Note: The revised or new cap(s) will be used to calculate the percentage ratios for classifying the continuing connected transaction.

Analysis

10. Continuing connected transactions are connected transactions involving the provision of goods and services or financial assistance, carried out on a continuing or recurring business and expected to extend over a period of time. They are usually transactions in the ordinary and usual course of business.

11. For a continuing connected transaction, Rule 14A.51 requires an issuer to enter into a written agreement with the connected person for a fixed period, which must set out the basis of determining the consideration for the transaction. This will help shareholders assess the terms of the transaction.

12. The Exchange considered the following factors when assessing Company X's waiver application:

    - the Partners' identities and connectedness with Company X, and the practical difficulty in getting them to sign the framework agreements; and

    - despite the absence of a framework agreement, Company X had taken reasonable steps to ensure sufficient information about the Transactions would be provided to its shareholders to make an informed assessment, including the framework for determining the terms of the Transactions. The information provided in the circular would be comparable to normal cases where a framework agreement was signed and the terms disclosed in the circular. Company X would need to re-comply with the connected transaction rules for any transactions with the Partners outside the established framework set out in the circular. The granting of the waiver would be unlikely to result in undue risks to its shareholders.

Conclusion

13. The Exchange granted Company X a waiver and did not require written agreements for the Transactions.

Continuing connected transactions

Written agreement and terms of an agreement

1. MB Rule 14A.34 / GEM Rule 20.32 requires a listed issuer to enter into a written agreement for a connected transaction. Please clarify the meaning of:

(i) an agreement with fixed terms; and

An agreement with fixed terms refers to an agreement which sets out the specific terms for a continuing connected transaction, including the actual or per unit consideration in monetary terms, or a fixed formula for determining the consideration, or specific reference prices (e.g. prices prescribed by government or commodity prices quoted on an exchange) which form the basis of the consideration and where the volume transacted (e.g. number of units) is fixed.

(ii) a framework agreement.

A framework agreement refers to an agreement which sets out the framework within which a series of continuing connected transactions are to be conducted over a period. The actual terms of each transaction may be negotiated, and is subject to a framework such as pricing guidelines or mechanisms to determine that the terms would be consistent with those offered by/ to independent third parties (e.g. obtaining a minimum number of third party quotations etc.).

MB Rule 14A.34
GEM Rule 20.32
First released: March 2014; last updated: May 2024

2. Is it necessary for a listed issuer to enter into a framework agreement for its proposed continuing connected transactions if they will be fully exempt under the de minimis exemption in the current financial year?

No. A framework agreement is not required if the proposed transactions are fully exempt.

MB Rules 14A.51, 14A.52 and 14A.76
GEM Rules 20.49, 20.50 and 20.74
First released: February 2013; last updated: May 2024

3. MB Rule 14A.52 / GEM Rule 20.50 requires the period of a continuing connected transaction agreement must be fixed. If an agreement for a continuing connected transaction has an initial term of 3 years which will be automatically renewed unless both parties agree to terminate the agreement, will such agreement be regarded to have a fixed term?

No, because the listed issuer has no discretion on the renewal of the agreement upon expiry of the initial term of 3 years.

MB Rule 14A.52
GEM Rule 20.50
First released: November 2008; last updated: May 2024

4. A listed issuer proposes to enter into a framework agreement for a continuing connected transaction with a director of its subsidiary. The transaction is a de minimis transaction and subject to announcement and annual report disclosure only. If the agreement is more than 3 years, is the listed issuer required to obtain an independent financial adviser's opinion on the duration of the agreement under MB Rule 14A.52 / GEM Rule 20.50?

Yes.

MB Rules 14A.52 and 14A.101
GEM Rules 20.50 and 20.99
First released: March 2014; last updated: May 2024

Annual cap

5. Should a listed issuer set the annual cap for its continuing connected transaction with reference to its financial year or calendar year?

While this is a matter to be decided by the listed issuer, we encourage listed issuer to set the annual cap with reference to its financial year to align with the annual review of the continuing connected transaction required under MB Rules 14A.55 and 14A.56 / GEM Rules 20.53 and 20.54.

MB Rules 14A.53, 14A.55 and 14A.56
GEM Rules 20.51, 20.53 and 20.54
First released: November 2008; last updated: May 2024

6. A listed issuer proposes to enter into an agreement for a continuing connected transaction for a period of 6 years.

(i) Is the listed issuer required to disclose the independent financial adviser's opinion on the duration of the agreement which exceeds 3 years under MB Rule 14A.52 / GEM Rule 14A.53?

Yes.

(ii) Is the listed issuer required to set annual caps in respect of the continuing connected transaction for the entire period for the agreement?

Yes. If the listed issuer cannot set annual caps for the entire term of agreement for any reasons, it should seek guidance from the Exchange. The listed issuer would normally be required to set annual caps for a shorter period (say 3 years) and after the expiration of the initial period, re-comply with the relevant Listing Rule requirements (including setting annual caps, issuing announcements and/or obtaining shareholders' approval for the cap).

MB Rules 14A.52, 14A.53, 14A.76, 14A.78 and 14A.80
GEM Rules 20.50, 20.51, 20.74, 20.76 and 20.78
First released: November 2008; last updated: May 2024

7. For continuing connected transactions involving purchases or sales of commodity products in a listed issuer's ordinary and usual course of business, can the listed issuer propose annual caps of a fixed quantum as monetary caps may not be meaningful due to volatility in the commodity prices?

The connected transaction rules require annual caps to be expressed in monetary terms. However, the Exchange may waive this requirement if the listed issuer discloses alternative caps based on the estimated volume of the commodity products to be purchased, and a sensitivity analysis to illustrate how changes to the commodity prices will affect the value of the continuing connected transactions. The listed issuer would not be required to estimate the future commodity prices.

The SFC has given consent pursuant to MB Rule 2.04 / GEM Rule 2.07 and agreed to allow the Exchange to grant waivers of general application to the monetary cap requirements in the circumstances described.

A listed issuer should consult the Exchange if it wishes to apply for the waiver.

MB Rules 2.04 and 14A.53
GEM Rules 2.07 and 20.51
First released: February 2013; last updated: May 2024

When a continuing transaction subsequently becomes connected

8. A listed issuer intends to acquire interests in a target company from an independent third party and issue shares as consideration. Thereafter, the vendor will be a substantial shareholder of the listed issuer. The listed issuer will also enter into a framework agreement to purchase raw materials from the vendor at the prevailing market prices from time to time for a 3-year period after the completion of the acquisition. Is the framework agreement a connected transaction?

Yes, as the terms are not fixed at the time the vendor is an independent third party.

MB Rule 14A.25
GEM Rule 20.23
First released: March 2014; last updated: May 2024

9. A listed issuer proposes to purchase raw materials from Company X on a recurring basis which constitutes a continuing connected transaction. Company X currently meets the conditions for the insignificant subsidiary exemption. If the listed issuer enters into a framework agreement with Company X for the purchases for say 3 years, does it mean that all purchases conducted under this agreement are exempt?

No, because the framework agreement is not an agreement with fixed terms. If Company X can no longer meet the conditions for the exemption during the 3-year period, the listed issuer must comply with all applicable connected transaction rules for its subsequent purchases from Company X.

MB Rules 14A.09, 14A.60, 14A.99 and 14A.100
GEM Rules 20.08, 20.58, 20.97 and 20.98
First released: May 2010; last updated: May 2024

10. A listed issuer entered into a lease agreement with a director of its subsidiary for a fixed term of 3 years and has complied with the applicable connected transaction requirements. If after 1 year, the director meets the conditions for the insignificant subsidiary exemption, is the listed issuer required to comply with the reporting and annual review requirements for the remaining term of the lease?

Reporting and annual review of the lease will not be required if the director can continue to meet the conditions for the exemption. If the director do not qualify for the exemption in year 3, the listed issuer must comply with the announcement, reporting and annual review requirements for the remaining term of the lease.

Alternatively, the listed issuer may continue to comply with the Listing Rules requirements for the remaining period of the lease.

MB Rule 14A.09
GEM Rule 20.08
First released: May 2010; last updated: May 2024

11. Some time ago, a listed issuer entered into a lease agreement with fixed terms for a period of 10 years with an independent third party. If the lessor subsequently became a connected person of the listed issuer, will the listed issuer be required to provide an independent financial adviser's opinion on the duration of the lease agreement which exceeds 3 years?

No, the listed issuer is only required to comply with applicable reporting, annual review and disclosure requirements for the lease agreement under MB Rule 14A.60 / GEM Rule 20.58.

MB Rules 14A.52 and 14A.60
GEM Rules 20.50 and 20.58
First released: February 2013; last updated: May 2024

Whether a listed issuer was required to aggregate its purchase of products of the same nature from associates of a connected person

Parties

- **Company A** – a Main Board listed company
- **Company Z** – a substantial shareholder of Company A
- **Company X** and **Company Y** – non-wholly owned subsidiaries of Company Z

Facts

1. Company A and its subsidiaries (the **Group**) were principally engaged in the business of retailing and wholesaling optical products.

2. In March 2007, the Group entered into two purchase agreements with Company X in respect of the Group's purchases of certain branded optical frames and sunglasses from Company X for a period of three years (the First Transaction). Company X was the exclusive wholesale distributor and licensee of these products in various territories.

3. In May 2008, the Group proposed to enter into a manufacturing and supply agreement with Company Y under which Company Y would manufacture and supply optical frames and sunglasses under the Group's house-brands for a period of three years (the **Second Transaction**).

4. Both Company X and Company Y were non-wholly owned subsidiaries of Company Z which was a substantial shareholder of Company A. Therefore, Company X and Company Y were associates of Company Z and connected persons of Company A. The First Transaction and the Second Transaction (together the **Transactions**) constituted continuing connected transactions of Company A under Chapter 14A of the Main Board Listing Rules.

5. Company A submitted the following to support not aggregating the Transactions:

    - The nature of the Transactions was different from each other in that the First Transaction was a trading transaction involving purchases of certain branded optical products, whereas the Second Transaction was a manufacturing transaction involving the Group commissioning Company Y to manufacture optical products bearing brand-names owned by the Group.

- The nature of the Transactions was different from each other in that the First Transaction was a trading transaction involving purchases of certain branded optical products, whereas the Second Transaction was a manufacturing transaction involving the Group commissioning Company Y to manufacture optical products bearing brand-names owned by the Group.

- In respect of the First Transaction, Company A had no choice of supplier as Company X was the exclusive distributor of the branded optical products, whereas in respect of the Second Transaction, Company Y was a manufacturer selected by Company A from a group of possible suppliers by reference to objective criteria without any element of favourism.

- In terms of Company A's procurement timetable, the First Transaction was regarded as a downstream transaction whereas the Second Transaction was an upstream transaction.

- The procurement of branded optical products and products under the Group's own brand names was handled by different teams in the Group

Relevant Listing Rules

6. Main Board Listing Rule 14A.81 provides that:

   The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they were all completed within a 12-month period or are otherwise related. …

7. Main Board Listing Rule 14A.82 provides that:

   Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:

   (1) they are entered into by the listed issuer's group with the same party, or parties who are connected with one another;

   (2) they involve the acquisition or disposal of parts of one asset, or securities or interests in a company or group of companies; or

   (3) they together lead to substantial involvement by the listed issuer's group in a new business activity.

8. Main Board Listing Rule 14A.83 provides that:

   The Exchange may aggregate all continuing connected transactions with a connected person.

Analysis

9. The connected transaction rules seek to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as the listed issuer's directors, chief executives or substantial shareholders or their associates) taking advantage of their positions to the detriment of minority shareholders of an issuer. This is achieved by the general requirement for connected transactions to be disclosed and subject to independent shareholders' approval.

10. The purpose of aggregation is to prevent a listed issuer from "splitting" an otherwise large transaction into two or more smaller transactions so that, when size tests are applied to each smaller transaction, it does not reach the relevant thresholds for requiring disclosure and/or shareholders' approval under Chapter 14A. Pursuant to Rule 14A.81, the Exchange may require a listed issuer to aggregate a series of transaction if they are all completed within a 12 month period or are otherwise related.

11. Rule 14A.82 sets out a non-exhaustive list of factors which the Exchange will take into account in applying the aggregation rule. The rule intends to provide guidance on the circumstances where the Exchange may require aggregation of transactions of a listed issuer. When determining whether aggregation of transactions is required in a particular case, the Exchange will consider all relevant facts and circumstances of the case.

12. The aggregation rules apply to both one-off connected transactions and continuing connected transactions that generally involve provision of goods and/or services. When determining whether a series of continuing connected transactions should be aggregated, the Exchange will also consider whether they are of a similar nature as this may indicate "splitting" of a transaction. Rule 14A.83 provides that the Exchange may consider aggregating all continuing connected transactions with a single connected person.

13. In the present case, the First Transaction and the Second Transaction were to be carried out on a continuing basis over a period of time. The Transactions fell within the circumstances described in Rule 14A.82(1) as they were entered into by the Group with subsidiaries of Company Z which, the Exchange considered, were "parties who are connected with each other" under Rule 14A.82(1).

14. The Exchange considered that the Transactions were of the same nature as they all involved purchases of optical frames and sunglasses by the Group. The Exchange did not accept Company A's submission that the nature of the First Transaction and the Second Transaction were different on the basis of distinctions in terms of brands, the process and timing for procurement of the products.

15. Having considered all relevant factors, the Exchange was of the view that the First Transaction and the Second Transaction were related and there was a concern on splitting of a transaction into smaller transactions.

Conclusion

16. The connected transactions should be aggregated under Rule 14A.81.

Whether a listed issuer would be required to aggregate its continuing connected transaction with its controlling shareholder which involved both revenue and expenditure items

Parties

- **Company A** – a Main Board listed company
- **Parent Company** – the holding company of Company A
- **Parent Group** – Parent Company and its subsidiaries (excluding Company A and its subsidiaries)

Facts

1. Company A and its subsidiaries (the **Group**) were principally engaged in the business of providing mobile telecommunications services to retail customers in Hong Kong.

2. The Parent Group was a major provider of telecommunications services in Hong Kong.

3. After the Parent Company acquired a controlling interest in Company A, Company A's board of directors had conducted a review of the Group's business model and the viability of various alternative options available to Company A.

4. Company A proposed to enter into a variety of transactions with the Parent Group in relation to various aspects of its business (the **Transactions**), each constituting a continuing connected transaction. The Transactions served to facilitate the Group to adopt a new business model in wholesaling products and services to the Parent Group and outsourcing material business functions to the Parent Group.

Relevant Listing Rules

5. Main Board Listing Rule 14A.81 provides that:

   The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they were all completed within a 12-month period or are otherwise related.…

6. Main Board Listing Rule 14A.82 provides that:

   Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:

(1) they are entered into by the listed issuer's group with the same party, or parties who are connected with one another;

(2) they involve the acquisition or disposal of parts of one assets, or securities or interests in a company or group of companies; or

(3) they together lead to substantial involvement by the listed issuer's group in a new business activity.

7. Main Board Listing Rule 14A.83 provides that:

The Exchange may aggregate all continuing connected transactions with a connected person.

Analysis

8. The connected transaction rules seek to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as the listed issuer's directors, chief executives or substantial shareholders or their associates) taking advantage of their positions to the detriment of minority shareholders of an issuer. This is achieved by the general requirement for connected transactions to be disclosed and subject to independent shareholders' approval.

9. The purpose of aggregation is to prevent a listed issuer from "splitting" an otherwise large connected transaction into two or more smaller transactions so that, when percentage ratios are applied to each smaller transaction, it does not reach the de minimis thresholds for de requiring disclosure and/or shareholders' approval under Chapter 14A. Pursuant to Rule 14A.81, the Exchange may require a listed issuer to aggregate a series of connected transaction if they are all completed within a 12 month period or are otherwise related.

10. Rule 14A.82 sets out a non-exhaustive list of factors which the Exchange will take into account in applying the aggregation rule. The rule intends to provide guidance on the circumstances where the Exchange may require aggregation of transactions of a listed issuer. When determining whether aggregation of transactions is required in a particular case, the Exchange will consider all relevant facts and circumstances of the case.

11. The aggregation rules apply to both one-off connected transactions and continuing connected transactions that generally involve provision of goods and/or services. When determining whether a series of continuing connected transactions should be aggregated, the Exchange will also consider where whether they are of a similar nature as this may indicate "splitting" of a transaction. Rule 14A.83 provides that the Exchange may consider aggregating all continuing connected transactions with a single connected person.

12. In the present case, the Transactions were proposed to be made at the same time and they fell within the circumstances described in Rule 14A.82(1) as the Transactions were entered into by Group A with members of the Parent Group which, the Exchange considered, were "*parties who are connected with each other*" under Rule 14A.82(1).

13. The Transactions were proposed to facilitate the implementation of a new business model for the Group. While the Group's retail business would continue, the Group would commence a new line of business in wholesaling products and services to the Parent Group and would outsource certain material business functions to the Parent Group. The Exchange considered that the Transactions would lead to a substantial change to the business model of the Group and they "*together lead to substantial involvement by the listed issuer's group in a new business activity*" described in Rule 14A.82(3).

14. There were a variety of Transactions relating to various aspects of the Group's telecommunication business and Company A originally proposed to aggregate the Transactions based on product/service types. Given the special circumstances of the case, in particular the parties' intention to effect a substantial change to the business activities of the Group through the Transactions, the Exchange determined to aggregate the Transactions under three major categories: (i) provision of services and products by the Group to the Parent Group; (ii) purchases made by the Group from the Parent Group; and (iii) provision of outsourcing services by the Parent Group to the Group. The Transactions, when aggregated on such basis, would require independent shareholders' approval under Chapter 14A.

15. While the Exchange considered it possible to, in appropriate circumstances, aggregate revenue and expenditure items, it was of the view that the purpose of the aggregation rules was achieved in the present scenario in the manner described in paragraph 14. Accordingly, the question of whether all the Transactions needed to be aggregated as if there were one transaction became irrelevant in this case.

Conclusion

16. The connected transactions should be aggregated under Rule 14A.81.

Whether a listed issuer was required to aggregate its transactions in relation to the lease and license of properties in the same building to two directors who were associates of each other

Parties

- **Company X** – a Main Board listed company
- **Mr A** – a director of Company X
- **Company A** – a company wholly owned by Mr A
- **Mr B** – a director of Company X, and the son of Mr A
- **Company B** – a company wholly owned by Mr B

Facts

1. The principal activities of Company X included property development and investment.

2. Company X proposed to enter into a licence agreement with Company B to license to it certain car park spaces in a commercial building (**Building**) for three years (**Licence**). Company X submitted that the car park spaces were licensed to Company B mainly for business use and might be sub-licensed to third parties.

3. In the previous 12 months, Company X had entered into an agreement to lease two shops in the Building to Company A for two years (**Lease**). Company X submitted that these shops had been leased to Company A for a few years and the Lease was a renewal of previous leases. The shops were leased for the lessee's own use and could not be sublet.

4. As Company A and Company B were connected persons of Company X, the Lease and the Licence (together, **Transactions**) constituted connected transactions under Chapter 14A.

5. Based on the percentage ratio calculations, each of the Lease and the Licence fell within the de minimis provision of Rule 14A.76(1) and was fully exempt from the connected transaction requirements. If the Transactions were aggregated, they would be subject to disclosure under Rule 14A.76(2).

Relevant Listing Rules

6. Rule 14A.81 provides that:

   The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they are all completed within a 12-month period or are otherwise related. The listed issuer must comply with the applicable connected transaction requirements based on the classification of the connected transactions when aggregated. …

7. Rule 14A.82 provides that:

   Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:

   (1) they are entered into by the listed issuer's group with the same party, or parties who are connected with one another;

   (2) they involve the acquisition or disposal of parts of one asset, or securities or interests in a company or group of companies; or

   (3) they together lead to substantial involvement by the listed issuer's group in a new business activity.

8. Rule 14A.83 provides that:

   The Exchange may aggregate all continuing connected transactions with a connected person.

Analysis

9. The connected transaction rules seek to ensure that an issuer takes account of the interests of shareholders as a whole when it enters into transactions with connected persons, in particular to safeguard against connected persons (such as the issuer's directors, chief executives or substantial shareholders, or their associates) taking advantage of their positions to the detriment of minority shareholders. This is achieved by the general requirement for connected transactions to be disclosed and subject to independent shareholders' approval.

10. The purpose of aggregation is to prevent an issuer from "splitting" an otherwise large transaction into smaller transactions so that, when size tests are applied to each smaller transaction, it does not reach the thresholds for requiring disclosure and/or shareholders' approval under Chapter 14A. Under Rule 14A.81, the Exchange may require an issuer to aggregate a series of transaction if they are all completed within a 12 month period or are otherwise related.

11. Rule 14A.82 sets out a non-exhaustive list of factors which the Exchange will take into account in applying the aggregation rule. The rule intends to provide guidance on the circumstances where the Exchange may require aggregation. When determining whether aggregation is required in a particular case, the Exchange will consider all relevant facts and circumstances.

12. The aggregation rules apply both to one-off connected transactions and to continuing connected transactions that generally involve provision of goods and/or services. When determining whether a series of continuing connected transactions should be aggregated, the Exchange will consider whether they are of a similar nature as this may indicate "splitting" of a transaction. Rule 14A.83 provides that the Exchange may consider aggregating all continuing connected transactions with a single connected person.

13. In this case, the Lease and the Licence were to be carried out on a continuing basis over a period of time. Given the relationship between Mr A and Mr B, Company A and Company B were "*parties who are connected with each other*" and the Transactions fell within the circumstances in Rule 14A.82(1).

14. The Exchange took into account the following factors suggesting that the Transactions were not connected or related in substance and that "splitting" of a transaction into smaller transactions was not a concern:

    - The Transactions were not made under any master agreement between Company X and any connected persons.

    - While the properties subject to the Lease and the Licence were located in the same building, the nature and use of the properties were different.

    - The Transactions were in line with the principal business of Company A and the circumstances described in Rule 14A.82(3) did not exist.

15. The Exchange accepted that it was not appropriate to conclude that aggregation was required solely on the basis of the factor in Rule 14A.82(1) applying.

Conclusion

16. The Transactions would not be aggregated under Rule 14A.81.

Whether a listed issuer was required to aggregate its construction contracts for different parts of a railway line with associates of a connected person

Parties

- **Company A –** a Main Board issuer
- **Company B –** a substantial shareholder of a subsidiary of Company A
- **Company C** and **Company D –** each an associate of Company B

Facts

1. Company A's principal activities included operating railway systems.

2. It would construct a new railway line. The project involved a number of construction contracts with contractors for different parts of the railway line. Each contract was subject to a separate tender process.

3. Among these construction contracts, Company A intended to award one contract (**Contract 1**) to Company C and another contract (**Contract 2**) to Company D.

4. Companies C and D were both associates of Company B and therefore connected persons. Company A enquired whether Contracts 1 and 2 should be aggregated under Chapter 14A. It submitted that:

    - the contracts were awarded to Companies C and D through separate tender processes. Each contract related to a different and distinct aspect of the railway line.

    - Company A decided to construct the new railway line under a number of separate construction contracts (including Contracts 1 and 2) to minimise the programme risk to the project, taking into account various factors including the nature of the civil works and its strategy and experience in the construction of other railway projects in the past. It did not "split" the construction works with a view to circumventing the Listing Rules.

Relevant Listing Rules

5. Rule 14A.81 states that:

    The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they are all completed within a 12-month period or are otherwise related. The listed issuer must comply with the applicable connected transaction requirements based on the classification of the connected transactions when aggregated. …

6. Rule 14A.82 states that:

   Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:

   (1) they are entered into by the listed issuer's group with the same party, or parties who are connected with one another;

   (2) they involve the acquisition or disposal of parts of one asset, or securities or interests in a company or group of companies; or

   (3) they together lead to substantial involvement by the listed issuer's group in a new business activity.

7. Rule 14A.83 states that:

   The Exchange may aggregate all continuing connected transactions with a connected person.

Analysis

8. Under Rule 14A.81, the Exchange may require an issuer to aggregate a series of transaction if they are completed within a 12 month period or are otherwise related.

9. Rule 14A.82 sets out a non-exhaustive list of factors which the Exchange will consider in applying the aggregation rule. The Rule is intended to provide guidance on the circumstances where aggregation may be required. When determining whether aggregation is required in a particular case, the Exchange will consider all relevant facts and circumstances.

10. The Exchange considered Contracts 1 and 2 were related and should be aggregated because:

    - they were parts of the new railway project of Company A; and
    - they were entered into by Company A with Companies C and D who were parties connected with one another.

11. Contracts 1 and 2 would be treated as one connected transaction and classified based their total contract sum.

Conclusion

12. The connected transactions should be aggregated under Rule 14A.81.

Whether a listed issuer was required to aggregate its transactions with its parent company involving (i) the parent company contracting out certain works to the listed issuer; and (ii) the listed issuer sub-contracting some of the works back to the parent group

Parties

- **Company A** – a Main Board issuer
- **Parent Company** – Company A's controlling shareholder
- **Parent Group** – the Parent Company and its subsidiaries

Facts

1. Company A was engaged in the provision of information technology infrastructure and internet services.

2. It proposed to enter into two framework agreements (**Agreements 1 and 2**) with the Parent Company for the following transactions for 3 years:

    - Under Agreement 1, the Parent Company would engage Company A to carry out certain network infrastructure and security system works on a project basis for the buildings owned and/or managed by the Parent Group.

    - Under Agreement 2, Company A would engage the Parent Company's subsidiaries as sub-contractors to carry out part of the works in projects awarded to Company A under Agreement 1.

3. Based on the percentage ratio calculations, Agreement 1 was a non-exempt continuing connected transaction, and Agreement 2 was exempt from the independent shareholders' approval requirement under the de minimis provision in Rule 14A.76(2).

4. Company A considered that the agreements should not be aggregated under Chapter 14A because:

    - They were distinct and separate from each other.

    - The transactions were of different nature to Company A. One of them was of an income nature and the other was of an expense nature.

Relevant Listing Rules

5. Rule 14A.81 states that:

   The Exchange will aggregate a series of connected transactions and treat them as if they were one transaction if they are all completed within a 12-month period or are otherwise related. The listed issuer must comply with the applicable connected transaction requirements based on the classification of the connected transactions when aggregated. …

6. Rule 14A.82 states that:

   Factors that the Exchange will consider for aggregation of a series of connected transactions include whether:

   (1) they are entered into by the listed issuer with the same party, or parties who are connected with one another;

   (2) they involve the acquisition or disposal of parts of one asset, or securities or interests in a company or group of companies; or

   (3) they together lead to substantial involvement by the listed issuer's group in a new business activity.

7. Rule 14A.83 states that:

   The Exchange may aggregate all continuing connected transactions with a connected person.

Analysis

8. Under Rule 14A.81, the Exchange may require an issuer to aggregate a series of transaction if they are completed within a 12 month period or are otherwise related.

9. Rule 14A.82 sets out a non-exhaustive list of factors which the Exchange will consider in applying the aggregation rule. The Rule is intended to provide guidance on the circumstances where aggregation may be required. When determining whether aggregation is required in a particular case, the Exchange will consider all relevant facts and circumstances.

10. The Exchange considered Agreements 1 and 2 were related and should be aggregated because:

    - they were entered into by Company A with the same party i.e. the Parent Company; and
    - the sub-contracting arrangements under Agreement 2 were part of the transactions subject to Agreement 1. The agreements were connected with each other.

11. Company A submitted that the transaction of an income nature under Agreement 1 should not be aggregated with that of an expense nature under Agreement 2. However, the Exchange did not agree. It may aggregate income and expense items in appropriate circumstances (see also Listing Decision LD64-4).

12. Here, Agreements 1 and 2 were in substance one transaction involving (i) the Parent Group contracting out certain system works to Company A and (ii) Company A sub-contracting some of the works back to the Parent Group. They, when aggregated, would be classified with reference to the larger of (i) or (ii). On this basis, both agreements would be non-exempt continuing connected transactions and would require independent shareholders' approval.

Conclusion

13. The connected transactions should be aggregated under Rule 14A.81.

Aggregation of transactions

1. A listed issuer recently entered into a continuing connected transaction with its parent group for a term of 3 years. It now proposes a second continuing connected transaction over the next 2 years. How do the connected transaction requirements apply to the second transaction if:

(i) both transactions, on a standalone basis, were exempt from the independent shareholders' approval requirement under the de minimis exemption?

The two transactions should be aggregated for the purpose of calculating the percentage ratios for the second transaction. If the percentage ratio(s) calculated on an aggregate basis exceeds the de minimis threshold for shareholders' approval, the second transaction would require shareholders' approval.

(ii) the first transaction was non-exempt and the listed issuer has complied with the independent shareholder's approval requirement?

The second transaction would be subject to the connected transaction requirements based on the percentage ratios calculated on a standalone basis.

MB Rules 14A.81, 14A.82 and 14A.83
GEM Rules 20.79, 20.80 and 20.81
First released: February 2013; last updated: May 2024

2. The Listing Rules require a listed issuer to consult the Exchange on aggregation of transactions before it enters into any proposed transaction(s). Must a listed issuer consult the Exchange under all circumstances?

No. The purpose of the Listing Rules is to minimise the risk of non-compliance with the aggregation Rules by a listed issuer before it enters a transaction. A listed issuer does not need to consult the Exchange if that is not the case, for example:

- the proposed transaction when aggregated with the previous transaction(s), would not result in a higher transaction classification; or
- the listed issuer intends to aggregate the proposed transaction with the previous transaction(s) and comply with the relevant requirements.

MB Rules 14.23B, 14A.84, 14A.85 and 14A.86
GEM Rules 19.23B, 20.82, 20.83 and 20.84
First released: November 2008; last updated: May 2024

3. Is a listed issuer required to aggregate leases it entered into with the same party as lessee within a 12-month period?

Generally the Exchange would not require aggregation of the lease transactions solely because they are made with the same party. When applying the aggregation Rules, the Exchange would consider whether the lease transactions are connected or related in substance and whether there is a concern about "splitting" of a lease transaction into smaller ones to circumvent the notifiable/ connected transaction requirements. It would take into account factors including:

- whether the leases are made under a master agreement or negotiated and concluded at the same time;
- whether the leased assets form part of one asset; and/or
- whether the leases would together lead to substantial involvement by the issuer in a new business activity.

(See also Listing Decisions HKEX-LD64-1 (2008) under Section 11 "Notifiable Transactions" and HKEX-LD76-3 (2009) under Section 12 "Connected Transactions" of the Guidance Materials for Listed Issuers).

MB Rules 14.22, 14.23, 14.23B, 14A.24(1), 14A.24(3), 14A.31 and 14A.84
GEM Rules 19.22, 19.23, 19.23B, 20.22(1), 20.22(3), 20.29 and 20.82
First released: September 2018; last updated: May 2024

Whether certain shareholders of a listed issuer had a material interest in the issuer's proposal to privatise a listed subsidiary

Parties

- **Company X** – a Main Board listed company
- **Subsidiary** – a GEM listed company and a subsidiary of Company X
- **Company A** – a substantial shareholder of Company X. It was controlled by Individual A.
- **Company B and Company C** – each a substantial shareholder of Company X. They were controlled by a company listed on the Exchange.
- **Individual D, Individual E** – each a director and a shareholder of Company X
- **Relevant Shareholders** – Company A, Company B, Company C, Individual D and Individual E collectively

Facts

1. Company X and certain companies, including Company A, controlled by Individual A (**Group A**) held approximately 65 per cent and 9.9 per cent of the issued shares of the Subsidiary respectively.

2. Company X proposed to privatise the Subsidiary by a scheme of arrangement.

    - Under the scheme, all shares in the Subsidiary excluding those held by Company X and Group A (**Scheme Shares**) would be cancelled in exchange for cash consideration.

    - Company X would also make an offer to the holders of the outstanding options granted by the Subsidiary according to the Takeovers Code.

3. Upon the scheme becoming effective, all Scheme Shares would be cancelled and any outstanding options not exercised on or before the record date would lapse.

4. The proposal was subject to approval of the independent shareholders of the Subsidiary (ie shareholders other than Company X and parties acting in concert with it) under the Takeovers Code. The Relevant Shareholders were parties acting in concert with Company X in relation to the proposal.

5. Upon completion, Company X's shareholding in the Subsidiary would increase to about 90 per cent. The proposal constituted a major transaction for Company X and was subject to shareholder approval at a general meeting of Company X.

6. As some holders of the Scheme Shares or outstanding options were connected persons of Company X, the transactions with them under the proposal constituted connected transactions for Company X.

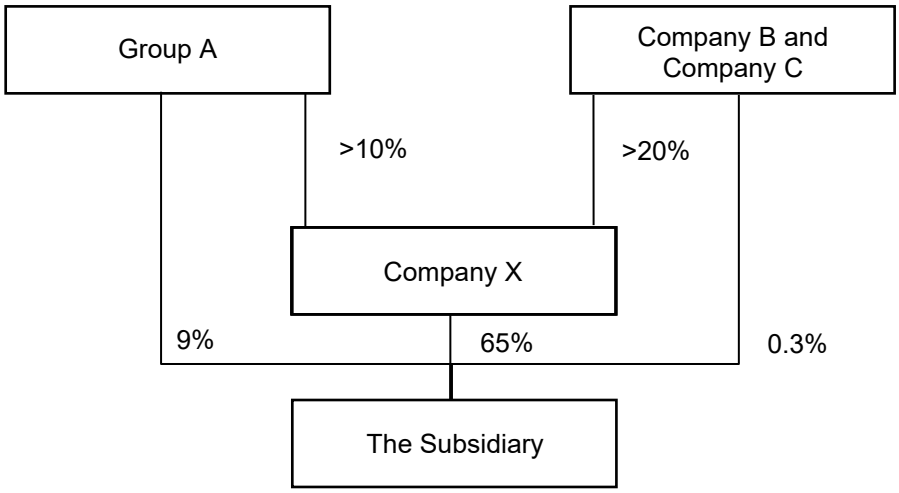
7. Company X would convene a general meeting to seek shareholders' approval of the proposal, which included the transactions with connected persons of Company X. There was a question whether each of the Relevant Shareholders had a material interest in the proposal and was required to abstain from voting on the resolution to approve the proposal at the general meeting of Company X.

Company A, Company B and Company C – substantial shareholders of Company X

8. Company A was wholly owned by Individual A. Group A (which included Company A) held approximately 9.9 per cent of the issued share capital of the Subsidiary (other than those indirect interests in the subsidiary held through Company X). The shares in the Subsidiary held by Group A would not form part of the Scheme Shares and would not be cancelled upon the scheme becoming effective.

9. Company B and Company C were ultimately controlled by a company whose shares were also listed on the Exchange. They together held approximately 0.3 per cent of the issued share capital of the Subsidiary (other than those indirect interests in the Subsidiary held through Company X).

10. The simplified shareholding structure showing the interest of Group A, Company B and Company C in Company X and the Subsidiary before the proposed privatisation is set out below:



Individual D and Individual E – shareholders of Company X

11. Individual D and Individual E were each a director of Company X and the Subsidiary. Individual E was also the chief executive officer of the Subsidiary.

12. Individual D held some shares in the Subsidiary which represented less than 0.0001 per cent of the Subsidiary's issued share capital.

13. Individual E did not hold any shares in the Subsidiary but held a number of outstanding options. The shares to be issued upon exercise of the vested outstanding options represented approximately 2 per cent of the Subsidiary's issued share capital.

Relevant Listing Rules

14. Rule 2.15 provides that:

> Where a transaction or arrangement of an issuer is subject to shareholders' approval under the provisions of the Exchange Listing Rules, any shareholder that has a material interest in the transaction or arrangement shall abstain from voting on the resolution(s) approving the transaction or arrangement at the general meeting.
>
> *Note: For the avoidance of doubt, any provision in the Exchange Listing Rules requiring any other person to abstain from voting on a transaction or arrangement of an issuer which is subject to shareholders' approval shall be construed as being in addition to the requirement set out in rule 2.15.*

15. Rule 2.16 provides that:

> For the purpose of determining whether a shareholder has a material interest, relevant factors include:
>
> (1) whether the shareholder is a party to the transaction or arrangement or a close associate of such a party; and
>
> (2) whether the transaction or arrangement confers upon the shareholder or his close associate a benefit (whether economic or otherwise) not available to the other shareholders of the issuer.
>
> There is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms. The materiality of an interest is to be determined on a case by case basis, having regard to all the particular circumstances of the transaction concerned.

16. Rule 14.40 provides that:

> In the case of a major transaction, the listed issuer must comply with the requirements for all transactions and for discloseable transactions set out in rules 14.34 to 14.39. In addition, a major transaction must be made conditional on approval by shareholders.

17. Rule 14.46 provides that:

> The Exchange will require any shareholder and his associates to abstain from voting at the relevant general meeting on the relevant resolution(s) if such shareholder has a material interest in the transaction. …

18. Rule 14A.36 provides 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.

Analysis

19. Rule 2.16 provides a non-exhaustive list of factors to determine whether a shareholder has a material interest for the purposes of the Listing Rules. The Rule also states that there is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms.

20. When determining the materiality of an interest, the Exchange will need to consider all the circumstances of the proposed transaction.

Company A

21. Company X submitted that Company A as a substantial shareholder of Company X did not have a material interest in the proposal as the 9 per cent shareholding in the Subsidiary directly held by Group A would not form part of the Scheme Shares and Group A would not be entitled to any payment of the cash consideration.

22. The Exchange did not agree. As set out in Rule 2.16, a material interest may not necessarily be defined in monetary or financial terms.

23. Under the proposal, there was a specific arrangement between Company X and Group A that the shares in the Subsidiary held by Group A would be excluded from the scheme and would not be cancelled upon the scheme becoming effective. The Exchange considered that Group A, as a party to this arrangement, had a material interest in the proposal. Accordingly, Company A must abstain from voting at the general meeting of Company X.

Company B and Company C

24. Company B and Company C each held a substantial shareholding in Company X, which owned a 65 per cent interest in the Subsidiary. Although these companies were holders of the Scheme Shares, their direct interest in the Subsidiary (in aggregate about 0.3 per cent) was immaterial compared to that held through Company X. The Exchange accepted that as substantial shareholders of Company X, the interest of Company B and Company C in the proposal was in alignment with the interest of other shareholders of Company X. Therefore, Company B and Company C would not be regarded as having a material interest in the proposal.

25. The Exchange also noted that the connected transactions with Company B and Company C would be exempt from the independent shareholders' approval requirement under the de minimis provisions in Chapter 14A of the Listing Rules.

26. Company B and Company C would not be required to abstain from voting at the relevant general meeting of Company X.

Individual D

27. The Exchange agreed that Individual D did not have a material interest in the proposal because the amount of Scheme Shares he held was insignificant. He had also undertaken to donate his Scheme Shares to a charitable body and there was not any transaction between Company X and him under the proposal. Accordingly, he would not be required to abstain from voting at the relevant general meeting of Company X.

Individual E

28. The proposal involved privatising the Subsidiary. Individual E was then the chief executive officer of the Subsidiary and held a number of outstanding options. His interest in the proposal was different from the other shareholders of Company X and was regarded as material in light of the circumstances.

29. Under the proposal, the transaction between Company X and Individual E constituted a connected transaction that required independent shareholders' approval under Chapter 14A of the Listing Rules. Therefore, when Company X put forward a resolution to seek shareholders' approval of the proposal which included the transaction with Individual E, Individual E must abstain from voting.

Conclusion

30. The Exchange determined that Company A and Individual E had a material interest in the proposal and must abstain from voting on the resolution to approve the proposal at the general meeting of Company X.

Whether a substantial shareholder of a listed issuer had a material interest in the proposed acquisition of interests in a target company

Parties

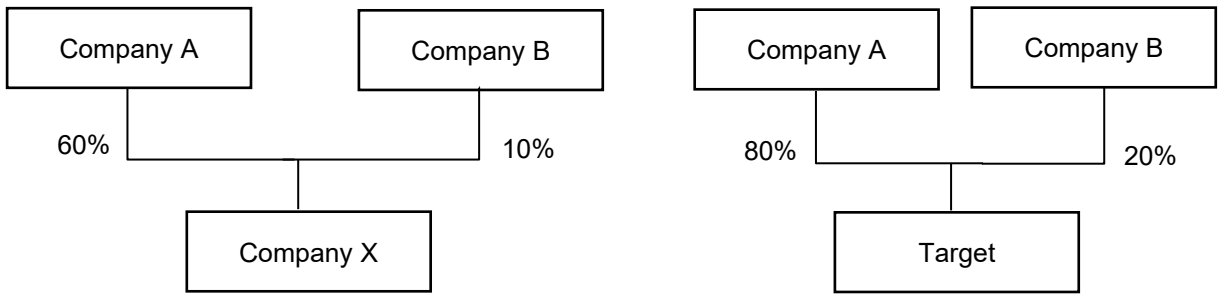
- **Company X** – a Main Board listed company
- **Company A** – a private company holding a 60% interest in Company X and an 80% interest in the Target
- **Company B** – a private company holding a 10% interest in Company X and a 20% interest in the Target
- **Target** – a private company in which Company X proposed to acquire an 80% interest from Company A

Facts

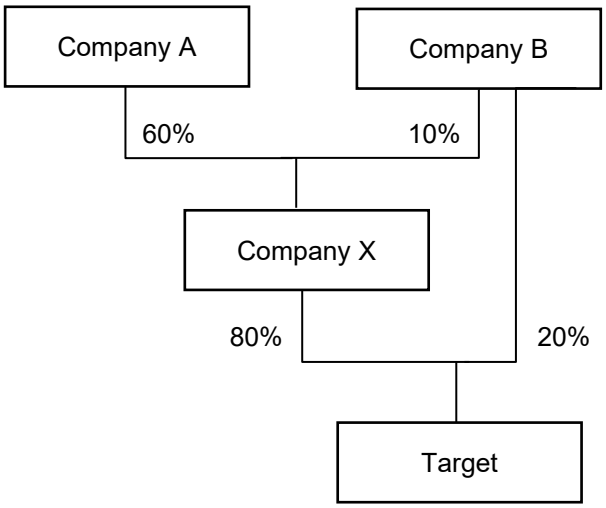
1. Company X proposed to acquire Company A's 80% interest in the Target to facilitate its business expansion in overseas markets. The Target was engaged in a similar line of business to Company X. It had been Company A's intention to inject its interest in the Target into Company X to increase the group's business synergies and overall competitiveness.

2. The simplified shareholding structures before and after the acquisition are set out below:

Before the acquisition



After the acquisition



3. As Company A was the controlling shareholder of Company X, the acquisition was a connected transaction for Company X and was subject to approval by its independent shareholders. Company A would abstain from voting on the resolution to approve the acquisition.

4. Company B was a substantial shareholder of Company X. Company X submitted that it should not be required to abstain from voting because:

   a. Company B was not a party to the acquisition.

   b. Company B was not an associate of Company A. Company A and Company B were independent of each other.

   c. Company X was a subsidiary of Company A. The Target's shareholder agreement between Company A and Company B already provided that Company A's transfer of its interest in the Target to Company X was permitted and no consent from Company B was required.

   d. Company B's rights and obligations as a shareholder of the Target remained unchanged before and after the acquisition.

   e. Despite Company B's interest in both the Target and Company X, any benefit that might accrue to Company X as a result of the acquisition would only be relevant to Company B as a shareholder of Company X. Company B's position did not differ from the position of Company X's other shareholders.

Relevant Listing Rules

5. Rule 2.15 provides that:

   Where a transaction or arrangement of an issuer is subject to shareholders' approval under the provisions of the Exchange Listing Rules, any shareholder that has a material interest in the transaction or arrangement shall abstain from voting on the resolution(s) approving the transaction or arrangement at the general meeting.

Note: For the avoidance of doubt, any provision in the Exchange Listing Rules requiring any other person to abstain from voting on a transaction or arrangement of an issuer which is subject to shareholders' approval shall be construed as being in addition to the requirement set out in rule 2.15.

6. Rule 2.16 provides that:

For the purpose of determining whether a shareholder has a material interest, relevant factors include:

(1) whether the shareholder is a party to the transaction or arrangement or a close associate of such a party; and

(2) whether the transaction or arrangement confers upon the shareholder or his close associate a benefit (whether economic or otherwise) not available to the other shareholders of the issuer.

There is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms. The materiality of an interest is to be determined on a case by case basis, having regard to all the particular circumstances of the transaction concerned.

Note: The references to "close associate" shall be changed to "associate" where the transaction or arrangement is a connected transaction under Chapter 14A.

7. Rule 14A.36 provides 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.

Analysis

8. In this case, the acquisition was a connected transaction for Company X because of the connectedness of Company A but not Company B. It involved Company A transferring an interest in the Target to its subsidiary (i.e. Company X), and Company B's interest in the Target would remain unchanged. The Exchange accepted that as a substantial shareholder of Company X, Company B's interest in the acquisition aligned with the interest of Company X's minority shareholders.

Conclusion

9. Company B did not have a material interest in Company X's proposed acquisition of Company A's 80% interest in the Target.

Whether a substantial shareholder of a listed issuer had a material interest in the proposed acquisitions of interests in a target company

Parties

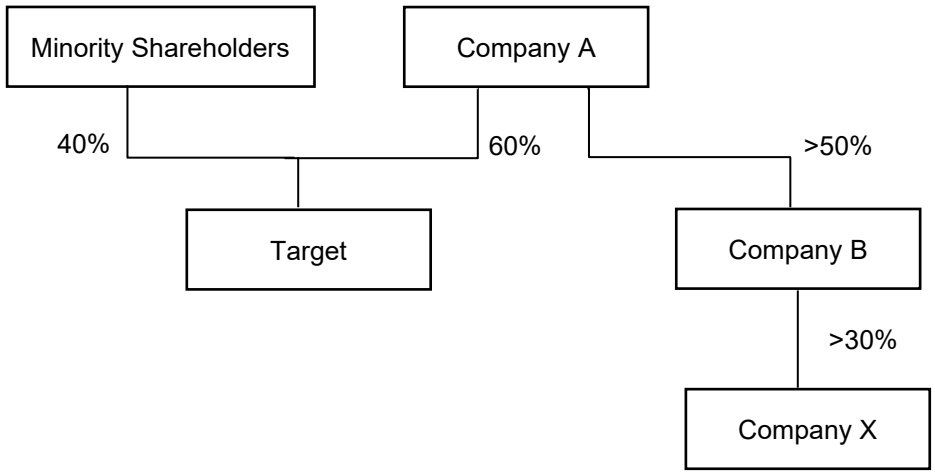
- **Company X** – a Main Board listed company
- **Target** – a private company which Company X proposed to acquire
- **Company A** – a private company holding a 60% interest in the Target
- **Minority Shareholders** – two independent third parties holding a 40% interest in the Target
- **Company B** – a company listed on the Exchange. It was also Company X's controlling shareholder and Company A's subsidiary

Facts

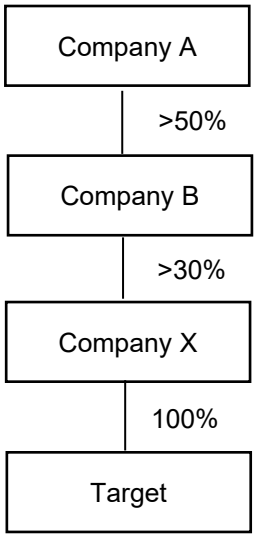
1. Company X proposed to acquire the entire interest in the Target, 60% from Company A and 40% from the Minority Shareholders (**1st Acquisition** and **2nd Acquisition** respectively).

2. The simplified shareholding structures showing the relationship among these parties before and after the acquisitions is below:

Before the acquisitions



After the acquisitions



3. The acquisitions would be agreed separately and independently; they would not be inter-conditional on each other.

4. Company B was Company X's controlling shareholder. As Company A was the holding company of Company B and therefore a connected person of Company X, the 1st Acquisition was a connected transaction for Company X under Rule 14A.25.

5. While the Minority Shareholders were not connected persons, the 2nd Acquisition was a connected transaction for Company X under Rule 14A.28 because Company A was a substantial shareholder of the Target.

6. Company X submitted that Company B should not be required to abstain from voting on the resolution to approve each of the acquisitions because:

<u>The 1st Acquisition</u>

- Company B did not have any interest in the Target. It was not a party to the acquisition.

- Company B was a listed company. Despite being a subsidiary of Company A, Company B's voting decision at Company X's general meeting should not automatically be deemed to be that of Company A. The common directors of Company A and Company B would abstain from voting on Company B's board resolutions regarding the vote to be cast on the resolution to approve the 1st Acquisition at Company X's general meeting.

<u>The 2nd Acquisition</u>

- Company A and Company B had no control over any of the Minority Shareholders and was unable to exert influence on any of them with respect to the acquisition.

- The 1st and 2nd Acquisitions were not inter-conditional on each other. Neither Company A nor Company B would derive any benefit from the 2nd Acquisition.

Relevant Listing Rules

7. Rule 2.15 provides that:

Where a transaction or arrangement of an issuer is subject to shareholders' approval under the provisions of the Exchange Listing Rules, any shareholder that has a material interest in the transaction or arrangement shall abstain from voting on the resolution(s) approving the transaction or arrangement at the general meeting.

Note: For the avoidance of doubt, any provision in the Exchange Listing Rules requiring any other person to abstain from voting on a transaction or arrangement of an issuer which is subject to shareholders' approval shall be construed as being in addition to the requirement set out in rule 2.15.

8. Rule 2.16 provides that:

For the purpose of determining whether a shareholder has a material interest, relevant factors include:

(1) whether the shareholder is a party to the transaction or arrangement or a close associate of such a party; and

(2) whether the transaction or arrangement confers upon the shareholder or his close associate a benefit (whether economic or otherwise) not available to the other shareholders of the issuer.

There is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms. The materiality of an interest is to be determined on a case by case basis, having regard to all the particular circumstances of the transaction concerned.

Note: The references to "close associate" shall be changed to "associate" where the transaction or arrangement is a connected transaction under Chapter 14A.

9. Rule 14A.25 provides that:

Any transaction between a listed issuer's group and a connected person is a connected transaction.

10. Rule 14A.28 provides that:

A listed issuer's group acquiring an interest in a company (the "target company") from a person who is not a connected person is a connected transaction if the target company's substantial shareholder:

(1) is, or is proposed to be, a controller. A "controller" is a director, chief executive or controlling shareholder of the listed issuer; or

(2) is, or will, as a result of the transaction, become, an associate of a controller or proposed controller.

11. Rule 14A.36 provides 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.

Analysis

12. Rule 2.16 provides a non-exhaustive list of factors to determine whether a shareholder has a material interest for the purposes of the Listing Rules. It also states that there is no benchmark for materiality of an interest nor may it necessarily be defined in monetary or financial terms.

The 1st Acquisition

13. The 1st Acquisition involved Company B's associate (i.e. Company A) disposing of its interest in the Target to Company X for a consideration. It fell within the circumstances described in Rule 2.16 and the Exchange considered Company B to have a material interest in the acquisition. Company X's submission was not sufficient to address the potential abuse of connected persons taking advantage of their positions in the acquisition.

The 2nd Acquisition

14. Rule 14A.28 expands the definition of connected transaction to include an acquisition of interests in a target company from independent parties where a substantial shareholder (not the vendor) of the target company is a controlling shareholder or its associate (i.e. the connected person). Under these circumstances, it is possible for the connected person to indirectly benefit from and/or influence the transaction. The 2nd Acquisition is a connected transaction because Company A is the substantial shareholder of Target and it is its association with Company B that results in the transaction being classified as a connected transaction under the Rule. Company B has a material interest in the acquisition which may not be expressed in monetary or financial terms.

Conclusion

15. Company B had a material interest in the proposed acquisitions.

Shareholders' approval requirement for connected transactions

1. A listed issuer proposes a connected transaction which involves an issue of new shares or a transfer of treasury shares to a connected person as consideration (consideration issue). The transaction is subject to independent shareholders' approval.

(i) Will the Exchange grant a waiver from the general meeting requirement under MB Rule 14A.37 / GEM Rule 20.35?

Yes, if the listed issuer is able to meet all the conditions set out in MB Rule 14A.37 / GEM Rule 20.35 (i.e. no shareholder other than a holder of treasury shares is required to abstain from voting if a general meeting is held to approve the transaction, and a written shareholders' approval is obtained).

(ii) Can the listed issuer conduct the consideration issue under a general mandate?

Yes, if the listed issuer has obtained independent shareholders' approval in a general meeting or a written shareholders' approval.

MB Rules 14A.37 and Note 1 to 13.36(2)(b)
GEM Rules 20.35, 17.39 and Note 1 to 17.41
First released: November 2008; last updated: June 2024

Exemptions from the connected transaction requirements

De minimis transactions

1. A listed issuer proposes to obtain a loan from its controlling shareholder on normal commercial terms, secured by certain assets of the listed issuer. Can the listed issuer apply the de minimis exemption? If yes, how should the percentage ratios be calculated?

Yes. It should calculate the assets and consideration ratios for the loan based on the principal amount of the loan and the revenue ratio based on the annual interests payable to its controlling shareholder.

Given the loan is to be secured by the listed issuer's assets, it should also calculate the percentage ratios for the security as if a disposal of the pledged assets. It should calculate the assets and consideration ratios based on the value of the pledged assets and the revenue ratio based on any identifiable revenue stream generated from the pledged assets. The loan should be classified based on the highest percentage ratios of the loan and the security.

MB Rules 14A.76, 14A.76(2) and 14A.90
GEM Rules 20.74(1), 20.74(2) and 20.88
First released: April 2013; last updated: May 2024

2. A listed issuer entered into an agreement for certain continuing connected transactions in the next 3 years which were exempt from the independent shareholders' approval requirement under the de minimis exemption based on the percentage ratios calculated at that time.

When the listed issuer publishes its next audited accounts, will it be required to calculate the percentage ratios again to determine whether the transactions under the remaining term of the agreement still qualify for the de minimis exemption?

No, if the listed issuer has already complied with the applicable requirements for the transactions at the time it entered into the agreement.

MB Rules 14A.54 and 14A.76
GEM Rules 20.52 and 20.74
First released: February 2013; last updated: May 2024

Financial assistance

3. A listed issuer proposes to fully guarantee a bank loan obtained by a 60% owned connected subsidiary. The controlling shareholder of the listed issuer holds the remaining 40% in the connected subsidiary and will provide a counter-guarantee to the listed issuer for 40% of the loan amount. Does the financial assistance exemption apply to the proposed guarantee?

No. The exemption only applies if the guarantee provided by the listed issuer is in proportion to its interest in the subsidiary and on a several basis.

MB Rule 14A.89
GEM Rule 20.87
First released: March 2014; last updated: May 2024

4. A substantial shareholder of a listed issuer will guarantee a bank loan obtained by the listed issuer. The listed issuer has agreed to indemnify the substantial shareholder for the loan guaranteed by it. Is the provision of indemnity by the listed issuer a connected transaction?

No, given the indemnity is provided in relation to the guarantee provided by the substantial shareholder.

MB Rules 14A.24(4) and 14A.25
GEM Rules 20.22(4) and 20.23
First released: March 2014; last updated: May 2024

Directors' indemnity, service contracts and insurance

5. Does the exemption for provision of directors' indemnity apply if:

(i) the indemnity relates to the director's liabilities to third parties in connection with negligence, default and breach of duty by directors?

No, because provision of indemnity that relates to such director's liabilities is not allowed under the Hong Kong Companies Ordinance.

(ii) the indemnity covers directors' liabilities which are not limited to those arising from his proper discharge of duties?

No, the indemnity would not meet all the conditions set out in MB Rule 14A.91 / GEM Rule 20.89.

MB Rule 14A.91
GEM Rule 20.89
First released: March 2014; last updated: May 2024

6. Can a listed issuer apply the de minimis exemption to a provision of an indemnity for its director that is not exempt under MB Rule 14A.91 / GEM Rule 20.89?

The listed issuer may apply the de minimis exemption only if it can ascertain the maximum exposure that may arise from the director's indemnity arrangement. In this case, it should compute the assets and consideration ratios based on the estimated maximum exposure amount.

MB Rules 14A.76 and 14A.91
GEM Rules 20.74 and 20.89
First released: March 2014; last updated: May 2024

7. How should a listed issuer compute the percentage ratios for a purchase of insurance for its director which is not exempt under MB Rule 14A.96 / GEM Rule 20.94?

The listed issuer should compute the assets, revenue and consideration ratios based on the maximum annual amount of premium payable under the director's insurance.

MB Rules 14A.76 and 14A.96
GEM Rules 20.74 and 20.94
First released: March 2014; last updated: May 2024

8. Does the director's service contract exemption apply if the contract covers the provision of indemnity or purchase of insurance for the director?

No.

MB Rules 14A.91, 14A.95 and 14A.96
GEM Rules 20.89, 20.93 and 20.94
First released: March 2014; last updated: May 2024

Transactions with persons connected with insignificant subsidiaries

9. Can a listed issuer apply alternative size tests to determine if a newly established joint venture (a non-wholly owned subsidiary) meets the insignificant subsidiary exemption?

Yes. The alternative assets ratio would normally be based on the listed issuer's total capital commitment in the joint venture. The profits and revenue ratios are not applicable as the joint venture is newly set up. The listed issuer should consult the Exchange.

MB Rule 14A.09
GEM Rule 20.08
First released: May 2010; last updated: May 2024

10. Is an issuance of securities or a resale of treasury shares to a director of an insignificant subsidiary of the listed issuer a connected transaction?

No. As the insignificant subsidiary exemption applies to the director, the director is not a connected person of the listed issuer.

MB Rules 14A.09 and Note 1 to 13.36(2)(b)
GEM Rules 20.08 and Note 1 to 17.41(2)
First released: February 2013; last updated: June 2024

11. When assessing whether a subsidiary is "insignificant" under MB Rule 14A.09 / GEM Rule 20.08, is a listed issuer required to make adjustments to the financial figures shown in the financial statements in the manner set out in MB Rules 14.16 to 14.19 / GEM Rules 19.16 to 19.19 (e.g. adjust the total assets by the amount of any dividend proposed by the listed issuer)?

No. The listed issuer should use the figures shown in its financial statements without adjustments.

MB Rule 14A.09
GEM Rule 20.08
First released: February 2013; last updated: May 2024

12. When assessing whether a subsidiary is "insignificant" under MB Rule 14A.09 / GEM Rule 20.08, can a listed issuer change from the three-year test to the one year test (or vice versa) from time to time?

Yes.

MB Rule 14A.09
GEM Rule 20.08
First released: May 2010; last updated: May 2024

Buying or selling of consumer goods or services

13. Rule 14A.97(2)(b) / GEM Rule 20.95(2)(b) allows a listed issuer to acquire consumer goods or services in connection with its business provided that there is an open market and transparency in the pricing of the goods or services. How does the listed issuer determine whether there is a "transparency in the pricing of the goods or services"?

Generally, the pricing should not be negotiable. For example, the price labels/price lists are on display at retail stores or the prices are published or publicly quoted.

MB Rule 14A.97(2)(b)
GEM Rule 20.95(2)(b)
First released: May 2010; last updated: May 2024

14. A listed issuer is principally engaged in the provision of financial services including sale of wealth management products to retail customers. Does the consumer goods or service exemption apply to sales of wealth management products to its directors for their personal investments?

Yes, if the same products are made available for sale to other independent customers and the transaction with the director is conducted on normal commercial terms.

MB Rule 14A.97
GEM Rule 20.95
First released: March 2014; last updated: May 2024

Transactions with associates of passive investors

15. To qualify for the passive investor exemption, the passive investor must not have any representatives on the board of directors of the listed issuer or its subsidiaries. Can the passive investor have any board seat(s) at an insignificant subsidiary of the listed issuer?

No.

MB Rule 14A.99
GEM Rule 20.97
First released: March 2014; last updated: May 2024

Transactions with connected persons at the subsidiary level

16. MB Rule 14A.101 / GEM Rule 20.99 exempts transactions between a listed issuer and a connected person at the subsidiary level from the independent shareholder approval requirements. Does this exemption apply to an issue of new shares or a resale of treasury shares by a listed issuer to a connected person at the subsidiary level?

No. Transactions or arrangements involving an issuance of new shares or a resale of treasury shares by a listed issuer to its connected persons are exempt from the connected transaction rules only if they fall under the circumstances described in MB Rules 14A.92 and 14A.92B / GEM Rules 20.90 and 20.90B.

MB Rules 14A.92, 14A.92B, 14A.101 and Note 1 to 13.36(2)(b)
GEM Rules 20.90, 20.90B, 20.99 and Note 1 to 17.41(2)
First released: March 2014; last updated: June 2024

Whether the Exchange would waive the profit forecast requirements in respect of a valuation report on the disposal target disclosed in the listed issuer's announcement and circular for the disposal

Parties

- **Company A** – a PRC issuer listed on the Main Board
- **Purchaser** – a company listed on a PRC exchange
- **Parent** – the ultimate controlling shareholder of each of Company A and the Purchaser
- **Target** – a subsidiary of Company A proposed to be sold to the Purchaser

Facts

1. Company A proposed to sell the Target to the Purchaser in return for new A shares to be issued by the Purchaser (**Transaction**). This was a major and connected transaction for Company A.

2. Since the Transaction involved a transfer of state-owned assets, the PRC regulations required the Purchaser to engage an appraiser to prepare a valuation report on the Target to determine the consideration. The valuation was partly based on the projections of the Target's earnings. A subsidiary of the Parent (but not Company A) would indemnify the Purchaser for any shortfall in the Target's profits compared to the forecasted profits in the valuation report.

3. Company A would disclose the Target's valuation prepared by the appraiser and the basis for determining the consideration in its announcement and circular for the Transaction.

4. As the valuation was based on projections of the Target's earnings, Company A would need to comply with the disclosure and reporting requirements on profit forecasts under the Rules. It requested the Exchange to waive these requirements because:

    a. It was the Purchaser, and not Company A, which was obliged to prepare the valuation report.

    b. Company A was not involved in preparing the report, except for providing the Purchaser with historical financial information. The accounting principles and policies used by the appraiser differed from those used by Company A.

c. While the consideration was based on the valuation report under PRC regulations, Company A's board had considered other factors when assessing the Transaction, including the historical earnings and dividend distributions of the Target and Company A.

d. The Target would cease to be part of Company A after the Transaction so the profit forecast was irrelevant to its future financial position.

e. Therefore, it would be unduly burdensome for Company A to comply with the requirements.

Relevant Listing Rules

5. Rule 14.61 defines a "profit forecast" to mean:

> … any forecast of profits or losses, however worded, and includes any statement which explicitly or implicitly quantifies the anticipated level of future profits or losses, either expressly or by reference to previous profits or losses or any other benchmark or point of reference. It also includes any profit estimate, being any estimate of profits or losses for a financial period which has expired but for which the results have not yet been published. Any valuation of assets (other than land and buildings) or businesses acquired by a listed issuer based on discounted cash flows or projections of profits, earnings or cash flows will also be regarded as a profit forecast.

6. Rule 14.62 states that if an announcement contains a profit forecast for the issuer or a company which is or is proposed to become its subsidiary, the issuer must provide the Exchange with the following no later than the publication of the announcement:

(1) details of the principal assumptions, including commercial assumptions, upon which the forecast is based;

(2) a letter from the listed issuer's auditors or reporting accountants confirming that they have reviewed the accounting policies and calculations for the forecast and containing their report; and

(3) a report from the listed issuer's financial advisers confirming that they are satisfied that the forecast has been made by the directors after due and careful enquiry. If no financial advisers have been appointed in connection with the transaction, the listed issuer must provide a letter from the board of directors confirming they have made the forecast after due and careful enquiry.

7. Rules 14.66(2) and 14A.70(13) state that a circular relating to a major transaction/ connected transaction must contain information in paragraph 29(2) of Appendix 1B if there is a profit forecast.

8. Rule 14A.68(7) states that a connected transaction announcement must contain the information set out in rule 14.62 if the announcement contains a profit forecast of the listed issuer's group or a company which is, or will become, the listed issuer's subsidiary.

9. Paragraph 29(2) of Appendix 1B states that

> … Where a profit forecast appears in any listing document, it must be clear, unambiguous and presented in an explicit manner and the principal assumptions, including commercial assumptions, upon which it is based, must be stated. The accounting policies and calculations for the forecast must be examined and reported on by the reporting accountants or auditors, as appropriate, and their report must be set out. The financial adviser must report in addition that they have satisfied themselves that the forecast has been stated by the directors after due and careful enquiry, and such report must be set out. …

Analysis

10. The reason for preparing the Target's valuation was to comply with the PRC regulations. Company A was not involved in preparing the valuation report. This was different from the circumstances contemplated under Rules 14.62 and 14A.68(7) which assume that the issuer's directors made the forecast. Company A had practical difficulty in complying with the requirements.

Conclusion

11. The Exchange waived the requirements.

Disclosure and other requirements for connected transactions

1. For an acquisition of mining asset, is a listed issuer required to disclose in its circular an independent valuation of the asset under MB Rule 14A.70(8) / GEM Rule 20.68(8)?

Under MB Rules 18.09(3) and 18.10 / GEM Rules 18A.09(3) and 18A.10, a valuation is required for a major or above acquisition of mineral and/or petroleum assets. For the purpose of MB Rule 14A.70(8) / GEM Rule 20.68(8), we will apply the same principle and will only require a valuation if the transaction is classified as major or above.

MB Rules 14A.70(8), 18.09(3) and 18.10
GEM Rules 20.68(8), 18A.09(3) and 18A.10
First released: November 2008; last updated: May 2024

13

Share schemes

Whether the Exchange would approve the proposed changes to the terms of pre-IPO share option plan of the listed issuer

Facts

1. At the listing of a Main Board issuer (**Company A**), the Exchange approved the listing of, and permission to deal in, Company A's shares to be issued upon exercise of the options granted under a pre-IPO share option plan. This was conditional upon the following:

   a. There would be no material change to the rules of the plan without prior shareholder approval.

   b. Company A would promptly inform the Exchange of any modifications of the plan.

2. The options under the plan were granted to Company A's directors, other senior management and other employees. The plan contained the following material terms:

   a. The purpose of the plan was to recognise the contribution to Company A by its employees and to retain those whose contributions were important to the company's long term growth and profitability.

   b. The options could only be exercised in phases as set out in the plan.

   c. The options were personal to the grantees and were not assignable.

   d. The options should lapse automatically upon the grantee ceasing to be Company A's employee.

3. Company A proposed to amend the plan to allow them to transfer the options to persons independent of Company A and/or its connected persons before they became exercisable on condition that no transferees would be allowed to further transfer the options.

Relevant Listing Rules

4. Rule 17.01(1) states that:

   The following provisions apply, with appropriate modifications, to all schemes involving the grant by a listed issuer or any of its subsidiaries of options over new shares or other new securities of the listed issuer or any of its subsidiaries to, or for the benefit of, specified participants of such schemes (and, for the purpose of this chapter, "participant" includes any discretionary object of a participant which is a discretionary trust). Any arrangement involving the grant of options to participants over new shares or other new securities of a listed issuer or any of its subsidiaries which, in the opinion of the Exchange, is analogous to a share option scheme as described in this rule 17.01 must comply with the requirements of this chapter.

5. Rule 17.02(1)(b) states that:

   A scheme adopted by a new applicant does not need to be approved by its shareholders after listing. However, all the terms of the scheme must be clearly set out in the prospectus. Where the scheme does not comply with the provisions of this chapter, options granted before listing may continue to be valid after listing (subject to the Exchange granting approval for listing of the new applicant's securities to be issued upon exercise of such options) but no further options may be granted under the scheme after listing. … .

   Notes: (1) The Exchange reserves the right to review and consider these matters on a case-by-case basis.

   (2) …

6. Rule 17.03(17) states that the scheme document must include a provision on:

   transferability of options; …

   Note: Options granted under the scheme must be personal to the respective grantee. No options may be transferred or assigned.

   (Rules 17.01, 17.02(1)(b) and 17.03(17) were revised on 1 January 2023. Rule 17.01 was further amended on 11 June 2024. See Notes below.)

Analysis

7. At the time of Company A's new listing application, the Exchange granted listing approval for shares to be issued under the pre-IPO plan. The plan did not need to comply with Chapter 17 as it was adopted before listing.

8. The purpose of the plan was to reward and retain employees making contributions to Company A. This was reflected in the conditions that the options (i) could only be exercised in phases; (ii) could not be transferred or otherwise disposed of; and (iii) would automatically lapse upon the grantee ceasing to be Company A's employee or disposing of the options. The proposed amendments which permitted the transfer of the options and enabled the grantees to realise the benefit before they became exercisable would defeat the purpose of and fundamentally change the plan.

9. As a result of the proposed amendments, the circumstances under which the listing approval was granted would be fundamentally changed and the listing approval no longer valid.

10. The Exchange would not approve the proposed amendments to the pre-IPO plan because the amended plan would not comply with Chapter 17.

11. Company A failed to satisfy the Exchange that the proposed amendments would be in the interest of Company A and its shareholders as a whole. The amendments would only benefit the grantees.

Conclusion

12. The Exchange did not allow the proposed amendments.

Notes:

1. Chapter 17 was amended on 1 January 2023. Rules 17.01(1), 17.02(1)(b) and 17.03(17) were extended to cover share award schemes as follows:

   Rule 17.01(1):

   " (1) This Chapter deals with:

   (a) share schemes involving the grant by a listed issuer of (i) new shares of the listed issuer; or (ii) options over new shares of the listed issuer, to, or for the benefit of, specified participants of such schemes (which includes a grant of any such shares or options to a trust or similar arrangement for the benefit of a specified participant (see rules 17.02 to 17.11);

   …"

   Rule 17.02(1)(b):

   "A scheme adopted by a new applicant prior to its listing does not need to be approved by its shareholders after listing. However, all material terms of the scheme must be clearly set out in the prospectus. Where the scheme does not comply with the provisions of this chapter, options and awards granted to, or for the benefit of, specified participants before listing may continue to be valid after listing (subject to the Exchange granting approval for listing of the new applicant's shares to be issued in respect of such options and awards) but no further options or awards may be granted under the scheme after listing…

   Notes: (1) The Exchange reserves the right to review and consider these matters on a case-by-case basis.

   (2) …"

   Rule 17.03(17):

   "The scheme document must include the following provisions and/or provisions as to the following (as the case may be):

   …

   (17) transferability of options or awards;

   Note: Options or awards granted under the scheme must be personal to the respective grantee. No options or awards may be transferred or assigned…

   …"

2. Chapter 17 was further amended on 11 June 2024 to treat a share scheme funded by treasury shares as a share scheme funded by new shares by adding Rule 17.01(4) as follows:

   Rule 17.01(4):

"(4) In this chapter 17, references to new shares or new securities include treasury shares, and references to the issue of shares or securities include the transfer of treasury shares."

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

Share schemes

I. Share schemes funded by issuance of new shares or transfer of treasury shares of listed issuers

(a) Eligible participants

1. Can a part-time employee be included as an eligible employee participant?

MB Rule 17.03A(1) / GEM Rule 23.03A(1) does not differentiate between full-time employees and part-time employees. Listed issuers may define the scope of employee participants for their share schemes to include part-time employees, depending on their remuneration policies. This should be in line with the information relating to employees as disclosed by listed issuers under other Listing Rule requirements (e.g. Appendix D2 to the MB Rules / GEM Chapter 18).

MB Rule 17.03A(1)
GEM Rule 23.03A(1)
First released: July 2022; last updated: May 2024

2. Under MB Rule 17.03A(1) / GEM Rule 23.03A(1), eligible participants of share schemes do not include former employees of the listed issuer group. An individual was granted share options or awards as an eligible employee participant under a listed issuer's share scheme.

(a) Can such grantee continue to hold any outstanding options or awards upon termination of his/her employment with the listed issuer group (e.g. as a good leaver due to retirement, death or disability)?

Yes, if the terms of the scheme provide for it. Under MB Rule 17.03(12) / GEM Rule 23.03(12), the scheme document should set out the circumstances under which options or awards will automatically lapse.

(b) Can the listed issuer continue to make share grants if the individual continues to provide service to the group?

Yes, if the individual meets the definition of service provider under MB Rule 17.03A(1) / GEM Rule 23.03A(1) and the criteria set out in the scheme.

MB Rules 17.03A(1) and 17.03(12)
GEM Rules 23.03A(1) and 23.03(12)
First released: July 2022; last updated: May 2024

3. Are eligible service providers restricted only to natural persons (and not corporate entities)?

No. A service provider may be a natural person or corporate entity engaged by the listed issuer group to provide services.

MB Rule 17.03A(1)(c)
GEM Rule 23.03A(1)(c)
First released: July 2022; last updated: May 2024

4. MB Rule 17.03A(2) / GEM Rule 23.03A(2) requires the scheme document to clearly identify each category of service providers and the criteria for determining a person's eligibility under each category. What is the level of detail required to be disclosed by a listed issuer in this regard?

The listed issuer should clearly describe the types of services provided by service providers that would qualify them for the scheme, for example, insurance agents employed by an insurance company, advisory services provided on drugs under development, or persons providing services on a self-employed basis for specific projects. The listed issuer should also disclose the factors it applies to assess whether the person provides services on a continuing and recurring basis and in the listed issuer's ordinary and usual course of business.

The scheme document is subject to pre-vetting by the Exchange. Where necessary, the independent non-executive directors may be required to provide their views that the inclusion of these service providers as scheme participants aligns with the purpose of the scheme and the long term interests of the listed issuer and its shareholders (see note to MB Rule 17.02(2)(e) / GEM Rule 23.02(2)(e)).

MB Rules 17.02(2)(e) and 17.03A(2)
GEM Rules 23.02(2)(e) and 23.03A(2)
First released: July 2022; last updated: May 2024

5. Note to MB Rule 17.02(2)(e) / GEM Rule 23.02(2)(e) provides that where the scheme includes service providers and/or related entity participants as eligible participants, the Exchange may require the circular to include the views of the independent non-executive directors (INEDs) of the issuer on whether the inclusion of these participants aligns with the purpose of the scheme and the long term interests of the issuer and its shareholders.

(a) Is the listed issuer required to establish an independent board committee to form such views?

No. The listed issuer may obtain the views of its INEDs without establishing an independent board committee.

(b) Is the listed issuer required to appoint an independent financial adviser to advise the INEDs?

MB Rule 17.02(2)(e) / GEM Rule 23.02(2)(e) does not mandate a listed issuer to appoint an independent financial adviser to advise the INEDs. However, as provided under the Corporate Governance Code (CP C.5.6 of Appendix C1 to the MB Rules / Appendix C1 to the GEM Listing Rules), a listed issuer should, upon reasonable request, provide separate independent professional advice to its directors to assist them perform their duties to the listed issuer.

MB Rule 17.02(2)(e) and CP C.5.6 of AppC1
GEM Rule 23.02(2)(e) and CP C.5.6 of AppC1
First released: July 2022; last updated: May 2024

(b) Scheme mandate

6. Can a listed issuer adopt a share scheme that can be funded by either new shares issued by the listed issuer and/or existing shares purchased on market?

Yes.

MB Rule 17.01(1)
GEM Rule 23.01(1)
First released: July 2022; last updated: May 2024

7. Is the scheme mandate for grants of new shares under MB Chapter 17 / GEM Chapter 23 a separate mandate from the general mandate under MB Rule 13.36 / GEM Rule 17.39?

Yes.

MB Rules 13.36 and 17.03B
GEM Rules 17.39 and 23.03B
First released: July 2022; last updated: May 2024

8. Can a listed issuer grant new shares to a person for incentive purposes under a general or specific mandate under MB Rule 13.36 / GEM Rule 17.39 if the share grants fall outside the scope of share schemes under MB Chapter 17 / GEM Chapter 23?

Yes, for example, if the grantee does not meet the definition of eligible participant under MB Chapter 17/ GEM Chapter 23.

MB Rules 13.36 and 17.03B
GEM Rules 17.39 and 23.03B
First released: July 2022; last updated: May 2024

9. Will the Exchange grant waivers from scheme mandate limit of 10% and individual limit of 1% for schemes of issuers operating in businesses other than the internet technology sector? If so, what are the criteria?

The Exchange will consider waiver applications from listed issuers operating in businesses other than the internet technology sector on a case-by-case basis, taking into account factors such as the industry norm, the listed issuer's remuneration policy and its justification for requiring a higher limit.

MB Rules 17.03B, 17.03C and 17.03D
GEM Rules 23.03B, 23.03C and 23.03D
First released: July 2022; last updated: May 2024

10. Can an applicant adopt a post-IPO share scheme and issue new shares to the trustee of the share scheme before listing in order to fund future grants of awards and options to participants after listing?

No, since there are no specified participants when issuing new shares to the trustee.

Grants made to a trust or similar arrangement are allowed only if they are made for the benefit of specified participants. The Exchange would not grant listing approval for the issue of new shares under the proposed scheme which is not in compliance with MB Chapter 17 / GEM Chapter 23.

MB Rules 17.01(1) and 17.02(1)(b)
GEM Rules 23.01(1) and 23.02(1)(b)
First released: July 2022; last updated: May 2024

11. A listed issuer granted a certain amount of share awards to an employee who may, upon vesting, choose to receive new shares of the listed issuer and/or cash in accordance with the terms of the share scheme. If all or part of the awards are settled by cash (instead of new shares) upon vesting, would the listed issuer be required to deduct that portion from the scheme mandate limit?

No.

MB Rule 17.03B
GEM Rule 23.03B
First released: July 2022; last updated: May 2024

(c) Minimum vesting period

12. Under MB Rule 17.03F / GEM Rule 23.03F, a scheme document may set out the specific circumstances where options or awards may be granted to employee participants with a shorter (or no) vesting period. What would the Exchange consider as justifiable circumstances for a shorter (or no) vesting period?

The Exchange would consider factors such as the purpose of the schemes, the listed issuers' remuneration policies and the market practices. This review takes place during the pre-vetting of the shareholders' circular for the approval of the scheme. The following are examples of circumstances where the Exchange may consider to be justifiable:

(i) Grants of "make-whole" share awards to new joiners to replace the share awards they forfeited when leaving the previous employers;

(ii) Grants to a participant whose employment is terminated due to death or disability or occurrence of any out of control event. In those circumstances the vesting of share awards may accelerate;

(iii) Grants of options or awards with performance-based vesting conditions provided in the scheme document, in lieu of time-based vesting criteria;

(iv) Grants that are made in batches during a year for administrative and compliance reasons. They may include share awards that should have been granted earlier but had to wait for a subsequent batch. In such cases, the vesting periods may be shorter to reflect the time from which an award would have been granted;

(v) Grants of options or awards with a mixed or accelerated vesting schedule such as where the awards may vest evenly over a period of 12 months; and

(vi) Grants of options or awards with a total vesting and holding period of more than 12 months.

MB Rule 17.03F
GEM Rule 23.03F
First released: July 2022; last updated: May 2024

(d) Limits on granting options or awards to individual participants and connected persons

13. Do the limits on grants of options or awards to connected persons under MB Rule 17.04 / GEM Rule 23.04 apply to grants to persons connected at the subsidiary level?

No. The limits set out in the Rule apply to connected persons at the listed issuer level only.

MB Rule 17.04
GEM Rule 23.04
First released: July 2022; last updated: May 2024

14. A listed issuer proposes to grant share awards to an individual participant who is an associate of a director of the listed issuer. Would the listed issuer be required to aggregate the grants of awards to the individual participant with any grants to the director within a 12-month period for the purpose of calculating (i) the 1% individual limit; and (ii) the limit on grants to connected persons?

No. The grants are for the service of, and to incentivise each participant and as such, the listed issuer is not required to aggregate such options and awards with those granted to the director.

MB Rules 17.03D and 17.04
GEM Rules 23.03D and 23.04
First released: July 2022; last updated: May 2024

(e) Transfer of share awards or options

15. Under the note to MB Rule 17.03(17) / GEM Rule 23.03(17), the Exchange may consider granting a waiver to allow a transfer of options or awards to a vehicle (such as a trust or a private company) for the benefit of the participant and any family members of such participant (e.g. for estate planning or tax planning purposes) that would continue to meet the purpose of the scheme and comply with other requirements of MB Chapter 17 / GEM Chapter 23. What are the conditions for granting the waiver?

The listed issuer and the grantee must establish appropriate measures to ensure that after the transfer, the options or awards granted would continue to be for the benefit of the participant and any family members of such participant. These may include, among other, measures to restrict further transfers of the options or awards or changes in the beneficiaries of the trust upon the grant of the waiver.

MB Rules 17.03D, 17.04 and 17.03(17)
GEM Rules 23.03D, 23.04 and 23.03(17)
First released: July 2022; last updated: May 2024

(f) Adjustments to the exercise price of share options

16. MB Rule 17.03(13) / GEM Rule 23.03(13) permits adjustments to be made to the exercise or purchase price and/or the number of shares subject to share options or share awards granted under a share scheme in the event of certain corporate activities. Any adjustments must give a participant the same proportion of the equity capital as that to which that person was previously entitled.

How should a listed issuer calculate the adjustments in the event of (i) a capitalisation or bonus issue, (ii) rights issue or open offer, or (iii) subdivision or consolidation of shares?

See **Appendix 1** for further guidance and examples on how adjustments are calculated in the event of the corporate activities.

MB Rule 17.03(13)
GEM Rule 23.03(13)
First released: November 2020; last updated: May 2024

II. Share schemes of subsidiaries of listed issuers

17. A listed issuer has complied with the requirements of MB Chapter 14 / GEM Chapter 19 when its subsidiary (which is not a principal subsidiary) adopted a share scheme. Will the listed issuer be required to comply with the requirements of MB Chapter 17 / GEM Chapter 23 for the share scheme if the subsidiary subsequently became a principal subsidiary?

The requirements of MB Chapter 17 / GEM Chapter 23 will apply to the share scheme when the subsidiary proposes to refresh the scheme mandate limit or effect a material change to the terms of the subsidiary's scheme after it has become a principal subsidiary.

MB Rule 17.14
GEM Rule 23.14
First released: July 2022; last updated: May 2024

III. Implementation and transitional arrangements

18. The amended Rules relating to share schemes became effective on 1 January 2023. What are the transitional arrangements for existing share schemes of listed issuers and their subsidiaries adopted before the effective date of the Rule amendments?

See **Appendix 2** for details of the transitional arrangements.

MB Chapter 17
GEM Chapter 23
First released: July 2022; last updated: May 2024

19. A listed issuer has adopted (i) a share option scheme and (ii) a share award scheme involving issue of new shares under an advanced / general mandate before the effective date of the Rule amendments (ie before 1 January 2023). After the effective date of the Rule amendments, can the listed issuer refresh or seek a new scheme mandate for its share option scheme and share award scheme separately at different times?

No. As the scheme mandate limit of 10% applies to all schemes of the listed issuer, it must amend all its existing share schemes involving issue of new shares when it refreshes or seeks a new scheme mandate for any one share scheme.

MB Rule 17.03B
GEM Rule 23.03B
First released: July 2022; last updated: May 2024

20. Is a listed issuer required to seek shareholders' approval if it proposes to amend the terms of its existing share schemes to comply with MB Chapter 17 / GEM Chapter 23 as amended?

Yes. Any alterations to the terms and conditions of a share scheme which are of material nature must be approved by shareholders under MB Rule 17.03(18) / GEM Rule 23.03(18). However, as provided under the transitional arrangements, a listed issuer can continue to make grants to participants eligible under existing schemes until refreshment or expiry of the existing scheme mandate, upon which the listed issuer would be required to amend the terms of the schemes to comply with the amended MB Chapter 17 / GEM Chapter 23 and seek shareholders' approval for a new scheme mandate.

MB Rule 17.03(18)
GEM Rule 23.03(18)
First released: July 2022; last updated: May 2024

Appendix 1

Supplementary Guidance on MB Rule 17.03(13) / GEM Rule 23.03(13) and the Note to the Rule

Interpretation

The overriding principle is that no adjustments to the exercise price or number of shares should be made to the advantage of scheme participants without specific prior shareholders' approval. The adjustment should have a neutral impact or worse from the perspective of the scheme participants. Another way of looking at this is that no adjustments should be made that would increase the aggregate Intrinsic Value[1] of the outstanding options.

A straightforward proportionate adjustment should be made for a capitalisation issue, sub-division, consolidation or reduction in share capital. Generally, adjustments should also be made for transactions where there is a price-dilutive element e.g. a rights issue or open offer. (Although MB Rule 17.03(13) / GEM Rule 23.03(13) does not cover an open offer, the Exchange considers that an open offer should be subject to the requirement of such rule if there is a price-dilutive element). That adjustment should be based on a scrip factor similar to the one used in accounting standards in adjusting the earnings per share figures, to account for the bonus or price-dilutive element embedded in a rights issue (see Hong Kong Accounting Standards 33, Appendix A). No adjustment should be made for a transaction made at full consideration unless it also involves a capitalisation issue.

Set out below are examples for calculating the permitted adjustment to the exercise price of outstanding options for a capitalisation or bonus issue, rights issue or open offer and sub-division or consolidation of shares. These examples also apply to cases involving the calculation of adjustment to the purchase price of shares subject to share awards granted.

I. *Capitalisation or Bonus Issue and Rights Issue or Open Offer of Shares*

Adjustments follow the formula:

$$\text{New Number of Options} = \text{Existing Number of Options} \times F$$

$$\text{New Exercise Price} = \text{Existing Exercise Price} \times \frac{1}{F}$$

Where:

$$F = \frac{CUM}{TEEP}$$

CUM = Closing price as shown in Daily Quotation Sheet of the Exchange on the last trading day before going ex-entitlement to the offer (the cum-rights price)

$$\text{TEEP (Theoretical Ex Entitlement Price)} = \frac{CUM + [M \times R]}{1 + M}$$

M = Entitlement per Existing Share

R = Subscription Price

[1] The Intrinsic Value is the difference between the market price (or theoretical ex-entitlement price) of shares under option and the exercise price (or revised exercise price) of the option.

(a) Capitalisation or Bonus Issues

Example:

Existing shares in issue (excluding treasury shares) : 100m
Shares under Option : 10m (10% of the existing share capital (excluding treasury shares))
Existing market price of the Shares : $1.00
Existing Exercise Price of the Option : $1.00 per Share
Bonus issue ratio: 1 new Share for every ten Shares held

i.e. CUM = $1.00, R = $0 and M = 0.1

Therefore,

$$TEEP = \frac{CUM + [M \times R]}{1 + M}$$

$$= \$0.909$$

$$F = \frac{CUM}{TEEP}$$

$$= 1.1$$

New Number of Options = Existing Number of Options x F

= 11m

(Additional 1m Options will be allocated to the existing holder of Options in the proportion of 1 new Option for every 10 Options held by an Optionholder.)

$$\text{New Exercise Price} = \text{Existing Exercise Price} \times \frac{1}{F}$$

$$= \$0.909$$

Intrinsic Value of Options immediately before the Bonus Issue = 10m x ($1.00 - $1.00)

= Zero

Intrinsic Value of Options immediately after the Bonus = 11m x ($0.909 - $0.909)

= Zero

The purpose of these adjustments is to ensure that, as far as possible, the intrinsic value of the Options remains unchanged before and after the corporate action.

(b) Rights Issue or Open Offer

Example:

Existing shares in issue (excluding treasury shares) : 100m
Shares under Option : 10m (10% of the existing share capital (excluding treasury shares))
Existing market price of the Shares : $1.00
Existing Exercise Price of the Option : $1.00 per Share
Rights issue (or open offer) price : $0.50
Rights issue (or open offer) ratio : 4 new Shares for each Share held

i.e. CUM = $1.00, R =$0.50 and M = 4

Therefore,

$$\text{TEEP} = \frac{\text{CUM} + [\text{M} \times \text{R}]}{1 + \text{M}}$$

$$= \$0.60$$

$$\text{F} = \frac{\text{CUM}}{\text{TEEP}}$$

$$= 1.667$$

New Number of Options = Existing Number of Options x F

= 16.67m

(Additional 6.67m Options will be allocated to the existing holders of Options in the proportion of 2 new Options for every 3 Options held by an Optionholder.)

$$\text{New Exercise Price} = \text{Existing Exercise Price} \times \frac{1}{\text{F}}$$

$$= \$0.60$$

Intrinsic Value of Options immediately before the Bonus Issue = 10m x ($1.00 - $1.00)

= Zero

Intrinsic Value of Options immediately after the Bonus = 16.67m x ($0.60 - $0.60)

= Zero

II. *Subdivision or Consolidation of Shares*

Adjustments follow the formula:

New Number of Options = Existing Number of Options x F

New Exercise Price = Existing Exercise Price x $\frac{1}{F}$

Where F = Subdivision or Consolidation Factor

(a) Share Sub-division

Example:

Existing shares in issue (excluding treasury shares) : 100m
Shares under Option : 10m (10% of the existing share capital (excluding treasury shares))
Existing market price of the Shares : $1.00
Existing Exercise Price of the Option : $1.00 per Share
Share Subdivision: subdivide 1 old Share into 5 new Shares

i.e. F = 5

Therefore,

New Number of Options = Existing Number of Options x F

= 50m

(Additional 40m Options will be allocated to the existing holder of Options in the proportion of 4 new Options for each Option held by an Optionholder.)

New Exercise Price = Existing Exercise Price x $\frac{1}{F}$

= $0.20

Intrinsic Value of Options immediately before the Bonus Issue = 10m x ($1.00 - $1.00)

= Zero

Intrinsic Value of Options immediately after the Bonus = 50m x ($0.20 - $0.20)

= Zero

(b) Share Consolidation

Example:

Existing shares in issue (excluding treasury shares) : 100m
Shares under Option : 10m (10% of the existing share capital (excluding treasury shares))
Existing market price of the Shares : $1.00
Existing Exercise Price of the Option : $1.00 per Share
Share Consolidation: consolidate 5 old Shares into 1 new Share

i.e. F = 1/5 = 0.20

Therefore,

New Number of Options = Existing Number of Options x F

= 2m

(The new 2m Options will be allocated to the existing holder of Options in the proportion of 1 new Option for every 5 old Options held by an Optionholder.)

$$\text{New Exercise Price} = \text{Existing Exercise Price} \times \frac{1}{F}$$

= $5.00

Intrinsic Value of Options immediately before the Bonus Issue = 10m x ($1.00 - $1.00)

= Zero

Intrinsic Value of Options immediately after the Bonus = 2m x ($5.00 - $5.00)

= Zero

Appendix 2

Transitional arrangements for share schemes existing as at 1 January 2023

<table>
<tr><th rowspan="2"></th><th colspan="3">Listed issuer</th><th colspan="2">Principal subsidiary</th><th>Other subsidiaries</th></tr>
<tr><th>Share option scheme</th><th colspan="2">Share award scheme</th><th>Share option scheme</th><th>Share award scheme</th><th>Share option scheme / Share award scheme</th></tr>
<tr><td>Disclosure in:-
- Announcement[2]
- Interim Report[3]
- Annual Report[4]</td><td colspan="5">From effective date (1 January 2023)</td><td rowspan="4"><u>Share option scheme that has complied with existing Chapter 17:</u>

The subsidiary may continue to grant share options under its scheme mandate

<u>Other existing or new share schemes:</u>

Grants of share awards or options must comply with MB Chapter 14 / GEM Chapter 19 (based on the size of the scheme mandate for future grants) and/or MB Chapter 14A / GEM Chapter 20</td></tr>
<tr><td>Share grants to eligible participants (amended definition)[5]</td><td colspan="5">New definition of eligible participants applies for financial years commencing on or after 1 January 2023</td></tr>
<tr><td>Scheme mandate[6]</td><td>Listed issuers may continue to make share grants using existing scheme mandate</td><td colspan="2">Listed issuers may grant shares under general mandate until the <u>second</u> AGM after 1 January 2023</td><td>Same as listed issuer</td><td>Listed issuers must comply with MB Chapter 14 / GEM Chapter 19 (based on the size of the scheme mandate for future grants) and/or MB Chapter 14A / GEM Chapter 20 before making share grants</td></tr>
<tr><td>Amendment of terms of scheme to comply with amended MB Chapter 17 / GEM Chapter 23</td><td colspan="5">On or before the refreshment of the scheme mandate limit / expiry of scheme mandate above or adoption of new share scheme</td></tr>
</table>

[2] See MB Rules 17.06A, 17.06B and 17.06C / GEM Rules 23.06A, 23.06B and 23.06C

[3] See MB Rules 17.07 and 17.09 / GEM Rules 23.07 and 23.09

[4] See footnote 3

[5] See MB Rule 17.03A / GEM Rule 23.03A

[6] See MB Rules 17.03B and 17.03C / GEM Rules 23.03B and 23.03C

14

Issuers listed under special listing regimes or other listing structures

14.1 Overseas issuers

Guidance letter – Guidance for overseas issuers	GL111-22	14.1 – 1
Guidance letter – Change of listing status from secondary listing to dual-primary or primary listing on the Main Board	GL112-22	14.1 – 12
Frequently asked questions – Overseas issuers	FAQ14.1 – No.1-3	14.1 – 38

14.2 Mineral companies

Guidance letter – Guidance on continuing obligations under Chapter 18	GL47-13	14.2 – 1
Listing decision – Whether the Exchange would grant a waiver to a listed issuer to allow it to defer the publication of the competent person's report, valuation report and other disclosures for an acquisition of an overseas listed mineral company in a hostile takeover	LD45-2013	14.2 – 4
Listing decision – Whether the Exchange would waive the requirement to publish a competent person's report on the mineral resources to be disposed of by a listed issuer	LD42-2013	14.2 – 8
Listing decision – Whether the Exchange would waive the requirements to publish competent person's reports and valuation reports on some of the mining interests held by the target company to be acquired by the listed issuer	LD40-2013	14.2 – 10

Listing decision – Whether the Exchange would waive the requirements to publish a competent person's report and a valuation report on the mineral assets held by an overseas listed target company to be acquired by the listed issuer	LD65-2013	14.2 – 12
Frequently asked questions – Mineral companies	FAQ14.2 – No.1-5	14.2 – 16

14.3 SPACs

Guidance letter – Guidance on special purpose acquisition companies	GL113-22	14.3 – 1
Frequently asked questions – Special Purpose Acquisition Companies	FAQ14.3 – No.1-13	14.3 – 13

14.4 Collective investment schemes

Guidance letter – Guidance on disclosure by management companies of SFC-authorised Exchange Traded Funds	GL109-20	14.4 – 1
Guidance letter – Guidance on authorised collective investment schemes	GL79-14	14.4 – 4

Guidance for overseas issuers

I. Background and purpose

1. This letter provides guidance for new listing applicants and listed issuers that are incorporated outside of Hong Kong or the PRC (i.e. overseas issuers), including those seeking a dual-primary or secondary listing. The guidance is also set out in Chapter 2.1 of the Guide for New Listing Applicants (**Guide**). See also the "Listing of Overseas Issuers" on the Exchange's website for further information.

2. Overseas issuers may face practical or operational difficulties complying with the Listing Rules or the Codes on Takeovers and Mergers and Share Buy-backs (**Codes**) where there is a potential conflict between the laws and regulations of its home jurisdiction and the Listing Rules or the Codes:

Below are some examples of foreign laws and regulations that may cause compliance difficulties with the Listing Rules or the Codes:

- Those that prohibit a company from restraining or restricting its shareholders from voting on any particular resolution, including shareholders with a material interest in the transaction or arrangement being voted upon.
- Those that require a management or supervisory body of a company to approve matters that, under the Listing Rules, would require shareholders' approval.
- Those that require a company to employ a board of statutory auditors, instead of establishing a board committee to oversee accountability and audit related matters. A board of statutory auditors may play a role similar to audit committees under the Listing Rules and may have broader oversight responsibilities and greater independence.
- Those that do not recognise a nominee company holding securities on behalf of third parties, such as HKSCC Nominees Limited (**HKSCCN**) that holds listed securities on behalf of CCASS participants.

3. Overseas issuers subject to such compliance difficulties may need to take alternative procedures, including providing undertakings to the Exchange to put in place a shareholder protection measure or by demonstrating it has adopted internal compliance measures that achieve the same outcome. Companies are strongly encouraged to consult the Exchange and the Takeovers Executive[1] (where applicable) at the earliest opportunity.

[1] The Takeovers Executive refers to the Executive Director of the Corporate Finance Division or any delegate of the Executive Director of SFC.

II. Core shareholder protection standards and admission to CCASS

4. MB/GEM Appendix A1 requires an issuer to demonstrate how the domestic laws, rules and regulations to which it is subject and its constitutional documents, in combination (**Domestic Standards**) provide the shareholder protection standards set out therein (**Core Shareholder Protection Standards**). For this purpose, the Exchange may require an overseas issuer to amend its constitutional documents to provide the Core Shareholder Protection Standards.

5. Each overseas issuer is required to comply with the following requirements:

   (a) (a) Its constitutional documents conform with the Core Shareholder Protection Standards, and on the whole, are not inconsistent with the Listing Rules and the laws of the place where the overseas issuer is incorporated or otherwise established; (b) there are no material issues identified in relation to the matters under Part I of Form M120 (Information Required From Overseas Issuers) (**Form M120**)[2]; and (c) it can comply with other applicable requirements set out in this letter (collectively the **Shareholder Protection Requirements**); and

   (b) The overseas issuer is incorporated in a jurisdiction where securities of companies incorporated therein is eligible for admission into CCASS for trading on the Exchange (the **Admission Requirement**).

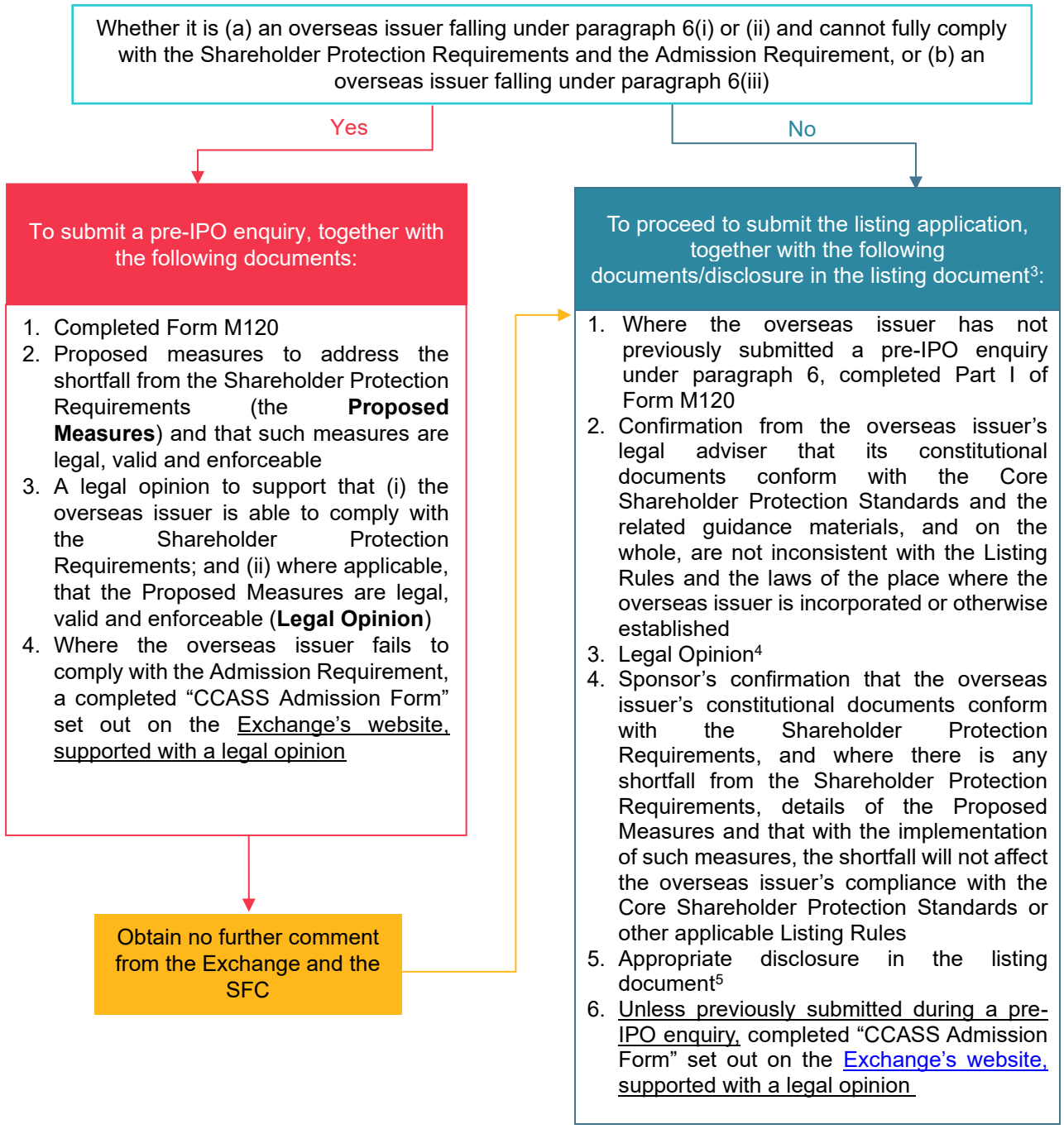
6. Prior to filing a listing application, an overseas issuer and sponsor should check its compliance with the Shareholder Protection Requirements and the Admission Requirement and assess whether a pre-IPO enquiry is required:

[2] The Exchange reserves the right to require any overseas issuer to complete and submit the Form M120 where it considers necessary.

	(i) Overseas Issuer Incorporated in Bermuda or Cayman Islands	(ii) Overseas Issuers incorporated in a jurisdiction listed on the "List of Overseas Jurisdictions of Incorporation" published on the Exchange's website	(iii) Overseas Issuers other than paragraph 6(i) and (ii)
To comply with the Shareholder Protection Requirements and identify any material issues	Yes		
To comply with the Admission Requirement	Yes		
Whether a pre-IPO enquiry is required	Generally no, unless the overseas issuer cannot fully comply with the Shareholder Protection Requirements and the Admission Requirement	Depends on whether the overseas issuer can fully comply with the Shareholder Protection Requirements and the Admission Requirement (and where applicable, further guidance on specific jurisdictions published on the Exchange's website)	Yes

7. An overseas issuer that is required to make a pre-IPO enquiry based on the assessment under Paragraph 6 above can only submit its listing application after the Exchange and the SFC have confirmed they have no further comment on the issues.

8. The diagram below sets out the documentary requirements and when such documents are required to be submitted:



[3] Overseas issuers incorporated in Bermuda or the Cayman Islands are not required to submit items 1, 4 and 6, unless they have previously submitted a pre-IPO enquiry under paragraph 6.

[4] If any legal opinion has been provided at the pre-IPO enquiry stage, the overseas issuer only needs to provide a bring-down legal opinion confirming that the position in the earlier legal opinion is still valid at the time of submitting a listing application. If a legal opinion cannot be obtained, the requirement may be met by the submission of a written confirmation issued by the overseas issuer's legal adviser.

[5] (i) The major differences between Domestic Standards and the Core Shareholder Protection Standards and details of the Proposed Measures; and (ii) the risk that the extent to which Hong Kong courts may be used as an avenue for aggrieved shareholders of non-Hong Kong issuers is subject to certain limitations concerning, for example, enforcement of a Hong Kong judgment against the overseas assets, operations and/or directors of a non-Hong Kong issuer listed on the Exchange and enforcement of an overseas judgment in Hong Kong courts.

9. Listed overseas issuers should monitor their on-going compliance with the Core Shareholder Protection Standards. They must, at the earliest opportunity, inform the Exchange of any material changes in the overseas laws, rules and market practices that would, or may, adversely affect their compliance with the Core Shareholder Protection Standards and other Listing Rules. Where applicable, the Exchange will publish guidance on the relevant jurisdictions[6].

10. With regard to matters not covered by any Core Shareholder Protection Standard or Listing Rules, reliance will be placed on a combination of the overseas laws and regulations to which the overseas issuers are subject and their constitutional documents.

11. Overseas issuers are reminded that they are required under the Listing Rules to ensure all information provided to the Exchange must be accurate and complete in all material respects. They should notify the Exchange of any material matters that may assist the Exchange's consideration of its listing application. The Exchange reserves the right to reject an overseas issuer on suitability grounds where the issuer fails to address any material issue.[7]

12. It is the responsibility of each overseas issuer to exercise reasonable judgment (after seeking professional advice where necessary) as to what falls within the scope of the requirement under paragraph 11 and how material issues associated with the applicable laws and regulations or the overseas issuer's constitutional documents should be addressed. We will determine, on a case-by-case basis, whether an overseas issuer has satisfactorily addressed such matters to ensure a sufficient level of investor protection.

III. Eligibility of securities and admission of securities into CCASS

13. HKSCC is a recognised clearing house under the SFO. It operates the CCASS which provides deposit, clearance and settlement services to participants of CCASS subject to the General Rules of HKSCC and HKSCC Operational Procedures in effect from time to time.

14. All listing applicants must make arrangements with HKSCC to ensure their securities are accepted as eligible for deposit, clearance and settlement in CCASS in accordance with the General Rules of HKSCC[8]. See paragraph 8 above for documentary requirements and the Exchange's website for further information on admission of securities into CCASS.

15. An overseas issuer is encouraged to notify the Exchange at an early stage of the nature of the securities it plans to issue and list, particularly as to:

(i) The form of its securities:	(a) Physical scrip; or (b) Scripless/book entry;
(ii) Where physical scrip is issued, whether:	(a) It will be in definitive or global form; and (b) The certificate will be in registered or bearer form;

6 Prior to 2021, the Exchange had published country guides on various jurisdictions to provide specific guidance for overseas issuers incorporated in those jurisdictions on the relevant comparison between the Domestic Standards and the then applicable shareholder protection standards, as well as the Exchange's expectations, practices, procedures and the criteria it considers when applying the Listing Rules to overseas issuers incorporated in such jurisdictions. From 2021, guidance may be issued on a case-by-case basis if there are novel issues relating to the listing of securities (including securities of companies incorporated in a jurisdiction not covered by any guidance materials).

7 See MB Rule 9.03(3A) and paragraph (b) of MB Appendix E1; GEM Rule 12.09(3A) and paragraph (b) of GEM Appendix E1.

8 MB Rule 8.13A; GEM Rule 11.29.

(iii) Where securities are to be issued in scripless form	The applicant must inform the Exchange of the holding structure of the securities with details of: (a) How Hong Kong investors (through HKSCCN) will hold the securities; (b) The financial intermediaries or depositories holding the securities on behalf of Hong Kong investors, in particular their roles and responsibilities under the relevant overseas jurisdiction's rules and regulations; and (c) Who will be recognised as the legal owners of the securities in the applicant's place of incorporation[9];
(iv) How will its Hong Kong branch register of members be maintained and when the register will be opened for inspection by members[10];	
(v) If securities are in physical scrip, what are the procedures to replace lost certificates and whether there will be any restrictions on holding or transfer of the new certificates; and	
(vi) Whether there will be any restrictions on Hong Kong investors' right to attend the applicant's general meetings to vote and/or to appoint proxies.	

IV. Cross-border clearing and settlement

16. The Hong Kong securities market adopts a T+2 settlement period in the post-IPO market. This means that executed trades are settled in CCASS two business days after the trade day.

17. Dual-primary or secondary listed companies normally have their principal share registers in their overseas markets and a branch register in Hong Kong. To ensure liquidity in the Hong Kong registered shares, dual-primary or secondary listed companies must ensure there are a sufficient number of registered shares on their Hong Kong share registers.

18. A dual-primary or secondary listed company that does not conduct a public offering is expected to transfer a sufficient number of shares to its Hong Kong share register from its overseas share register before listing. The estimate of "sufficient number of shares" should be based on the historical trading statistics of the issuer's securities in its overseas market and the expected increase in trading upon listing in Hong Kong. This can be arranged by the appointed share registrars cancelling and re-issuing share certificates[11] in the issuer's respective markets.

19. An overseas issuer that has a listing on the Exchange and another exchange must adopt precautionary measures to mitigate price volatility of its shares upon listing and the demand/supply imbalances between its overseas market and Hong Kong to ensure sufficient liquidity. The precautionary measures must take into account the issuer's shareholding structure and availability of arbitrage opportunities between Hong Kong and the other market where it is listed. Overseas issuers may refer to Chapter 4.12 of the Guide on some precautionary measures for overseas issuers listed in Hong Kong by way of introduction.

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9 The need for these notifications will be reviewed upon the implementation of an uncertificated securities market in Hong Kong. The consultation conclusions for this regime was published on 8 April 2020.

10 The overseas issuer must also inform members of the conditions for inspection.

11 Unless where the securities are issued in scripless form.

V. HDRs

20. HDRs can be held by Hong Kong investors in substantially the same way as shares. They are issued by a financial institution acting as a depositary and represent a particular ratio to an applicant's shares.

21. See (i) information on the HDR Framework section of the Exchange's website; and (ii) Chapter 5.1 of the Guide for further details on HDRs.

VI. Alternative procedures for U.S. "domestic issuers"

22. "Domestic issuers" within the meaning of Regulation S (**Regulation S**) under the United States Securities Act of 1933 who wish to offer their equity securities (**Regulation S Securities**) in "offshore transactions" within the meaning of, and in reliance on the safe harbor provided by, Regulation S must fulfil the requirements of that regulation (the **Regulation S Category 3 Requirements**).

23. Given the manner in which securities are traded and settled on the Exchange, it is not feasible for such "domestic issuers" and their underwriters to comply strictly with certain of the Regulation S Category 3 Requirements in connection with a listing of Regulation S Securities on the Exchange. Accordingly, the Exchange has formulated certain alternative procedures tailored to address the underlying policy concerns. See the Exchange's website for further details.

VII. Stock name identification

24. To enable investors to identify the following types of listed overseas issuers, such overseas issuers that are listed on the Exchange are required to clearly label their stock short names with appropriate suffixes. The specified stock short names/codes for such overseas issuers are as follows:

Suffix "DR" and a stock code between 6200-6399	Listed HDRs.
Suffix "RS" and a stock code between 6300-6399	Incorporated in the U.S. with listed securities/HDRs that are restricted securities under U.S. federal securities laws.
Suffix "S"	Secondary listing in Hong Kong.
Suffix "TP"	Secondary listed issuer in Hong Kong that voluntarily converts or delists it shares or depositary receipts from the overseas exchange on which it is primary listed but cannot comply fully with the applicable Listing Rules immediately upon the change of its listing status and has applied for a grace period as time-relief waiver.

VIII. Company Information Sheet

25. Company Information Sheets must be prepared by (i) all secondary listed issuers (see MB Rule 19C.24); and (ii) any other primary listed or dual-primary listed overseas issuers (including issuers incorporated in Bermuda and Cayman Islands) that meet any of the criteria set out in MB Rule 19.60 (GEM Rule 24.27).

26. The Exchange may also at its own discretion require a primary listed or dual-primary listed overseas issuer to publish a Company Information Sheet where the Exchange believes the publication of a Company Information Sheet would be informative to investors (for example, to provide them with information on overseas laws and regulations to which the issuer is subject and which may be unfamiliar to investors in Hong Kong). The issuers and their advisers should determine the materiality of information to be included in the Company Information Sheet. Issuers are encouraged to consult the Exchange if they are uncertain about the requirements.

27. A listed overseas issuer required to issue a Company Information Sheet as stated above shall publish the Company Information Sheet within 3 months from the time of the Exchange's request.

IX. Financial reporting standards, auditing standards and taxation

Financial reporting standards

28. The Listing Rules state that the annual financial statements[12] and the accountants' reports of overseas issuers must be prepared and drawn up in conformity with financial reporting standards acceptable to the Exchange, which will normally be HKFRS or IFRS. However, the Exchange may allow a report to be drawn up otherwise than in conformity with HKFRS and IFRS[13].

29. The suitability of a body of alternative financial reporting standards depends on whether there is any significant difference between the foreign financial reporting standards and IFRS, and whether there is any concrete proposal to converge or substantially converge the foreign financial reporting standards with IFRS.

30. On this basis, the Exchange has accepted that the financial statements and accountants' reports of overseas issuers can be prepared in conformity with the financial reporting standards set out in the table below subject to the prescribed scope therein:

Standard	Prescribed Scope
EU-IFRS	For issuers incorporated in a member state of the European Union.
U.S. GAAP	For issuers with, or seeking, a dual-primary or secondary listing in the U.S. and on the Exchange.

[12] A listed issuer must also prepare its interim report in accordance with the same accounting standards that it adopted in the preparation of its most recent published annual financial statements (paragraph 38 of MB Appendix D2 and note 5 to GEM Rule 18.55).

[13] Primary Listing: MB Rules 19.13 and 19.14 and GEM Rules 7.12 and 7.14 (accountants' reports) and MB Rule 19.25A and GEM Rule 24.18A (annual financial statements). Secondary Listing: MB Rules 19C.10D (accountants' reports) and 19C.23 (annual financial statements).

Standard	Prescribed Scope
Australian Accounting Standards	Only issuers with, or seeking, a primary listing in the same jurisdiction as the standard setter that have, or are seeking, a dual primary listing or secondary listing on the Exchange.
Generally Accepted Accounting Principles of Canada	
Accounting Principles Generally Accepted in Japan issued by the Accounting Standards Board of Japan	
Singapore Financial Reporting Standards	
UK Adopted International Accounting Standards	

31. An overseas issuer adopting a body of financial reporting standards other than HKFRS or IFRS for the preparation of its financial statements must include a reconciliation statement setting out the financial effect of any material differences between those financial statements and financial statements prepared using HKFRS or IFRS in its accountants' reports and annual/interim reports[14]. See Chapter 3.11 of the Guide for further details on the preparation of the reconciliation statement and the waiver requirement[15].

The use of U.S. GAAP for existing secondary listed issuers

32. Existing secondary listed issuers listed in the U.S. are allowed to use U.S. GAAP[16] will be able to continue to do so, but will be required to include a reconciliation statement in their annual financial statements starting from the first full financial year commencing on or after 1 January 2022 and in all subsequent financial statements (including interim financial statements[17]).

Auditing standards

33. The Listing Rules state that an accountants' report and annual financial statements of an overseas issuer must be audited to a standard comparable to that required by the Hong Kong Institute of Certified Public Accountants (**HKICPA**) or the International Auditing and Assurance Standards Board (**IAASB**)[18].

34. The Exchange is satisfied that the following seven sets of alternative standards are comparable to those required by HKICPA or the IAASB, and allows them to be used in the auditing of overseas issuers' financial statements:

    (i) Australian Auditing Standards;

14 Primary Listing: MB Rule 19.14 and GEM Rule 7.14 (accountants' reports) and MB Rule 19.25A and GEM Rule 24.18A (annual/interim financial statements). Secondary Listing: MB Rules 19C.10D (accountants' reports) and 19C.23 (annual/interim financial statements).

15 For automatic waivers and common waivers, please refer to MB Rule 19.58 (GEM Rule 24.25) (for issuers with, or seeking a dual primary listing) and MB Rule 19C.11B (for issuers with, or seeking a secondary listing) for details.

16 For the avoidance of doubt, overseas issuers with, or seeking, a dual primary listing that prepare their financial statements using U.S. GAAP are required to continue to comply with the requirement to prepare reconciliation statements for the annual and interim financial statements and accountants' report.

17 A secondary listed issuer listed in the U.S. is not required to prepare a reconciliation statement in respect of its U.S. GAAP quarterly financial statements which are published pursuant to overseas rules and regulations.

18 Primary Listing: MB Rule 19.12 and GEM Rule 7.17A (accountants' reports) and MB Rule 19.21 and GEM Rule 24.14 (annual financial statements). Secondary Listing: MB Rules 19C.10C (accountants' reports) and 19C.17 (annual financial statements).

(ii) The Generally Accepted Auditing Standards of Canada;

(iii) Professional auditing standards applicable in France in accordance with the French Commercial Code;

(iv) Italian Auditing Standards;

(v) Singapore Standards on Auditing;

(vi) International Standards on Auditing (UK); and

(vii) The U.S. Public Company Accounting Oversight Board auditing standards.

35. Overseas issuers seeking to adopt a body of financial reporting standards or auditing standards that is not covered by this letter should consult the Exchange at the earliest opportunity.

X. Taxation

36. If withholding tax on distributable entitlements or any other tax is payable by shareholders (e.g. capital gains, inheritance or gift taxes), an overseas issuer must bring this to the Exchange's attention at the earliest possible opportunity prior to listing. The overseas issuer must disclose in its listing document details of the stamp duty and tax payable by shareholders, and whether Hong Kong investors have any tax reporting obligations and related procedures.

XI. Recognition of overseas audit firms under the AFRCO

37. AFRC is Hong Kong's independent regulator of listed entity auditors. All audit firms intending to carry out a PIE Engagement are subject to a system of registration (for Hong Kong audit firms) and recognition (for non-Hong Kong audit firms[19]) as PIE Auditors.

38. Any overseas audit firm is required to be recognised by the AFRC before the overseas audit firm can (i) undertake (i.e. accept an appointment to carry out) any PIE Engagement; and (ii) carry out any PIE Engagement for an overseas issuer. Under the AFRCO, the Exchange needs to issue a statement of no objection ("**SNO**") before the AFRC considers an application of the overseas audit firm to be recognised as a Recognised PIE Auditor. The overseas audit firm must not accept an appointment for carrying out any PIE Engagement for an overseas issuer unless the application for recognition has been granted by the AFRC.

39. The overseas issuers are reminded that they should plan their applications ahead[20] and allow sufficient time to seek the SNO and obtain the AFRC's approval for recognition of a Recognised PIE Auditor. For further details on the recognition of overseas audit firms, please refer to the AFRC's website.

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 Division on a confidential basis for an interpretation of the Listing Rules, or this letter.

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19 Recognition of overseas audit firms does not apply to audit firms located in Mainland China. Under the AFRCO, the endorsed Mainland audit firms (for the PRC issuers only) will be recognised as a PIE Auditors without a recognition application being made to the AFRC.

20 It is the responsibility of the overseas issuer to submit the application for appointing an overseas audit firm for the PIE Engagement, together with a SNO issued by the Exchange. The AFRC considers the application of an overseas audit firm on a case-by-case basis.

Change of listing status from secondary listing to dual-primary or primary listing on the Main Board

1. Purpose

1.1 This letter provides guidance to Overseas Issuers[1] that have a secondary listing on the Exchange pursuant to Chapter 19C of the Listing Rules with regards to issues relating to:

(a) the migration of the majority of trading in their listed shares to the Exchange's markets under Listing Rule 19C.13 (**Migration**);

(b) voluntary conversion to dual-primary listing on the Exchange (**Primary Conversion**); and

(c) de-listing (voluntary or involuntary) of their shares or depositary receipts issued on their shares from the Recognised Stock Exchange[2] on which they are primary listed under Listing Rule 19C.13A (**Overseas De-listing**).

Any reference to shares in this letter shall include depositary receipts issued on such shares where applicable.

2. Relevant Listing Rules

2.1 Listing Rule 19C.13 states that if the majority of trading in an Overseas Issuer's listed shares migrates to the Exchange's markets on a permanent basis, the Exchange will regard the issuer as having a dual-primary listing and consequently Listing Rules 19C.11, 19C.11A, 19C.11B and 19C.11C (as applicable) will no longer apply to the Overseas Issuer. Listing Rules 19.02, 19.58 to 19.59 relating to the basis for waivers, modifications and exceptions and common waivers for Overseas Issuers may apply depending on the relevant facts and circumstances.

2.2 Note 1 to Listing Rule 19C.13 states that the majority of trading in an Overseas Issuer's listed shares is considered to have migrated to the Exchange's markets on a permanent basis if 55% or more of the total worldwide trading volume, by dollar value, of those shares (including the volume of trading in depositary receipts issued on those shares) over the Overseas Issuer's most recent financial year, takes place on the Exchange's markets.

[1] As defined in Chapter 1 of the Listing Rules.
[2] As defined in Chapter 1 of the Listing Rules.

2.3 Note 2 to Listing Rule 19C.13 provides such an Overseas Issuer (**Migration Issuer**) with a grace period of 12 months within which to comply with the applicable Listing Rules (**Migration Grace Period**).[3] The Migration Grace Period will end at midnight on the first anniversary of the date of the Exchange's written notice of its decision that the majority of trading in the listed shares has migrated permanently to the Exchange's markets (**Migration Exchange Notice**).

2.4 Listing Rule 19C.13A states that if an Overseas Issuer's shares or depositary receipts issued on its shares (as the case may be) cease to be listed on the Recognised Stock Exchange on which it is primary listed, the Exchange will regard the issuer as having a primary listing in Hong Kong and consequently Listing Rules 19C.11, 19C.11A, 19C.11B and 19C.11C (as applicable) will no longer apply to the issuer.

2.5 Listing Rule 2.04 states that the Exchange may waive, modify or not require compliance with the Listing Rules in individual cases (to suit the circumstances of a particular case), as a variety of circumstances may exist which require it to make ad hoc decisions.

3. Guidance

3.1 The Exchange will regard an Overseas Issuer as having (i) a dual-primary listing on the Exchange upon the expiry of Migration Grace Period or the effective date of Primary Conversion; and (ii) a primary listing on the Exchange upon the effective date of Overseas De-listing (**Change of Listing Status**).

A. General - Dis-application of exceptions, waivers and exemptions upon Change of Listing Status

3.2 Upon a Change of Listing Status, all exceptions, waivers and exemptions available to an Overseas Issuer on the basis of, or conditional upon, its secondary listing status will cease to apply[4] save as otherwise provided under the "Applicability of Listing Rules to transactions entered into before the Change of Listing Status" in the **Appendix I**. See also paragraphs 3.10, 3.17, 3.24 and 3.34 for the arrangements relating to the dis-application of the stock marker "S".

3.3 For those exceptions, waivers and exemptions available to an Overseas Issuer which were not expressly conditional on its secondary listing status (**Specific Waivers**), in general, they will continue to apply despite a Change of Listing Status. However, a change in the nature of a secondary listed Overseas Issuer's listing status due to Migration, Primary Conversion or Overseas De-listing may constitute a change in circumstances that may result in a prior specific waiver being no longer appropriate. Therefore, the Exchange may revisit any prior specific waiver granted to an Overseas Issuer which is not granted on the basis of, or conditional upon, its secondary listing status and has the right to withdraw a specific waiver under such circumstances pursuant to Listing Rule 2.04.

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[3] For the avoidance of doubt, the Migration Grace Period is conditional on the continued primary listing of the Overseas Issuer on the relevant Recognised Stock Exchange. If this condition is not fulfilled, the Overseas Issuer would be subject to the relevant guidance under the section headed "D. De-listing from a Recognised Stock Exchange of primary listing" in this guidance letter.

[4] This includes exceptions, waivers and exemptions to the Listing Rules set out in Listing Rules 19C.11, 19C.11A, 19C.11B and 19C.11C but subject to paragraph 3.3, excludes those exceptions, waivers and exemptions available to an Overseas Issuer which were not expressly conditional on its secondary listing status.

3.4 Accordingly, unless waivers (including any grace period) are granted in respect of specific Listing Rules (see paragraphs 3.7 to 3.8) and save as otherwise provided under "Applicability of Listing Rules to transactions entered into before the Change of Listing Status" in **Appendix I**, an Overseas Issuer will become subject to all Listing Rules applicable to a dual primary or primary listed issuer[5] immediately upon a Change of Listing Status, and must make arrangements at the earliest opportunity to ensure full compliance of applicable Listing Rules.

3.5 This means that upon a Change of Listing Status, an Overseas Issuer should observe the following:

(a) In relation to corporate governance requirements under the Listing Rules, for example, the establishment of an audit committee, an Overseas Issuer should ensure all changes to its corporate and organisational structure have been introduced to enable itself to be fully compliant with the relevant Listing Rules;

(b) In relation to other applicable Listing Rules, i.e. the compliance with which are usually event-driven and/ or time-based in nature (for example, (a) Model Code for Securities Transactions by Directors of Listed Issuers (Appendix C3 of the Listing Rules); (b) restriction on purchase of own shares; (c) notifiable transactions; and (d) connected transactions), an Overseas Issuer is expected to have put in place all necessary internal control systems upon a Change of Listing Status to monitor its ongoing compliance from time to time and, if applicable, carry out all such actions in accordance with the relevant Listing Rules when the situation requires.

Should an Overseas Issuer envisage any issues arising in connection with Migration, Primary Conversion or Overseas De-listing, it is expected to consult the Exchange as early as practicable.

3.6 For the avoidance of doubt, a Migration Issuer and a Conversion Issuer (as defined in paragraph 3.23) can continue to adopt a body of alternative financial reporting standards (as set out in Guidance Letter HKEX-GL111-22 - Guidance for Overseas Issuers) as the accounting standards used for the preparation of its financial statements provided that such Overseas Issuer maintains a primary listing in the relevant jurisdiction of the alternative overseas financial reporting standards[6].

Waiver applications (including applications for a grace period as a time-relief waiver)

3.7 If an Overseas Issuer believes it has grounds for certain exceptions, waivers or exemptions to continue after the Change of Listing Status or wishes to apply for a new waiver from strict compliance with any Listing Rules, it should submit an application(s) to the Exchange in accordance with the timing referred to in paragraphs 3.15(b), 3.23 and 3.33 or, if it is not possible, at the earliest opportunity.

3.8 The waiver application(s) under paragraphs 3.7 should contain sufficient information to demonstrate the basis for the Exchange to grant (or as the case may be, continue to grant) such waiver(s), including the reasons why any exception, waiver or exemption should apply (or as the case may be, continue to apply). The Exchange will make the assessment on a case-by-case basis and exercise its discretion as to whether to grant the waiver(s).

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5 This includes Listing Rules previously not applicable to the Overseas Issuers such as Listing Rules 6.12 to 6.15 in relation to withdrawal of listing, Listing Rules 19.09 to 19.61 in relation to additional requirements, modifications or exceptions which apply to an Overseas Issuer whose primary listing is on the Exchange (where applicable).

6 Only issuers incorporated in a member state of the European Union are allowed to adopt EU-IFRS.

Dis-application of stock marker "S" and the application of the stock maker "TP" in the stock short name

3.9 The purpose of the stock marker "S" in the stock short name of a secondary listed issuer is to provide sufficient notification to inform investors that the relevant issuer is not subject to the full extent of the Listing Rules due to its status as a secondary listed issuer.

3.10 Normally, the stock marker "S" should be retained until the Change of Listing Status, subject to the following sub-paragraphs:

(a) for Migration Issuers, the stock marker "S" will not be dis-applied until a Migration Issuer is able to comply with all relevant Listing Rules applicable to a dual primary listed issuer (except as otherwise provided under "Applicability of Listing Rules to transactions entered into before the Change of Listing Status" in **Appendix I**). The rationale is to provide an indication to investors that such Migration Issuer has yet to make all necessary arrangements to enable itself to fully comply with all relevant Listing Rules applicable to a dual primary listed issuer and remains to be regarded as a secondary listed issuer.

(b) for Conversion Issuers and De-listing Issuers (as defined in paragraph 3.33), the stock marker "S" in the stock short name will be dis-applied on the effective date of Primary Conversion or Overseas De-listing.

If any Overseas Issuer anticipates difficulty in complying fully with the applicable Listing Rules immediately upon the Change of Listing Status and would like to apply for a grace period as time-relief waiver, the Exchange will consider the application on a case-by-case basis. Grace period will only be granted under rare and exceptional circumstances based on compelling reasons so that the Overseas Issuer may make necessary arrangements during such period to enable itself to comply with the Listing Rules as soon as practicable. Please see paragraph 3.26 (for Conversion Issuer) and paragraph 3.39 (for De-listing Issuer) for details of the grace period.

Should any grace period be granted to a Conversion Issuer or a De-listing Issuer, the Exchange has the power to require the Conversion Issuer or De-listing Issuer to have a stock short name that ends with the stock marker "TP" when the Exchange considers necessary taking into account the nature and the materiality of the non-compliance with the Listing Rules covered by the grace period. The purpose of the stock marker "TP" is to inform investors that such Conversion Issuer or De-listing Issuer, while having been reclassified as having a dual primary or primary listing after the Primary Conversion or Overseas De-listing (as the case may be), is under transitional arrangements to enable itself to achieve full compliance with all applicable Listing Rules.

B. Migration of the majority of trading in an Overseas Issuer's shares to the Exchange's markets under Chapter 19C

Responsibility for monitoring

3.11 Subject to paragraph 3.12 below, all secondary listed Overseas Issuers should monitor their compliance with Listing Rule 19C.13 from the start of their first full financial year after listing on the Exchange.

3.12 Existing Overseas Issuers which are Greater China Issuers[7] and listed on the Exchange's markets under Chapter 19C of the Listing Rules on or before 31 December 2021 have been subject to Listing Rule 19C.13 since their listing. For Overseas Issuers (i) that are Non-Greater China Issuers[8] that secondary listed through Chapter 19C of the Listing Rules; or (ii) listed on the Exchange's markets under the route to secondary listing on the Exchange in accordance with the requirement set out in section 5 of the JPS[9]on or before 31 December 2021, they should monitor their compliance with Listing Rule 19C.13 from the start of their first full financial year that commences on or after the relevant amendments to the Listing Rules[10] come into effect (that is, 1 January 2022), for example, where such existing secondary listed Overseas Issuer has its financial year beginning from 1 January, it should monitor its compliance with Listing Rule 19C.13 from 1 January 2022.

Method of calculation of trading migration test

3.13 The following method is to be used to calculate the percentage of trading volume by dollar value on the Exchange's markets for the purpose of Listing Rule 19C.13:

$$= \frac{\text{Total trading volume in Hong Kong by dollar value over a full financial year}}{\text{Total worldwide trading volume by dollar value over a full financial year}} \times 100\%$$

3.14 For the purpose of calculating "dollar value" and the exchange rate to be adopted, data published by a reputable independent third party market data provider is expected to be used.

Notification to the Exchange

3.15 Subject to paragraph 3.11 above, a secondary listed Overseas Issuer should notify the Exchange in writing:

(a) within 5 business days of the end of the third quarter of its financial year, as to whether or not the trading volume of its shares, by dollar value, in Hong Kong has exceeded 50% of the total worldwide trading volume, by dollar value, of those shares (including the volume of trading in depositary receipts issued on those shares) based on the trading volume over that nine-month period and the respective total trading volume of its shares, by dollar value, in Hong Kong and the total worldwide trading volume over that period; and

7 As defined in Chapter 1 in the Listing Rules.
8 As defined in Chapter 1 in the Listing Rules.
9 The "Joint policy statement regarding the listing of overseas companies" first published jointly by the Exchange and the SFC in 2007, updated on 27 September 2013 and on 30 April 2018 and was withdrawn on 31 December 2021.
10 Certain amendments to the Listing Rules following the Exchange's consultation on the Listing Regime for Overseas Issuers have become effective since 1 January 2022.

(b) within 5 business days of the end of its financial year, as to whether or not the trading volume of its shares, by dollar value, in Hong Kong has exceeded 55% of the total worldwide trading volume, by dollar value, of those shares (including the volume of trading in depositary receipts issued on those shares) based on the trading volume over that financial year and the respective total trading volume of its shares, by dollar value, in Hong Kong and the total worldwide trading volume over that year. The notification to the Exchange shall be accompanied by waiver application (if any) under paragraph 3.7.

3.16 If the notification to the Exchange required by paragraph 3.15(a) above states that the relevant trading volume in the Overseas Issuer's shares has exceeded the threshold set out in that paragraph, the Overseas Issuer should begin its assessment of the impact to it of the dis-application of exceptions, waivers and exemptions due to the application of Listing Rule 19C.13 and the potential withdrawal of specific waivers granted by the Exchange, so that it is in a position to publish the announcement required by paragraph 3.20 below at the relevant time.

3.17 The Exchange will consider the notification made to it by an Overseas Issuer under paragraph 3.15(b) and may require additional information from the Overseas Issuer. Following its review of the information, the Exchange will issue a Migration Exchange Notice to the Overseas Issuer if it decides that the majority of trading in the listed shares in such Overseas Issuer has migrated permanently to the Exchange's markets under Listing Rule 19C.13 and it will regard such Migration Issuer as having a dual-primary (rather than secondary) listing status on the Exchange upon the expiry of the Migration Grace Period. The Migration Exchange Notice will also inform the Migration Issuer that the stock marker "S" in the stock short name will be dis-applied only when such Migration Issuer is able to fully comply with all the relevant Listing Rules applicable to a dual primary listed issuer[11]. In the event a Migration Issuer is unable to implement all necessary changes to its corporate and organisational structure in order to comply with the corporate government requirements in the Listing Rules (e.g. Rule 3.21 and Rule 3.23 relating to the establishment of the audit committee) and/ or put in place an internal control system to enable itself to fully comply with an applicable Listing Rule upon the expiration of the Migration Grace Period, the stock marker "S" shall remain in the stock short name and can only be removed after all rectification measures have been carried out and the Migration Issuer is fully compliant with all applicable Listing Rules. Besides, the Exchange may also consider pursuing disciplinary actions in respect of the non-compliance with the relevant Listing Rules.

3.18 For the avoidance of doubt, notwithstanding the receipt of the Migration Exchange Notice, save as otherwise provided under "Applicability of Listing Rules to transactions entered into before the Change of Listing Status" in **Appendix I**, a Migration Issuer will continue to be entitled to the exceptions, waivers and exemptions granted or applicable to it as a secondary listed Overseas Issuer on the Exchange before the expiry of the Migration Grace Period.

Update report to the Exchange

3.19 During the Migration Grace Period, the Migration Issuer should provide the Exchange with an update report, on a monthly basis, on its progress towards compliance with the Listing Rules that will apply to it at the end of the Migration Grace Period.

[11] Refer to paragraph 3.5 which sets out the expectation on the Migration Issuer relating to compliance with the applicable Listing Rules upon the expiry of the Migration Grace Period.

Migration Issuer's announcements

3.20 As soon as practicable after receiving a Migration Exchange Notice under paragraph 3.17 above, the Migration Issuer must publish an announcement stating that the majority of the trading of its shares has migrated to the Exchange's markets on a permanent basis under Listing Rule 19C.13, including:

(a) details of the consequences of the Migration Exchange Notice;

(b) details of the Migration Grace Period;

(c) its obligation to make necessary arrangements to enable it to fully comply with applicable Listing Rules upon the end of the Migration Grace Period; the potential consequences of its failure to comply with this obligation; the potential consequences of the withdrawal of any specific waivers from strict compliance with any Listing Rules granted by the Exchange on an individual basis upon the end of the Migration Grace Period;

(d) where applicable, the Migration Issuer's intention to apply to the Exchange for certain exception(s), waiver(s) and / or exemption(s) to continue after the Migration Grace Period ends and that the Exchange may or may not grant such exception(s), waiver(s) or exemption(s);

(e) the potential impact to shareholders and potential investors of any transitional measures to be put in place during the Migration Grace Period; and

(f) the stock marker "S" continues to apply until the expiry of the Migration Grace Period provided that such Migration Issuer is in compliance with all the relevant Listing Rules applicable to a dual primary listed issuer by then.

3.21 Upon the expiration of the Migration Grace Period, the Migration Issuer should publish an announcement which must state:

(a) the Migration Grace Period has ended;

(b) where applicable, any continuing transaction that will continue to be exempted pursuant to Note 3 to Listing Rule 19C.13 and the details of the relevant continuing transaction(s);

(c) its obligations to comply with all applicable Listing Rules as a dual- primary listed Overseas Issuer on the Exchange following the expiry of the Migration Grace Period; the potential consequences of its failure to comply with these obligations following the expiry of the Migration Grace Period; and the consequences of the withdrawal of any specific waiver from strict compliance with any Listing Rules granted by the Exchange on an individual basis;

(d) where applicable, details of any waiver(s) from strict compliance with any Listing Rules, including conditions and bases for granting such waiver(s);

(e) (*in the event that the Migration Issuer has already introduced all changes to its corporate and organisational structure to comply with all corporate governance requirements under the Listing Rules applicable to a dual primary listed issuer and put in place an internal control system to ensure ongoing compliance with other applicable Listing Rules*) the dis- application of the stock marker "S"; and

(f) *(in the event that the Migration Issuer has not yet introduced all changes to its corporate and organisational structure to comply with all corporate governance requirements under the Listing Rules applicable to a dual primary listed issuer and/ or put in place an internal control system to ensure ongoing compliance with other applicable Listing Rules*) the stock maker "S" continues to apply; details of such breaches of Listing Rules and the progress of the rectification and the amount of time needed for full compliance with the specific Listing Rules[12].

Failure to comply with applicable Listing Rule(s)

3.22 In the event that a Migration Issuer is unable to fully comply with an applicable Listing Rule upon the expiration of the Migration Grace Period (save for any continuing transaction that will continue to be exempted pursuant to Note 3 to Listing Rule 19C.13), the Exchange may, on a case by case basis, exercise its discretion to extend a grace period, suspend trading of such Migration Issuer's shares or impose other measures as it considers necessary for the protection of the investors and the maintenance of an orderly market. If any extended grace period has been granted under a time-relief waiver, the Overseas Issue shall publish an announcement upon the grant and the expiry of such extended grace period, informing the shareholders and the investors of the status of compliance.

C. Primary Conversion to dual-primary listing

Application to the Exchange

3.23 An Overseas Issuer seeking a Primary Conversion (**Conversion Issuer**) should apply to the Exchange in writing with regards to its plan to carry out a Primary Conversion (**Primary Conversion Application**) together with any waiver application(s) under paragraph 3.7, or if not possible, at the earliest opportunity but not later than the effective date of the Primary Conversion. The Primary Conversion Application should contain:

(a) the expected date on which the Primary Conversion will become effective, at which time the Conversion Issuer must be able to comply with all the relevant Listing Rules applicable to a dual-primary listed issuer[13]; and

(b) the detailed plan and arrangements on how it will comply with the applicable Listing Rules. In particular, where the Conversion Issuer was previously granted waivers by virtue of its secondary listing status but going forward it would not apply for such waivers upon the Primary Conversion, it shall set out clearly the arrangements in place to enable its full compliance with these rules.

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12 Upon the rectification measures being put in place such that the Overseas Issuer is fully compliant with the specific Listing Rules, the Overseas Issuer shall publish an announcement updating the shareholders and investors of its latest status of compliance.

13 Refer to paragraph 3.5 which sets out the expectation on the Conversion Issuer relating to compliance with the applicable Listing Rules upon the Primary Conversion becoming effective.

3.24 The Exchange will consider the information provided in the Primary Conversion Application and may require additional information. Following its review of the information, the Exchange will issue an acknowledgement to the Conversion Issuer (**Primary Conversion Exchange Acknowledgment**) which will (i) inform the Conversion Issuer on the dis-application of the stock marker "S" in the stock short name on the effective date of the Primary Conversion; and (ii) remind the Conversion Issuer that upon the Primary Conversion, it will regard such Conversion Issuer as having a dual-primary (rather than secondary) listing status on the Exchange.

3.25 For the avoidance of doubt, notwithstanding the submission of the Primary Conversion Application or receipt of the Primary Conversion Exchange Acknowledgment, a Conversion Issuer will continue to be entitled to the exception(s), waiver(s) and exemption(s) granted or applicable to it as a secondary listed Overseas Issuer on the Exchange before the Primary Conversion becomes effective provided that it remains primary listed on a Recognised Stock Exchange.

Grace period

3.26 In general, a Conversion Issuer is expected to submit a Primary Conversion Application to the Exchange only when it believes that it would be in a position to be able to fully comply with the applicable Listing Rules upon the Primary Conversion becoming effective. Therefore, a grace period will not normally be granted unless it is justified by a compelling reason. An application for a grace period will be considered on a case-by-case basis (for example, on the basis that certain changes to the corporate structure for full compliance with the corporate governance requirements under the Listing Rules upon Primary Conversion may require shareholders' approval and the Conversion Issuer can demonstrate to the Exchange that (i) there is imminent price sensitivity concern arising from issuing the circular and notice of meeting prior to the Conversion Issuer's announcements (see paragraph 3.29) in order to comply with the local requirement on notice period and obtain shareholders' approval before the effective date of Primary Conversion; and (ii) delaying the effective date of the Primary Conversion is not practicable).

3.27 Should any grace period be granted on the basis of the specific circumstances of the Conversion Issuer, the Exchange has the power to require the Conversion Issuer to have its stock short name end with the stock marker "TP" upon the Primary Conversion becoming effective when the Exchange considers necessary taking into account the nature and the materiality of the non-compliance with the Listing Rules covered by the grace period.

3.28 Any grace period granted under a time-relief waiver for a Conversion Issuer in exceptional circumstances will commence from the time of Primary Conversion. The length of the grace period for each Listing Rule under the time-relief waiver will be assessed with reference to the individual facts and circumstances of the Conversion Issuer, including but not limited to (a) the expected date of the Primary Conversion; and (b) the amount of time reasonably needed for the Conversion Issuer to fully comply with the specific Listing Rules.

Conversion Issuer's announcements

3.29 As soon as practicable after receiving a Primary Conversion Exchange Acknowledgment, the Conversion Issuer must publish an announcement stating the following:

(a) the intention and / or reasons for the Primary Conversion;

(b) the expected or estimated date of the Primary Conversion (i.e. the date on which the Conversion Issuer will be able to comply with all the relevant Listing Rules applicable to a dual-primary listed issuer unless otherwise waived or exempted);

(c) its obligations to make necessary arrangements to enable it to comply with all applicable Listing Rules following the Primary Conversion; the potential consequences of its failure to comply with these obligations following the Primary Conversion; and the potential consequences of the withdrawal of any specific waiver from strict compliance with any Listing Rules granted by the Exchange on an individual basis upon Primary Conversion becoming effective;

(d) where applicable, any application(s) made to the Exchange for exception(s), waiver(s) or exemption(s) from strict compliance with any Listing Rule following the Primary Conversion and that the Exchange may or may not grant such waiver(s); and

(e) the potential impact to shareholders and potential investors of any transitional measures to be put in place before the Primary Conversion becomes effective.

3.30 On or before the effective date of its Primary Conversion, the Conversion Issuer should publish an announcement which must state:

(a) the Primary Conversion has become effective (or, as the case may be, the date on which the Primary Conversion is expected to become effective);

(b) its obligations to comply with all applicable Listing Rules as a dual- primary listed Overseas Issuer on the Exchange following the Primary Conversion; the potential consequences of its failure to comply with these obligations following the Primary Conversion; and the

consequences of the withdrawal of any waiver from strict compliance with any Listing Rules granted by the Exchange on an individual basis;

(c) where applicable, details of any exception(s), waiver(s) or exemption(s) from strict compliance with any Listing Rules granted, including conditions and bases for granting such exception(s), waiver(s) or exemption(s);

(d) the dis-application of the stock marker “S”;

(e) *(if the Conversion Issuer is granted any grace period)* conditions and bases for granting a grace period including details of the Listing Rules in respect of which a grace period has been granted to the Conversion Issuer and the length of the grace period within which the Conversion Issuer is expected to make necessary arrangements to enable itself to comply with the applicable Listing Rules and the progress of the rectification; and

(f) (*if requested by the Exchange*) the application of the stock marker “TP”.

3.31 If any grace period has been granted under a time-relief waiver as described in paragraphs 3.10(b) and 3.26, the Conversion Issuer should publish an announcement upon expiration of all such grace periods informing the shareholders and the investors of its status of compliance.

Failure to comply with applicable Listing Rule(s)

3.32 In the event a Conversion Issuer is unable to fully comply with an applicable Listing Rule in time (where no waiver has been granted by the Exchange) upon its Primary Conversion, the Exchange may request the Conversion Issuer to delay the effective date of the Primary Conversion, in which case an announcement should be made by the Conversion Issuer on a timely basis. In the case where a grace period is granted pursuant to paragraphs 3.10(b) and 3.26, if the Conversion Issuer is still unable to fully comply with an applicable Listing Rule upon the expiry of the grace period, the Exchange may, on a case by case basis, exercise its discretion to extend the grace period, suspend trading of such Conversion Issuer's shares and/ or impose other measures as it considers necessary for the protection of investors and the maintenance of an orderly market. If any extended grace period has been granted under a time-relief waiver, the Overseas Issuer shall publish an announcement upon the grant and expiry of such extended grace period, informing the shareholders and the investors of its status of compliance.

D. De-listing from a Recognised Stock Exchange of primary listing

Notification to the Exchange

3.33 An Overseas Issuer that starts to plan a voluntary de-listing, or that reasonably expects it may be de-listed involuntarily, from its Recognised Stock Exchange of primary listing (**De-listing Issuer**), should notify the Exchange of this possibility in writing (stating in the notification whether it is a voluntary de-listing, or it expects to be de-listed involuntarily and the bases for such expectation) as soon as practicable to give the Exchange early notice[14] and submit any waiver application(s) under paragraph 3.7 or if not possible, at the earliest opportunity but not later than the effective date of the Overseas-De-listing. The De-listing Issuer Notification should contain:

(a) the expected date on which the Overseas De-listing will become effective, following which the De-listing Issuer must be able to comply with all the relevant Listing Rules applicable to a primary listed issuer[15]; and

(b) the detailed plan and arrangements on how it will comply with the applicable rules. In particular, where the De-listing Issuer was previously granted waivers by virtue of its secondary listing status but going forward it would not apply for such waivers upon the Overseas De-listing, it shall set out clearly the arrangements in place to enable its full compliance with these rules.

[14] For a secondary listed Overseas Issuer with primary listing on an exchange in the United States, such notification should be submitted to the Exchange as soon as practicable and before the first filing of Form 8K (domestic issuer) / 6K (foreign private issuer) with the US Securities and Exchange Commission which formally announces the potential de-listing.

[15] Refer to paragraph 3.5 which sets out the expectation on the De-listing Issuer relating to compliance with the applicable Listing Rules upon the Overseas De-listing becoming effective.

3.34 The Exchange will consider the information provided in the De-listing Issuer Notification and may require additional information. Following its review of the information, the Exchange will issue an acknowledgment to the De-listing Issuer (**Overseas De-listing Exchange Acknowledgment**) which will (i) inform the De-listing Issuer on the dis-application of the stock marker "S" on the effective date of the Overseas De-listing; and (ii) remind the De-listing Issuer that upon the Overseas De-listing, it will regard such De-listing Issuer as having a primary (rather than dual-primary or secondary) listing status on the Exchange.

3.35 For a De-listing Issuer seeking a voluntary delisting from its Recognised Stock Exchange of primary listing, the Exchange would like to emphasise that the De-listing Issuer is expected to submit the De-listing Issuer Notification only if it considers itself being able to fully comply with the applicable Listing Rules upon the Overseas De-listing becoming effective. See paragraphs 3.10(b) and 3.39 for the Exchange's approach to an application for a grace period.

3.36 For the avoidance of doubt, notwithstanding the submission of the De-listing Issuer Notification or receipt of the Overseas De-listing Exchange Acknowledgment, a De-listing Issuer will continue to be entitled to the exceptions, waivers or exemptions granted or applicable to it as a secondary listed Overseas Issuer on the Exchange before its Overseas De-listing becomes effective provided that it remains primary listed on a Recognised Stock Exchange.

Grace period in respect of financial reporting standards

3.37 Listing Rules 19.13 and 19.25A provide that accountants' reports and annual accounts are required to conform to financial reporting standards acceptable to the Exchange, which will normally be HKFRS or IFRS.

3.38 As set out in Note 4 to Rule 19C.23, where the annual accounts of a De-listing Issuer have been drawn up in conformity with alternative overseas financial reporting standards in accordance with Listing Rule 19C.23 (other than issuers incorporated in an EU member state which adopted EU-IFRS), it shall adopt HKFRS or IFRS with a grace period of one year from its Overseas De-listing to make the necessary amendments to its internal controls to facilitate the change upon Overseas De-listing. This means that any interim and annual financial statements falling due, and published, after the first anniversary of the Overseas De-listing shall be prepared in accordance with either HKFRS or IFRS. This grace period is automatic and no application to the Exchange is required.

Grace period in respect of other Listing Rules

3.39 As a general principle, a De-listing Issuer is expected to comply with all the Listing Rules as applicable to other primary listed Overseas Issuers following its Overseas De-listing. This is crucial as such De-listing Issuer will no longer be subject to the rules and regulations of the Recognised Stock Exchange on which it was originally primary listed. Except for the grace period available to such issuers in respect of financial reporting standards requirements set out in paragraph 3.38 above, the Exchange believes that a grace period will be considered only in limited circumstances. We will consider applications for a grace period in exceptional circumstances on a case-by-case basis (for example, (1) on the basis that certain changes to the corporate structure for full compliance with the corporate governance requirements under the Listing Rules upon voluntary De-listing may require shareholders' approval and the De-listing Issuer can demonstrate to the Exchange that (i) there is imminent price sensitivity concern arising from issuing the circular and notice of meeting prior to the De-listing Issuer's announcements (see paragraph 3.42) in order to comply with the local requirement on notice period and obtain shareholders' approval before the effective date of Overseas De-listing; and (ii) delaying the effective date of the Overseas De-listing is not practicable; or (2) the De-listing Issuer was requested to delist from the Recognised Stock Exchange of primary listing by the overseas regulator at short notice).

3.40 In general, the Exchange will not normally grant any grace period to De-listing Issuers for compliance in respect of those Listing Rules that have not been previously waived for issuers having a sole primary listing on the Exchange. These Listing Rules generally concern key requirements that, the Exchange considers, must be fully complied with for the purpose of primary listing, such as a majority of the Listing Rules on notifiable transactions and connected transactions.[16]

3.41 Any grace period granted under a time-relief waiver for a De-listing Issuer in exceptional circumstances will commence from the time of the Overseas De- listing. The length of the grace period for each Listing Rule under the time- relief waiver will be assessed with reference to the individual facts and circumstances of the De-listing Issuer, including but not limited to (a) the expected date of the Overseas De-listing; and (b) the amount of time reasonably needed for such De-listing Issuer to fully comply with the specific Listing Rules. Should any grace period be granted on the basis of the specific circumstances of the De-listing Issuer, the Exchange has the power to require the De-listing Issuer to have its stock short name end with "TP" upon the Overseas De-listing becoming effective when the Exchange considers necessary taking into account the nature and the materiality of the non- compliance with the Listing Rules covered by the grace period.

[16] Under exceptional circumstances (e.g. a transaction entered into but not yet completed before the effective date of the Overseas De-listing due to circumstances beyond the control of the De-listing Issuer (for example, there is a condition precedent regarding obtaining regulatory approvals or the counter-parties to the transaction have requested an extension of the long-stop date for completion), the Exchange may exercise its discretion to waive the shareholders' approval requirement but the Overseas Issuer will be expected to comply with the other requirements applicable to such transaction, including, where applicable, circular, independent financial advisor, accountants' report and annual reporting requirements.

De-listing Issuer's announcements

3.42 A De-listing Issuer must announce its forthcoming Overseas De-listing in accordance with its general obligation of disclosure under Listing Rule 13.09 and no later than the announcement of this information on its Recognised Stock Exchange of primary listing.[17] This announcement must state:

(a) the intention and / or reasons for the Overseas De-listing;

(b) the expected or estimated date of the Overseas De-listing (for voluntary De-listing Issuers, the date on which the voluntary De-listing Issuer will be able to comply with all the relevant Listing Rules applicable to a primary listed issuer unless otherwise waived or exempted; for involuntary De-listing Issuers, the date of which its listing status would be cancelled by the overseas regulator and it becomes a primary listed issuer on the Exchange);

(c) its obligations to make necessary arrangements to enable it to comply with all applicable Listing Rules following the Overseas De-listing; the potential consequences of its failure to comply with these obligations following the Overseas De-listing; and the potential consequences of the withdrawal of any specific waiver from strict compliance with any Listing Rules granted by the Exchange on an individual basis upon the Overseas De-listing becoming effective;

(d) where applicable, any application(s) made to the Exchange for exception(s),waiver(s) and exemption(s) from strict compliance with any Listing Rule following the Overseas De-listing and that the Exchange may or may not grant such exception(s), waiver(s) and exemption(s); and

(e) the potential impact to shareholders and potential investors of any transitional measures to be put in place before the Overseas De-listing becomes effective.

3.43 On or before the effective date of its Overseas De-listing, the De-listing Issuer should publish an announcement which must state:

(a) the Overseas De-listing has become effective (or, as the case may be, the date on which the Overseas De-listing is expected to become effective);

(b) its obligations to comply with all applicable Listing Rules as a primary listed Overseas Issuer on the Exchange following the Overseas De- listing; the potential consequences of its failure to comply with these obligations following the Overseas De-listing; and the consequences of the withdrawal of any specific waiver from strict compliance with any Listing Rules granted by the Exchange on an individual basis;

(c) *(for involuntary De-listing Issuer)* where applicable, any continuing transaction that will continue to be exempted pursuant to this guidance letter (see paragraph 1.1 of **Appendix I**) and the details of the relevant continuing transaction(s);

17 For a secondary listed Overseas Issuer with primary listing on an exchange in the United States, this refers to no later than the first filing of the Form 8K (domestic issuer) / 6K (foreign private issuer) with the US Securities and Exchange Commission which formally announces the potential de-listing.

(d) where applicable, details of any waiver(s) from strict compliance with any Listing Rules, including conditions and bases for granting such waiver(s);

(e) where applicable, the procedures for converting depositary receipts/ shares originally traded on its overseas exchange of primary listing to ordinary shares trading in Hong Kong;

(f) the dis-application of the stock marker "S";

(g) *(if the De-listing Issuer is granted any grace period)* conditions and bases for granting grace period including details of the Listing Rules in respect of which a grace period has been granted to the De-listing Issuer and the length of the grace period within which the De-listing Issuer is expected to make necessary arrangements to enable itself to comply with the applicable Listing Rules and the progress of the rectification; and

(h) (*if requested by the Exchange*) the application of the stock marker "TP".

3.44 If any grace period has been granted under a time-relief waiver as described in paragraph 3.39, the De-listing Issuer should publish an announcement upon the expiry of all such grace periods, informing the shareholders and the investors of the status of compliance.

Failure to comply with the applicable Listing Rule(s)

3.45 In the event a voluntary De-listing Issuer is unable to fully comply with an applicable Listing Rule in time (where no waiver has been granted by the Exchange) before its Overseas De-listing, the Exchange may request the voluntary De-listing Issuer to delay the effective date of the voluntary Overseas De-listing, in which case an announcement should be made by the voluntary De-listing Issuer on a timely basis.

3.46 In the event an involuntary De-listing Issuer is unable to fully comply with an applicable Listing Rule upon the later of (i) its Overseas De-listing or (ii) the end of the grace period granted under any time-relief waiver (if any), the Exchange may, on a case by case basis, exercise its discretion to extend the grace period (if applicable), suspend trading of such De-listing Issuer's shares or impose other measures as it considers necessary for the protection of investors and the maintenance of an orderly market. If any extended grace period has been granted under a time-relief waiver, the Overseas Issuer shall publish an announcement upon the grant and expiry of such extended grace period, informing the shareholders and the investors of its status of compliance.

E. WVR and VIE structures

3.47 Chapter 2.2 of the Guide for New Listing Applicants (the **Guide**) allows Grandfathered Greater China Issuers and Non-Greater China Issuers meeting specified conditions to secondary list or dual primary list in Hong Kong with Non-compliant[18] WVR Structures[19] and/or variable interest entity structures (**VIE structure**), if any. Where these issuers have Non-Compliant WVR Structures, they must also demonstrate that they are "Innovative Companies".

[18] "Non-compliant" in paragraphs 3.47 and 3.48 means non-compliance with the requirements concerning WVR Structures and VIE structures under the Listing Rules and Chapter 2.2 of the Guide.

[19] As defined in Listing Rule 8A.02.

3.48 For the avoidance of doubt, a Grandfathered Greater China Issuer or a Non- Greater China Issuer secondary listed in Hong Kong is allowed to retain its Non-compliant WVR and/ or VIE structures (in effect at the time of its listing in Hong Kong) if it becomes primary listed in Hong Kong as a result of Migration, Overseas De-listing or Primary Conversion.

3.49 Please refer to **Appendix II** for a summary of the requirements for a Change of Listing Status under the Listing Rules.

Appendix I

Applicability of Listing Rules to transactions entered into before the Change of Listing Status

1.1 Overseas Issuers may have transactions in place with third parties that they entered into as a secondary listed issuer on the basis that the Listing Rules on notifiable and/ or connected transactions did not apply. To prevent undue disruption to the ongoing business activities of a Migration Issuer or an involuntary De-listing Issuer following Migration or involuntary Overseas De- listing, the Exchange is prepared to allow exemptions on the bases set out in this paragraph.

Continuing transaction

Subject to paragraph 1.2 below, in the event that a Migration Issuer or an involuntary De-listing Issuer has entered into a continuing transaction:

(i) before the beginning of the Migration Grace Period; or

(ii) before the submission of the De-listing Issuer Notification for involuntary Overseas De-listing,

but the transaction is expected to continue after the expiry of the Migration Grace Period or the involuntary Overseas De-listing becomes effective (as the case may be), save for the requirement for disclosing the details of the transaction in an announcement issued pursuant to paragraph 3.21 (for Migration Issuer) or paragraph 3.43 (for involuntary De-listing Issuer), the Overseas Issuer will be exempted from the applicable notifiable and connected transaction rules set out in the Listing Rules in respect of the transaction, for a period of three years from the date of the Migration Exchange Notice[20] or the date of the De-listing Issuer Notification (as applicable).

However, if such transaction is subsequently amended or renewed before the expiry of the three-year period, the Migration Issuer or the involuntary De-listing Issuer must comply with the relevant requirements under the Listing Rules at such time.

In respect of involuntary Overseas De-listing, the Exchange retains the discretion to modify, or not to allow, the exemption described in this paragraph if the involuntary De-listing Issuer has failed to notify the Exchange of the anticipated Overseas De-listing on a timely basis in accordance with paragraph
3.33 of this letter.

[20] See Note 3 to Listing Rule 19C.13.

1.2 For the avoidance of doubt, the arrangements described in paragraph 1.1 above do not apply to a continuing transaction that is entered into by a Migration Issuer or an involuntary De-listing Issuer at the time set out below:

(i) during a Migration Grace Period; or

(ii) after the submission of the De-listing Issuer Notification for Overseas De- listing

and the transaction is expected to continue after the expiry of the Migration Grace Period or the Overseas De-listing becomes effective (as the case may be).

The arrangements described in paragraph 1.1 above also do not apply to any continuing transaction of a Conversion Issuer or voluntary De-listing Issuer that remains subsisting as at the date of the Primary Conversion Application or De- listing Issuer Notification and such transaction is expected to continue after the Primary Conversion or Overseas De-listing becomes effective (as the case may be).

One-off transaction

1.3 In the event that a Migration Issuer, a Conversion Issuer or a De-listing Issuer entered into a one-off transaction:

(i) before the expiry of the Migration Grace Period;

(ii) before the Primary Conversion becomes effective; or

(iii) before the Overseas De-listing (whether it concerns voluntary or involuntary Overseas De-listing) becomes effective;

but the transaction is expected to be completed thereafter, where such transaction would have been subject to the requirement to issue an announcement and a circular and/or seek shareholders' approval under the Listing Rules if such Migration Issuer or Conversion Issuer or De-listing Issuer were a primary listed issuer at the time when the transaction was entered into, the issuer should consult the Exchange at the earliest opportunity on the applicability of the Listing Rules to the transaction.

In general, the Overseas Issuer is required to issue an announcement of such one-off transaction to keep the market informed on a timely basis, providing details of the transaction[21].

[21] For the avoidance of doubt, the Overseas Issuers also need to publish an announcement of continuing transactions providing details of the transactions in the manner described in paragraph 1.1.

Notwithstanding its secondary-listing status at the time the transaction was entered into, normally, the Exchange would require the Overseas Issuer to make the transaction conditional on the issue of a circular and/or shareholders' approval (where applicable) if, at the time of entering into the transaction, it is aware of the imminent change of listing status (e.g. because the transaction is entered into shortly before or after the Migration Exchange Notice, the Primary Conversion Application or the De-listing Issuer Notification) and that the transaction is expected to be completed thereafter. Under Listing Rule 2.04, the Exchange has the power to waive, modify or not require compliance with the Listing Rules or impose additional requirements where it considers necessary. Below is a list of non-exhaustive factors that may be taken into consideration:

(i) the extent to which the change of listing status is within the issuer's control;

(ii) the materiality of the transaction (for example, whether it would have involved the issue of securities or have constituted a very substantial acquisition under Chapter 14 of the Listing Rules); and

(iii) the length of the period between the time at which the terms of the transaction are finalised and each of the dates of the Migration Exchange Notice, the Primary Conversion Application or the De-listing Issuer Notification and the effective date of the change of listing status.

1.4 Please see the table below for the summary of the Applicability of Listing Rules to transactions entered into before the Change of Listing Status.

Summary of the applicability of Listing Rules to transactions entered into before the Change of Listing Status

	Nature of transaction	**Required level of compliance with Listing Rules**
Migration of trading to the Exchange's markets	One-off transaction ▪ entered into before the expiry of the Migration Grace Period ▪ the transaction is expected to be completed after the Migration Grace Period ▪ such transaction would have been subject to the requirement to issue an announcement and a circular and/or obtain shareholders' approval under the Listing Rules if such Migration Issuer were a primary listed issuer at the time when the transaction was entered into (see paragraph 1.3)	Required to make an announcement of the transaction to keep the market informed on a timely basis, providing details of the transaction. Normally expected to make the transaction conditional on the issue of a circular and/or shareholders' approval (as the case may be) if the Migration Issuer is aware of the imminent Change of Listing Status at the time of entering into the transaction.
	Continuing transaction ▪ entered into before the beginning of the Migration Grace Period ▪ the transaction is expected to continue after the expiry of the Migration Grace Period (see paragraph 1.1)	Exempted from the applicable notifiable and connected transaction rules set out in the Listing Rules for a period of three years from the date of the Migration Exchange Notice. The continuing transaction must be disclosed in the Migration Issuer's announcement providing details of the transaction (see paragraph 3.21 of this letter). However, if such transaction is subsequently amended or renewed before the expiry of the three-year period, the Migration Issuer must comply with the relevant requirements under the Listing Rules at such time.

	Nature of transaction	Required level of compliance with Listing Rules
	Continuing transaction ▪ entered into during the Migration Grace Period ▪ the transaction is expected to continue after the Migration Grace Period (see paragraph 1.2)	Full compliance
Primary Conversion	One-off transaction ▪ entered into before the Primary Conversion becomes effective ▪ the transaction is expected to be completed after the Primary Conversion becomes effective ▪ such transaction would have been subject to the requirement to issue an announcement and a circular and/or obtain shareholders' approval under the Listing Rules if such Conversion Issuer were a primary listed issuer at the time when the transaction was entered into (see paragraph 1.3)	Required to make an announcement of the transaction to keep the market informed on a timely basis, providing details of the transaction. Normally expected to make the transaction conditional on the issue of a circular and/or shareholders' approval (as the case may be) if the Conversion Issuer is aware of the imminent Change of Listing Status at the time of entering into the transaction.

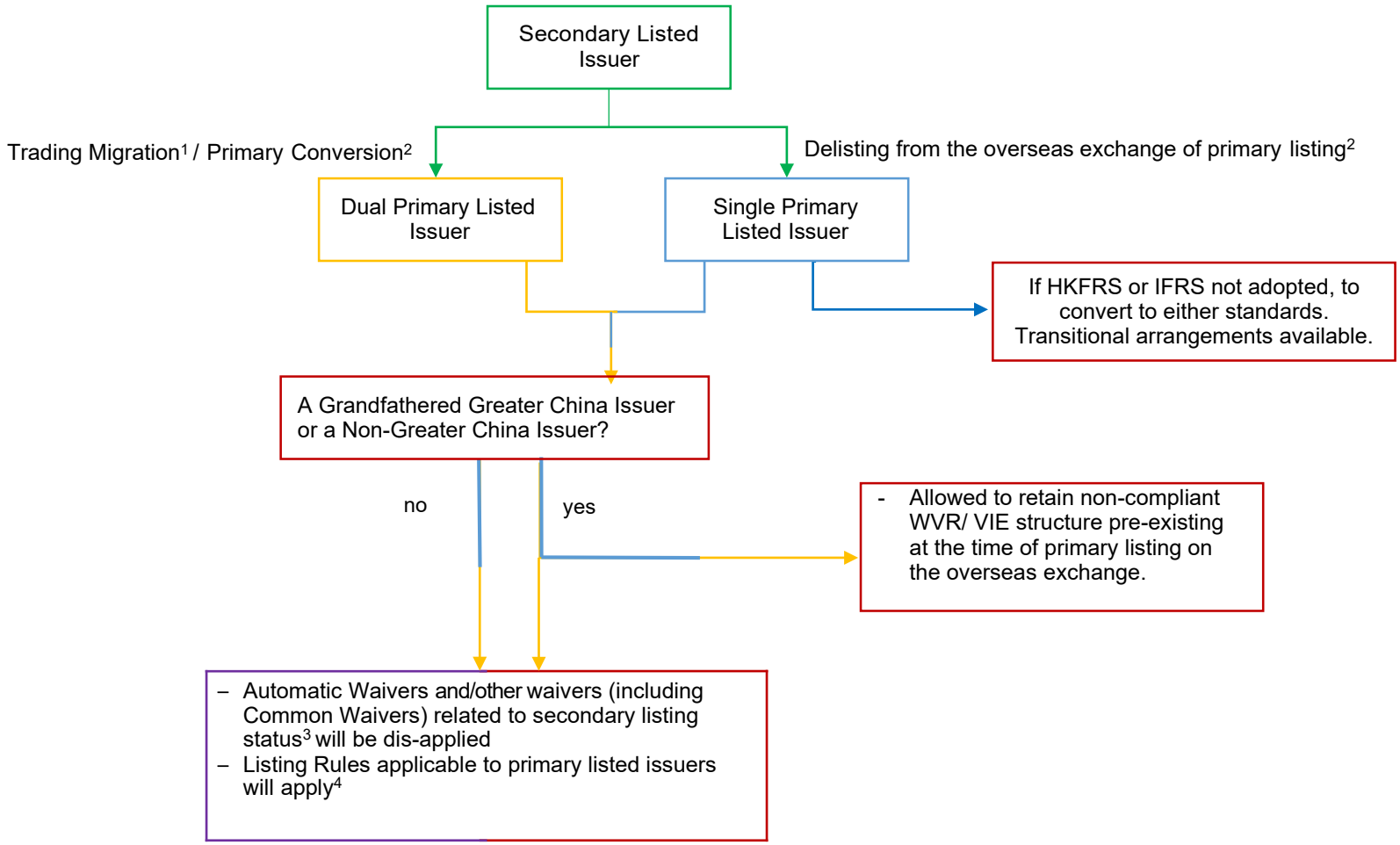
	Nature of transaction	Required level of compliance with Listing Rules
	Continuing transaction ▪ remains subsisting as at the date of the Primary Conversion Application ▪ the transaction is expected to continue after the Primary Conversion becomes effective (see paragraph 1.2)	Full compliance
Overseas De-listing (voluntary)	One-off transaction ▪ entered into before the Overseas De-listing becomes effective ▪ the transaction is expected to be completed after the Overseas De-listing becomes effective ▪ such transaction would have been subject to the requirement to issue an announcement and a circular and/or obtain shareholders' approval under the Listing Rules if such De-listing Issuer were a primary listed issuer at the time when the transaction was entered into (see paragraph 1.3)	Required to make an announcement of the transaction to keep the market informed on a timely basis, providing details of the transaction. Normally expected to make the transaction conditional on the issue of a circular and/or shareholders' approval (as the case may be) if the voluntary De-listing Issuer is aware of the imminent Change of Listing Status at the time of entering into the transaction.

	Nature of transaction	Required level of compliance with Listing Rules
	Continuing transaction ▪ remains subsisting as at the date of the De-listing Issuer Notification ▪ the transaction is expected to continue after the Overseas De-listing becomes effective (see paragraph 1.2)	Full compliance
Overseas De-listing (involuntary)	One-off transaction ▪ entered into before the Overseas De-listing becomes effective ▪ the transaction is expected to be completed after the Overseas De-listing becomes effective ▪ such transaction would have been subject to the requirement to issue an announcement and a circular and/or obtain shareholders' approval under the Listing Rules if such De- listing Issuer were a primary listed issuer at the time when the transaction was entered into (see paragraph 1.3)	Required to make an announcement of the transaction to keep the market informed on a timely basis, providing details of the transaction. Normally expected to make the transaction conditional on the issue of a circular and/or shareholders' approval (as the case may be) if the involuntary De-listing Issuer is aware of the imminent Change of Listing Status at the time of entering into the transaction.

	Nature of transaction	Required level of compliance with Listing Rules
	Continuing transaction ▪ entered into before the submission of the De-listing Issuer Notification ▪ the transaction is expected to continue after the Overseas De-listing becomes effective (see paragraph 1.1)	Exempted from the applicable rules set out in Listing Rule 19C.11 for a period of three years from the date of the De-listing Issuer Notification. The continuing transaction must be disclosed in the De-listing Issuer's announcement providing details of the transaction (see paragraph 3.43 of this letter). However, if such transaction is subsequently amended or renewed before the expiry of the three-year period, the De-listing Issuer must comply with the relevant requirements under the Listing Rules at such time.
	Continuing transaction ▪ entered into after the submission of the De-listing Issuer Notification ▪ the transaction is expected to continue after the Overseas De-listing becomes effective (see paragraph 1.2)	Full compliance

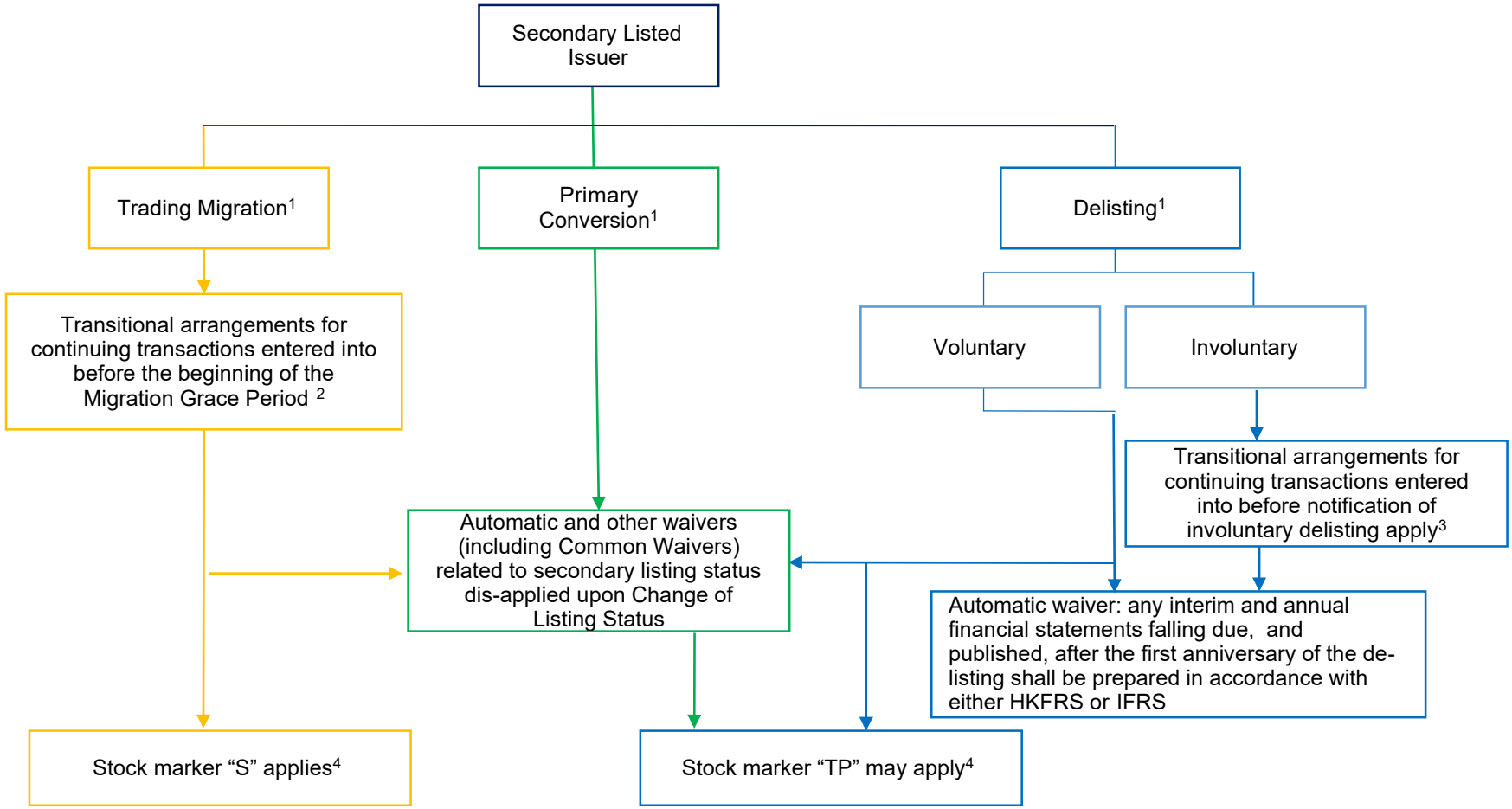
Appendix II

Change of Listing Status from Secondary Listing to Primary Listing



Notes:
1. Trading migration applies to all secondary listed issuers and is triggered when 55% or more of the total worldwide trading volume, by dollar value, of those shares (including the volume of trading in depositary receipts issued on those shares) over the Overseas Issuer's most recent financial year, takes place on the Exchange's markets.
2. See Sections C and D for the procedures relating to the application for primary conversion or de-listing from the overseas exchange of primary listing.
3. Where an Overseas Issuer would like to waive any applicable Listing Rules, a new wavier application is required despite a waiver previously granted under a secondary listing status.
4. In the event of trading migration, issuers are allowed to have a 12-month grace period from the Exchange's Notice on trading migration to comply with all applicable Listing Rules. In the event of primary conversion or delisting, issuers are expected to comply with all applicable Listing Rules upon primary conversion or delisting unless issuers have applied for, and have been granted, the relevant waivers.

Secondary Listed Issuers – Change of Listing Status Listing Rules Compliance



Note:
1. Refer to paragraph 1.3 of Appendix 1 for the arrangement for the one-off transaction entered into before the change of listing status but the transaction is expected to complete thereafter.
2. Refer to note 3 of R19C.13 of the Listing Rules.
3. Refer to paragraph 1.1 of Appendix 1.
4. The stock marker will only dis-apply upon full compliance with all Listing Rules applicable to dual-primary or, as the case may be, primary listed issuers.

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 Division on a confidential basis for an interpretation of the Listing Rules, or this letter.

Overseas issuers

1. Will the Exchange consider granting a waiver from compliance with any core shareholder protection standards (Core Standards) for an overseas issuer?

This depends on the facts and circumstances of an individual case. For example, the Exchange may consider granting a waiver if a Core Standard is legally impossible for an overseas issuer to comply with because it conflicts with the laws and regulation of its place of incorporation.

Normally a deviation from a Core Standard will not be granted if the Exchange considers that such variation may be detrimental to shareholder protection.

Furthermore, an overseas issuer cannot rely on the statutory minimum requirements under applicable laws that deviate materially from market norms in Hong Kong.

MB App A1
GEM App A1
First released: January 2022; last updated: May 2024

2. What information needs to be included in the Company Information Sheet?

The information expected to be included in a Company Information Sheet is set out in MB Rule 19.60(1) to (4) / GEM Rule 24.27(1) to (3).

For a primary listed or dual primary listed issuer, the overseas issuer is only required to include the specific information in its Company Information Sheet if any of the criteria stated in sub-paragraphs (1) to (4) of MB Rule 19.60 / sub-paragraphs (1) to (3) of GEM Rule 24.27 applies. For example, where criteria (1) applies, that is, novel waivers are granted to the overseas issuer and none of the other criteria are applicable, the overseas issuer is only required to include a summary of the novel waivers in its Company Information Sheet.

MB Rules 19.60, 19C.10B(7) and 19C.24, GL111-22
GEM Rule 24.27 and GL111-22
First released: January 2022; last updated: May 2024

3. What are considered to be novel waivers under MB Rule 19.60(1) / GEM Rule 24.27(1)?

The purpose of a Company Information Sheet is to provide investors with additional information on an issuer to enable them to make informed investment decision taking into account all relevant circumstances of the issuer. An overseas issuer should exercise its judgement in assessing what constitute novel waivers.

Below are non-exhaustive examples:

(i) compliance of any Core Standards or any other Listing Rules which affect shareholders' rights;

(ii) MB Rules 4.10 and 4.11 of, and note 2.1 to paragraph 2 of Appendix D2 to, MB Rules / GEM Rules 7.11, 7.12 and 18.04 requiring an issuer to prepare its financial statements in the listing document and the subsequent financial reports issued after listing to be in conformity with: (a) HKFRS; (b) IFRS; or (c) CASBE;

(iii) MB Rules 8.08(1), 8.09(1), 13.32 and 13.33 / GEM Rules 11.23(2)(a), 11.23(7), 11.23(11) and note 5 to GEM Rule 11.23 relating to minimum public float and minimum percentage of public holdings requirements;

(iv) MB Rules 10.05 and 10.06 / GEM Rules 13.03 to 13.14 relating to the restrictions and notification requirements on issuers purchasing their own shares on a stock exchange; and

(v) any provisions of the Takeovers Code/ SFO.

In general, the Exchange would not ordinarily regard the following as novel waivers:

(i) specific disclosure in the listing document on the offering and/ or placing of shares at the time of IPO e.g. dealing in shares prior to listing and clawback mechanism; and

(ii) MB Chapter 14A / GEM Chapter 20 waivers in respect of the continuing connected transaction.

MB Rules 4.10, 4.11, 8.08(1), 8.09(1), 10.05, 10.06, 13.32, 13.33, 19.60, 19C.10B(7), 19C.24 and Chapter 14A, AppD2 - note 2.1 to paragraph 2 and GL111-22
GEM Rules 7.11, 7.12, 11.23, 13.03 to 13.14, 18.04, and 24.27, Chapter 20 and GL111-22
First released: January 2022; last updated: May 2024

Guidance on continuing obligations under Chapter 18

A. Background and purpose

1. This letter assists Mineral Companies and listed issuers that publicly disclose details of resources and/or reserves (**R18.15 Companies**) by giving guidance for the better discharge of their continuing obligations under Chapter 18 of Main Board Rules (Chapter 18A of GEM Rules).

2. The revised Chapter 18 of Main Board Rules (Chapter 18A of GEM Rules) became effective on 3 June 2010. Since then, the Exchange has reviewed the operation of Chapter 18 by looking at specific required disclosures in annual reports for Mineral Companies and R18.15 Companies. It has identified certain disclosure areas that could be improved.

B. Relevant Listing Rules

3. Definition of Mineral Company under Chapter 18:

"Mineral Company"	*a new applicant whose Major Activity (whether directly or through its subsidiaries) is the exploration for and/or extraction of Natural Resources, or a listed issuer that completes a Relevant Notifiable Transaction involving the acquisition of Mineral or Petroleum Assets.*

Note: "Natural Resources" includes both minerals and oil and gas.

4. Extracts of provisions relating to continuing obligations under Main Board Chapter 18:

CONTINUING OBLIGATIONS

Disclosure in reports

18.14 A Mineral Company must include in its interim (half-yearly) and annual reports details of its exploration, development and mining production activities and a summary of expenditure incurred on these activities during the period under review. If there has been no exploration, development or production activity, that fact must be stated.

Publication of Resources and Reserves

18.15 A listed issuer that publicly discloses details of Resources and/or Reserves must give an update of those Resources and/or Reserves once a year in its annual report, in accordance with the reporting standard under which they were previously disclosed or a Reporting Standard.

18.16 A Mineral Company must include an update of its Resources and/or Reserves in its annual report in accordance with the Reporting Standard under which they were previously disclosed.

18.17 Annual updates of Resources and/or Reserves must comply with rule 18.18.

Note: Annual updates are not required to be supported by a Competent Person's Report and may take the form of a no material change statement.

STATEMENTS ON* RESOURCES *AND/OR RESERVES

Presentation of data

18.18 Any data presented on Resources and/or Reserves by a Mineral Company in a listing document, Competent Person's Report, Valuation Report or annual report, must be presented in tables in a manner readily understandable to a non-technical person. All assumptions must be clearly disclosed and statements should include an estimate of volume, tonnage and grades.

C. Guidance

5. The main purpose of imposing continuing obligations under Chapter 18 is to ensure that investors are provided with significant, relevant and reliable information about companies engaged in exploration and production of natural resources. The following guidance on disclosures is not meant to be exhaustive. A listed issuer should assess its own situation to decide whether additional disclosures are appropriate.

6. The Exchange expects Mineral Companies and R18.15 Companies to observe the following when preparing annual reports/interim reports in accordance with the above provisions of Chapter 18:

C.1 Interim and annual reports

Exploration, development and mining production activities

7. For the disclosures on exploration, development and mining production activities in the interim and annual reports:

(i) Details of exploration activities including number, average size, total length of holes drilled during the review period.

(ii) Details of development activities including progress on the mining structure or infrastructure.

(iii) Details of mining activities including quantity of mineral ore being mined during the period under review by project or at least a separate discussion on major projects.

(iv) Details of new contracts and commitments entered into during the period including those related to infrastructure projects (road and railway), subcontracting arrangements and purchases of equipment.

If a Mineral Company has several mineral assets/projects on hand, it should consider presenting this information on a project basis.

Expenditures incurred

8. The summary of expenditures incurred should not be limited to operating expenses, i.e. costs that were directly charged to income statement during the period they were incurred. A Mineral Company should also disclose the capital expenditures incurred, which could be much more significant than operating expenses.

9. Common expenses include mining costs, processing costs, transportation, royalties or fees payable to government and financing costs. A Mineral Company, depending on its own situation, should consider providing a further breakdown of expenses incurred in order to provide more meaningful information to its shareholders and enhance the transparency of its activities (e.g. separately disclose labour costs incurred for mining activities and processing activities).

C.2 Annual reports

Annual updates on resources and reserves

10. Generally, Rules 18.15 to 18.18 require a Mineral Company or a R18.15 Company to provide updates of its resources and reserves in a table and present it in a readily understandable manner in its annual reports. In addition, it should disclose the assumptions adopted. For any material change of assumption as compared with previous disclosed estimates, it is expected that the reasons for such changes should also be disclosed.

11. It would be useful for a Mineral Company to include a discussion on the reasons for changes in the resources and reserves estimates. Examples include changes in geological confidence level, additional drilling information becoming available, amount of mineral mined during the period etc.

Whether the Exchange would grant a waiver to a listed issuer to allow it to defer the publication of the competent person's report, valuation report and other disclosures for an acquisition of an overseas listed mineral company in a hostile takeover

Parties

- **Company A** – a Main Board issuer
- **Target** – a company listed on the Australian Stock Exchange

Facts

1. The Target was an iron ore development company and its principal assets were some iron mines in Australia.

2. Company A proposed to make a conditional offer to acquire all interests in the Target not already held by it (**Offer**). The Offer price was determined with reference to the Target's share price. The Offer was conditional on Company A acquiring at least a 50.1% interest in the Target.

3. The Offer was a major transaction for Company A. Company A submitted that it would defer complying with the financial and other disclosure requirements in accordance with Rule 14.67A as it could meet the conditions set out in the Rule:

   (i) the Offer was not invited by the Target's board. Company A did not have access to the Target's non-public information and records necessary for complying the disclosure requirements under the Rules;

   (ii) ASX is a regulated, regularly operating and open stock exchange recognized by the Exchange; and

   (iii) the Target would become a subsidiary of Company A.

4. According to Rule 14.67A, Company A would publish an initial circular to seek shareholders' approval for the Offer. It would publish a supplemental circular to include the outstanding information within 45 days of the earlier of it being able to (i) gain access to the Target's books and records; and (ii) exercise control over the Target.

5. As the Offer was a Relevant Notifiable Transaction under Chapter 18, Company A's initial circular for the Offer should also contain a Competent Person's Report (**CPR**) and a valuation report (**VR**) on the Target's natural resources and other disclosures required under Rules 18.09(2), (3) and (4). For the same reasons set out in paragraph 3, Company A would have practical difficulty in obtaining the Target's non-public information for making the disclosures in the initial circular.

6. Company A therefore sought a waiver from Rules 18.09(2), (3) and (4) so that it could defer the disclosure of information to the supplemental circular for the Offer. It submitted that it would summarise and reproduce the public statements and reports on the Target's mineral assets and other material information published by the Target in the initial circular to enable shareholders to make an informed voting decision on the Offer.

Relevant Listing Rules

7. Rule 18.05(2) to (6) provides that "*a Mineral Company must include in its listing document:—*

…

(2) a statement that no material changes have occurred since the effective date of the Competent Person's Report. Where there are material changes, these must be prominently disclosed;

(3) the nature and extent of its prospecting, exploration, exploitation, land use and mining rights and a description of the properties to which those rights attach, … . Details of material rights to be obtained must also be disclosed;

(4) a statement of any legal claims or proceedings that may have an influence on its rights to explore or mine;

(5) disclosure of specific risks and general risks. Companies should have regard to Guidance Note 7 on suggested risk analysis; and

(6) if relevant and material to the Mineral Company's business operations, information on the following:—

(a) project risks arising from environmental, social, and health and safety issues;

(b) any non-governmental organisation impact on sustainability of mineral and/or exploration projects;

(c) compliance with host country laws, regulations and permits, and payments made to host country governments in respect of tax,

(d) royalties and other significant payments on a country by country basis;

(e) sufficient funding plans for remediation, rehabilitation and, closure and removal of facilities in a sustainable manner;

(f) environmental liabilities of its projects or properties;

(g) its historical experience of dealing with host country laws and practices, including management of differences between national and local practice;

(h) its historical experience of dealing with concerns of local governments and communities on the sites of its mines, exploration properties, and relevant management arrangements; and

(i) any claims that may exist over the land on which exploration or mining activity is being carried out, including any ancestral or native claims."

8. Rule 18.09 requires that "*A mineral company proposing to acquire or dispose of assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must:-*

(1) comply with Chapter 14 and Chapter 14A, if relevant;

(2) produce a Competent Person's Report, which must form part of the relevant circular, on the Resources and/or Reserves being acquired or dispose of as part of the Relevant Notifiable Transaction;

…

(3) in the case of a major (or above) acquisition, produce a Valuation Report, which must form part of the relevant circular, on the Mineral or Petroleum Assets being acquired as part of the Relevant Notifiable Transaction; and…

(4) comply with the requirements of rules 18.05(2) to 18.05(6) in respect of the assets being acquired."

9. Rule 18.10 states that "*a listed issuer proposing to acquire assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must comply with rule 18.09*".

Analysis

10. Under the Listing Rules, an issuer must ensure that the information in its circular for a notifiable transaction is accurate and complete in all material respects and not misleading or deceptive. The circular must contain all information necessary to allow the issuer's shareholders to make a properly informed decision on how to vote on the transaction.

11. Rule 14.67A addresses issuers' practical difficulties in disclosing non-public financial and other information of the target companies in hostile takeover situations. The Exchange considers that the same principle may also apply to the disclosure requirements under Chapter 18 based on the circumstances of each case.

12. Here the Exchange agreed to grant the waiver because:

    - the Offer could meet the conditions set out in Rule 14.67A.

    - the Target was listed on an overseas stock exchange, and had been providing regular updates on its mineral assets. The disclosures were subject to supervision by regulatory authorities. Company A would include material public information of the Target in the initial circular to enable shareholders to make an informed voting decision.

Conclusion

13. Company A was granted a waiver to defer the CPR, the VR and other disclosures as required under Rules 18.09(2), (3) and (4) to the supplement circular.

Whether the Exchange would waive the requirement to publish a competent person's report on the mineral resources to be disposed of by a listed issuer

Facts

1. A Main Board issuer (**Company A**) proposed to sell its interest in one of its mining projects (**Mine Y**) to a third party, which would be a very substantial disposal. The consideration was determined with reference to the value of the reserves and resources of the mine. The Rules required Company A to include a competent person's report (**CPR**) on Mine Y in the circular for the disposal.

Background

2. Mine Y was acquired by Company A some years ago (before the current Chapter 18 came into effect). At that time, a technical report for Mine Y (**Technical Report**) was included in the transaction circular. The report was prepared by an expert (**Expert**) using the Chinese Standard. The Expert provided a comparison between the Chinese Standard and the JORC Code, and quoted the resources and reserves using categorization under the JORC Code. However, the resources and reserves were not reported as JORC Code compliant resources and reserves because certain information required for such conversion was not available to the Expert.

3. After the completion of the acquisition, Company A updated Mine Y's resources and reserves in accordance with the Chinese Standard in its subsequent annual reports.

Waiver application

4. For the proposed disposal, Company A sought a waiver from producing a CPR on Mine Y in the circular. It was of the view that its shareholders would have sufficient information to assess the proposed disposal based on the Technical Report previously provided, and a "no material change statement" by Company A and the Expert to be included in the circular for the disposal. It would be unduly burdensome to engage a competent person to prepare a new CPR on Mine Y given the substantial time and costs required.

Relevant Listing Rules

5. Rule 2.13 provides that "*… any announcement or corporate communication required pursuant to the Exchange Listing Rules must be prepared having regard to the following general principles:*

…

(2) the information contained in the document must be accurate and complete in all material respects and not be misleading or deceptive. …"

6. Chapter 18 defines that:

"***Mineral Company***" *… a listed issuer that completes a Relevant Notifiable Transaction involving the acquisition of Mineral or Petroleum Assets.*

7. Rule 18.09 requires that "*A mineral company proposing to acquire or dispose of assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must:-*

…

(2) produce a Competent Person's Report, which must form part of the relevant circular, on the Resources and/or Reserves being acquired or dispose of as part of the Relevant Notifiable Transaction;

Note: The Exchange may dispense with the requirement for a Competent Person's Report on disposals where shareholders have sufficient information on the assets being disposed of.

…"

8. Rule 18.29 states that "*A Mineral Company must disclose information on mineral Resources, Reserves and/or exploration results either:—*

(1) under:

(a) the JORC Code;

(b) NI 43-101; or

(c) the SAMREC Code,

…"

Analysis

9. In this case, the Exchange noted the Technical Report was issued some years ago and was outdated. It was prepared under the Chinese standard which however is not a recognised reporting standard acceptable by the Exchange under the current Chapter 18. The Exchange did not agree that Company A's proposed disclosure would provide accurate and complete information on the resources of Mine Y for the shareholders to make an informed voting decision on the disposal.

Conclusion

10. The Exchange refused the waiver.

Whether the Exchange would waive the requirements to publish competent person's reports and valuation reports on some of the mining interests held by the target company to be acquired by the listed issuer

Parties

- **Company A** – a Main Board issuer
- **Target** – a company which Company A proposed to acquire from a third party vendor

Facts

1. Company A proposed to acquire the Target.

2. The Target was in the business of exploration and mining of minerals. Its primary asset was the interest in a mining project (**Mine X**) and it held the mining licence for the mine. The Target also held the exploration licences for two other mines (**Other Mines**).

3. Under the Rules, Company A was required to include competent person's reports (**CPRs**) and valuation reports covering all the mines held by the Target in its circular for the acquisition. It sought a waiver from producing the CPRs and valuation reports on the Other Mines for the following reasons:

    - The Target had not undertaken any exploration or mining activities at the Other Mines. There was not much geological information or resources data for these mines. To prepare CPRs, the competent person would need to conduct substantial work and spend a long time to complete the process.

    - Based on the due diligence work performed by Company A, resources in the Other Mines appeared to be mainly inferred resources. Their economic values were expected to be immaterial and no valuation on these resources would be allowed under the Rules.

    - The reason for Company A to acquire the Target was to obtain a controlling interest in Mine X which had a substantial amount of reserves and resources. Company A had no intention to explore or exploit the Other Mines after completion of the acquisition. When determining the consideration for the acquisition, it did not take into account the value of the Other Mines. Based on the preliminary valuation, the value of Mine X represented over 90% of the consideration.

4. In light of the above, Company A considered the Other Mines were insignificant to the portfolio of mineral resources to be acquired under the acquisition. It would be unduly burdensome to require Company A to produce CPRs and valuation reports on the Other Mines in the circular.

Relevant Listing Rules

5. Rule 2.13 provides that "*… any announcement or corporate communication required pursuant to the Exchange Listing Rules must be prepared having regard to the following general principles:*

   … …

   (2) the information contained in the document must be accurate and complete in all material respects and not be misleading or deceptive. …"

6. Rule 18.09 requires that "*A mineral company proposing to acquire or dispose of assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must:-*

   …

   (2) produce a Competent Person's Report, which must form part of the relevant circular, on the Resources and/or Reserves being acquired or dispose of as part of the Relevant Notifiable Transaction;

   …

   (3) in the case of a major (or above) acquisition, produce a Valuation Report, which must form part of the relevant circular, on the Mineral or Petroleum Assets being acquired as part of the Relevant Notifiable Transaction; and… "

7. Rule 18.10 states that "*a listed issuer proposing to acquire assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must comply with rule 18.09*".

Analysis

8. In this case, the Exchange was satisfied with Company A's explanation that the Other Mines were only a minor part of the Target's portfolio of mineral resources under the acquisition, and the waiver would not result in an omission of material information in the circular. The Exchange agreed that it would be unduly burdensome for Company A to produce the CPRs and valuation reports on the Other Mines.

Conclusion

9. The Exchange agreed to waive the requirements for producing CPRs and valuation reports on the Other Mines.

Whether the Exchange would waive the requirements to publish a competent person's report and a valuation report on the mineral assets held by an overseas listed target company to be acquired by the listed issuer

Parties

- **Company A** – a Main Board issuer
- **Target** – a company listed on the Toronto Stock Exchange and the New York Stock Exchange

Facts

1. The Target was a global oil and gas exploration and development company.

2. Under the agreement between Company A and the Target, Company A would acquire all the shares in the Target through a plan of arrangement subject to the court's approval. Upon completion, the Target would become a subsidiary of Company A.

3. The acquisition was a major transaction for Company A. Under Rules 18.09(2) and 18.09(3), Company A's circular must include a CPR on the Target's oil and gas reserves and a VR on its petroleum assets. Company A sought a waiver from these requirements for the following reasons:

   (a) It would be unduly burdensome to produce a CPR on the Target's oil and gas reserves because:

   - The Target was an overseas listed company. It had regularly published information on its oil and gas reserves in accordance with the overseas regulatory requirements.
   - The Target's petroleum assets were extensive and located in various countries around the world. Substantial time and costs would be required to prepare the CPR.
   - Company A had obtained a written approval of the acquisition from its parent company according to Rule 14.44. The circular would be issued to its shareholders for information only.

   (b) Alternatively, the circular would include information on the Target's reserves estimates contained in its latest annual filings with the overseas stock exchanges (the **Reserves Information**). Company A believed that this would provide sufficient information for its shareholders' assessment because:

- The Reserves Information was prepared and reported on by technical experts with relevant qualifications and experience.

  - The Target had adopted strict internal procedures for preparing the Reserves Information to ensure compliance with the overseas regulatory requirements. The responsible officer, who prepared the information, possessed relevant qualifications and had extensive experience in the oil and gas industry. He was able to satisfy the eligibility requirements for a Competent Person under Chapter 18 of the Rules.

  - Further, over 90% of the reserves estimates had been reported on by independent reserves evaluators with international names and reputation.

  - The circular would include (i) the qualifications and experience of the responsible officer, and the primary technical persons of the independent reserves evaluators; and (ii) the opinion letters from the independent reserves evaluators.

- The Reserves Information was disclosed under NI 51-101[1] which was a well recognised international standard adopted by international oil and gas companies.

- Taking into account the Target's disclosure since the last annual filings and its recent review on the reserves estimates, Company A confirmed that there had been no material change to the Reserves Information.

(c) It would also be unduly burdensome to produce a VR on the Target's petroleum assets because:

- Company A was to acquire the Target's shares which were listed and traded on two overseas stock exchanges. It believed that the share trading price and market capitalisation of the Target would serve as a reasonable reference in assessing the Target's market value.

- The consideration for the acquisition was determined with reference to the market price of the Target's shares and Company A's view on the value of the Target's business and assets. The consideration was not based on an asset valuation approach.

[1] National Instrument 51-101 "Standards of Disclosures for Oil and Gas Activities", which was implemented in September 2003 by the Canadian Securities Administrators, provides comprehensive rules for reserves disclosure by relevant oil and gas companies in Canada. It requires oil and gas companies to report annually on their reserves and oil and gas activities, and where a material change occurs in a company's reserves after an annual filing is made, a company is required to disclose the changes to their reserves to the Canadian Securities Administrators and the public before the next required annual filing.

Relevant Listing Rules

4. Rule 18.09 states that

"*A mineral company proposing to acquire or dispose of assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must:-*

(1) comply with Chapter 14 and Chapter 14A, if relevant;

(2) produce a Competent Person's Report, which must form part of the relevant circular, on the Resources and/or Reserves being acquired or dispose of as part of the Relevant Notifiable Transaction;

Note: …

(3) in the case of a major (or above) acquisition, produce a Valuation Report, which must form part of the relevant circular, on the Mineral or Petroleum Assets being acquired as part of the Relevant Notifiable Transaction; and …

(4) ….

Note: …"

5. Rule 18.10 states that:

"*A listed issuer proposing to acquire assets which are solely or mainly Mineral or Petroleum Assets as part of a Relevant Notifiable Transaction must comply with rule 18.09.*"

Analysis

6. Under the Listing Rules, an issuer must ensure that the information in its circular for a notifiable transaction is accurate and complete in all material respects and not misleading or deceptive. The circular must contain all information necessary to allow the issuer's shareholders to make a proper assessment of the transaction and if voting is required, how to vote.

7. Where the transaction involves an acquisition or disposal of material mineral or petroleum assets, the issuer must comply with the additional disclosure requirements under Chapter 18.

8. When assessing Company A's waiver application, the Exchange noted that:

(a) the Target was listed on recognised overseas exchanges, and the Reserves Information was subject to supervision by regulatory authorities;

(b) the Reserves Information was prepared and reported on by technical experts with relevant qualifications and experience;

(c) NI 51-101 was an acceptable reporting standard for the Target's reserves estimates (see also Listing Decision HKEx-LD51-2013);

(d) Company A would provide a no material change statement for the Reserve Information in the circular for the acquisition.

9. The Exchange agreed that compliance with the CPR requirements would be unduly burdensome in this case. The proposed alternative disclosure would provide relevant and reliable information on the Target's oil and gas reserves comparable to that required under Chapter 18 of the Rules.

10. The Exchange also noted that the Target's share price and market capitalisation would represent its fair value, and the consideration for the acquisition was not based on a valuation of the Target's assets. Granting a waiver from the VR requirement would be unlikely to result in undue risks to the shareholders.

Conclusion

11. The Exchange granted the waiver to Company A.

Mineral Companies

1. What information does the Exchange require when assessing whether a person has the relevant experience to act as the Competent Person?

The person should ensure there are sufficient details to demonstrate that the experience is relevant to the relevant mineral or petroleum assets. In general, the person is expected to provide a list of engagements showing his relevant experience with the following information:

- the period of each engagement;
- a description of each project undertaken, including the location and the type of resources involved, and the relevance to the mineral or petroleum resources being acquired or disposed of;
- details of any technical reports on the resources of the project, including the reporting standards and the use of the reports; and
- details of his role and responsibilities in the project and the preparation of any technical reports.

MB Rule 18.21(1)
GEM Rule 18A.21(1)
First released: March 2013; last updated: May 2024

2. Is a listed issuer required to aggregate a series of acquisitions or disposals of Mineral or Petroleum Assets under MB Rules 14.22 and 14.23 / GEM Rules 19.22 and 19.23 and treat them as a Relevant Notifiable Transaction for the purpose of MB Chapter 18 / GEM Chapter 18A?

Yes.

MB Rule 14.22, 14.23 and 18.01(3)
GEM Rule 19.22, 19.23 and 18A.01(3)
First released: March 2013; last updated: May 2024

3. Does MB Chapter 18 / GEM Chapter 18A applies to connected transactions involving the acquisition or disposal of assets which are solely or mainly Mineral or Petroleum Assets?

MB Chapter 18 / GEM Chapter 18A applies if such acquisition or disposal also constitutes a Relevant Notifiable Transaction (as defined under MB Rule 18.01(3) / GEM Rule 18A.01(3)).

MB Rules 18.09, 18.10, Chapter 14A
GEM Rules 18A.09, 18A.10 and Chapter 20
First released: March 2013; last updated: May 2024

4. If the acquisition target reports its Reserve and Resource information using a different mineral report code, (e.g. NI 43-101), whilst the Mineral Company reports using the JORC Code, would the Exchange accept both Reporting Standards?

Yes, if the presentation of Reserves and Resources under the codes are very similar. For comparability, we will require the listed issuer to (i) disclose a reconciliation to one of the accepted Reporting Standards; and (ii) highlight any material differences in these Reporting Standards.

MB Rule 18.01(3), 18.28 to 18.33
GEM Rule 18A.01(3), 18A.28 to 18A.33
First released: March 2013; last updated: May 2024

5. Will valuations of Natural Resource assets (i.e. Reserves) based on discounted cash flows (DCF) be regarded as profit forecasts under MB Rules 14.60A and 14.61 / GEM Rules 19.60A and 19.61 which is required to be reviewed by the reporting accountants?

No, if the valuation meets the requirements of MB Chapter 18 / GEM Chapter 18A.

MB Rule 11.17, 14.60A, 14.61, 18.34, App1A(34)(2) and App1B (29)(2)
GEM Rule 14.29, 18A.34, 19.60A, 19.61, App1A(34)(2) and App1B(29)(2)
First released: March 2013; last updated: May 2024

Guidance on special purpose acquisition companies

I. Purpose

1. This letter provides guidance for special purpose acquisition companies (**SPAC(s)**) with, or seeking, a listing on the Exchange pursuant to MB Chapter 18B. The guidance is also set out in Chapter 2.4 of the Guide for New Listing Applicants (**Guide**).

II. Suitability of SPAC Promoters

Requirements

2. MB Rule 18B.10 provides that at listing of the SPAC and on an ongoing basis for the lifetime of the SPAC, the Exchange must be satisfied as to the character, experience and integrity of all SPAC Promoters and that each is capable of meeting a standard of competence commensurate with its position. For this purpose, a SPAC must ensure that:

   (i) At listing and on an ongoing basis, at least one of its SPAC Promoters is a firm that holds a Type 6 (advising on corporate finance) and/or a Type 9 (asset management) licence issued by the SFC; and

   (ii) It provides the Exchange with information that the Exchange requests in accordance with the Guide.

3. The Exchange will consider modifying or waiving the licensing requirement under MB Rule 18B.10(1), on a case-by-case basis, if a SPAC Promoter has overseas accreditation issued by a regulatory authority that the Exchange considers to be equivalent to a Type 6 and/or Type 9 licence issued by the SFC. A SPAC seeking such modification or waiver must provide:

   (i) Documentary evidence that the SPAC Promoter has obtained such accreditation; and

   (ii) Details of the initial and ongoing requirements that the SPAC Promoter must fulfil for the purpose of this overseas accreditation and a comparison against the corresponding requirements for a Type 6 and/or Type 9 licence issued by the SFC.

4. A SPAC Promoter that does not hold the requisite SFC licence would be considered to have met the licensing requirement under MB Rule 18B.10(1) if its controlling shareholder satisfies the requirement. This is subject to the conditions that:

   (i) The SPAC demonstrates that sufficient safeguards and/or undertakings are put in place to ensure the SPAC Promoter's controlling shareholder's oversight of the SPAC Promoter's responsibilities; and

   (ii) The SPAC Promoter's controlling shareholder gives an undertaking to the Exchange that they will ensure the SPAC Promoter's compliance with applicable Listing Rules.

5. MB Rules 18B.32 to 18B.34 would apply if there is a material change in such controlling shareholder.

Character, experience and integrity

6. The listing document should include the following information:

SPAC Promoter experience	(i) For each SPAC Promoter, its experience as a SPAC Promoter in other SPACs which it established/is interested in previously and/or currently, including its role, level of involvement, duration, and the names of such SPACs. (ii) For each of the SPACs referred to in (i): (a) Amount of funds raised at its initial offering; (b) Selection criteria (e.g. size and sector) of the De-SPAC Target; (c) Size and terms of the Promoter Shares; (d) Time that elapsed between the date of the SPAC's initial offering and the date of the completion of any De-SPAC Transaction; (e) Amount of funds raised from independent third party investment as part of any De-SPAC Transaction; (f) A summary of the De-SPAC Target that was the subject of any De-SPAC Transaction (e.g. sector and geographical location, market share, brief historical financial data and its management); (g) Salient terms of any De-SPAC Transaction, including valuation, conditions to completion and parties involved; (h) (1) Percentage of any redeeming SPAC shareholders in connection with any De-SPAC Transaction; (2) percentage of SPAC shareholders that voted against any De-SPAC Transaction; and (3) a summary of the impact of dilution to non-redeeming SPAC shareholders upon exercise of all SPAC Warrants and conversion of all Promoter Shares and all Promoter Warrants in the Successor Company; (i) Market capitalisation of the Successor Company following any De-SPAC Transaction; (j) Performance indicators of the Successor Company since any De-SPAC Transaction (absolute performance indicators and performance relative to that of relevant indexes); and (k) Whether the SPAC was liquidated and/or required to return its funds to SPAC shareholders.

Investment management experience	(i) Experience in the professional management of investments on behalf of third party investors and/or provision of investment advisory services to professional/institutional investors, including, for each role, a description of: (a) Its role and responsibilities; (b) The types and geographical coverage of investments managed, fund size, and the fund's investment objectives and policies; and (c) Performance indicators (e.g. net asset value of the managed funds, their absolute performance and relative performance compared to that of other major managed funds and indexes).
Other experience	(i) Other experience relevant to the role of SPAC Promoter for the SPAC seeking a listing (e.g. managing businesses in the sectors in which the SPAC aims to identify targets) with an explanation of how this experience is relevant to a SPAC Promoter role.
Other information	(i) Details of licences held (see paragraphs 2(i) and 3 above), including the year they were obtained and the granting institutions. (ii) Any business interests that compete or are likely to compete either directly or indirectly with the SPAC for prospective De-SPAC Targets with details of the nature of the competition[1]. (iii) Any breaches of laws, rules and regulations and any other matters that have a bearing on the integrity and/or competence of the SPAC Promoter.

7. A SPAC Promoter that can demonstrate the following experiences will be viewed favorably by the Exchange:

   (i) Managing assets with an average collective value of at least HK$8 billion over a continuous period of at least three financial years; or

   (ii) Holding a senior executive position (e.g. chief executive or chief operating officer) at an issuer that is or has been a constituent of the Hang Seng Index or an equivalent flagship index[2].

8. The factors set out in paragraphs 6 and 7 above are neither exhaustive nor binding. The Exchange will exercise its discretion on a case-by-case basis and adopt a holistic approach to determine whether it is satisfied with the suitability and eligibility of a SPAC Promoter.

III. Listing applications

9. A SPAC (for its initial listing) and a Successor Company (for a De-SPAC Transaction) must file a new application for listing in accordance with MB Chapter 9[3].

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1 Existing requirements on competing interests under MB Rule 8.10, paragraph 27A of Appendix D1A to the Listing Rules, and Chapter 3.8 of the Guide on guidance of relationship with controlling shareholders will apply to SPACs, and "controlling shareholders" in those materials shall be deemed to include "SPAC Promoters".

2 Including a well referenced index within a particular market. For example, S&P 500 (SPX), NASDAQ-100 Index (NDX) and Dow Jones Industrial Average (DJI) in the US, and FTSE 100 (UKX) in the UK.

3 See "Checklists and Forms for New Applicants" available on the Exchange's website for a list of documents required to be filed with the Exchange together with the respective listing application.

10. In respect of the prospectus and disclosure requirements under the Companies (Winding up and Miscellaneous Provisions) Ordinance (Cap. 32) (**C(WUMP)O**):

    (i) A SPAC and a Successor Company should seek legal advice on the extent to which its listing document at initial listing and De-SPAC Transaction (as the case may be) must comply with the prospectus requirements of C(WUMP)O; and

    (ii) The Exchange will view a De-SPAC Transaction as equivalent to an offering to the public and will vet the listing document issued for the De-SPAC Transaction on the basis that it must meet the prospectus disclosure requirements of C(WUMP)O in full.

IV. Stock marker

11. The listed securities of a SPAC will be assigned a special stock short name marker.

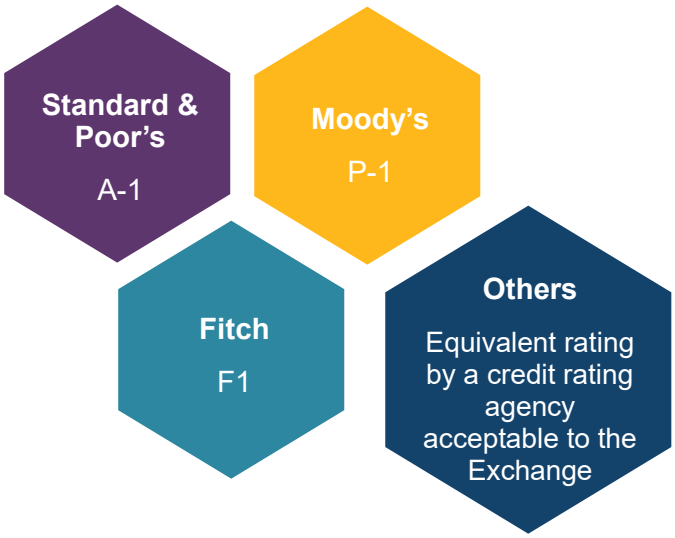
	Marker for stock short name
SPAC Shares	End with the marker "Z".
SPAC Warrants	End with the marker "Z Y Y M M" or "Z Y Y" (with YY representing the expiry year and MM representing the expiry month of the SPAC Warrants).

See the Exchange's website for details.

V. Funds in escrow account – cash equivalent

12. Proceeds from a SPAC's initial offering should be held in the form of cash or cash equivalent. Short-term securities issued by governments with the following minimum credit ratings are considered as cash equivalent for the purpose of MB Rule 18B.18:

Credit agency and minimum credit ratings



VI. Financial information and accounting matters

13. The following information should be included in the "Financial Information" section of the listing document of a SPAC's initial listing:

Significant accounting policies and judgements	Significant accounting policies and judgements for SPAC transactions and material events that occurred subsequent to the balance sheet date, which have a significant effect on the amounts recognised in the financial statements and/or are relevant to an understanding of the financial information of the SPAC. The above should also be disclosed in the accountants' report as required under the applicable accounting standards. In particular, in the context of the initial listing of the SPAC, those disclosures should also cover accounting policies for transactions entered into subsequent to the balance sheet date. This requirement also applies to a SPAC on an ongoing basis (e.g. in the audited financial statements of the SPAC's annual report). *Note: A SPAC with, or seeking, a listing on the Exchange is advised to consult its reporting accountants (and other professional advisers, as appropriate) to evaluate the accounting implications for complex areas arising from SPAC transactions (such as the issuance of shares and warrants) with reference to applicable financial reporting standards.*
Pro forma net tangible assets/ liabilities	Pro forma adjustments and notes regarding net tangible assets/liabilities as required under paragraph 21 of Appendix D1A to the Listing Rules, where appropriate, providing sufficient information in accordance with MB Rule 4.29 to illustrate the potential financial impact arising from a SPAC's initial listing, including the accounting implications and effects of the shares and other financial instruments issued or to be issued by a SPAC.
Working capital sufficiency	A statement of working capital sufficiency required under MB Rule 8.21A, including the basis of the directors' view on its working capital sufficiency as required under paragraph 36 of Appendix D1A to the Listing Rules, and the basis upon which the sponsor concurs with the directors' view. *Note: For the purpose of this requirement, the relevant cash flow forecast should focus on the working capital needed to cover the operating expenses prior to the De-SPAC Transaction and exclude any amounts of the initial offering proceeds that are subject to redemption or amounts that are expected to be used to fund a De-SPAC Transaction.*

VII. Independent third party investors

Minimum independent third party investment thresholds

14. The minimum amount of investment referred to in MB Rule 18B.41 has been modified[4], such that the total funds to be raised from the independent third party investors referred to in MB Rule 18B.40 must constitute at least the prescribed percentage of the negotiated value of the De-SPAC Target as set out in that rule, or HK$500 million in value, whichever is lower.

[4] The modification will apply from 1 September 2024 to 31 August 2027. See the "Joint Announcement of the SFC and the Exchange in relation to Temporary Modifications to Requirements for Specialist Technology Companies and De-SPAC Transactions" dated 23 August 2024 on the Exchange's website.

Independence requirement

15. The independence requirement referred to in MB Rule 18B.40 has been modified[5], such that third party investors must meet the following independence requirements, instead of those that apply to an independent financial adviser under MB Rule 13.84:

    (i) The independence of a third party investor will be determined as at the date of the signing of the definitive agreement for the relevant investment in the De-SPAC Transaction, and up to listing of the Successor Company.

    (ii) The following persons will not be considered as independent third party investors:

        (a) Core connected persons[6] of the SPAC or the De-SPAC Target, except for any substantial shareholder of the SPAC or the De-SPAC Target that is considered a core connected person only because of the size of its shareholding in the SPAC or the De-SPAC Target (subject to paragraph 15(ii)(b) below);

        (b) Controlling shareholder (or any person within the group of persons who are considered as controlling shareholders) of the SPAC or the De-SPAC Target; and

        (c) The founders of the De-SPAC Target and their respective close associates.

    (iii) The Exchange retains the discretion to deem any other person to be not independent based on the facts and circumstances of an individual case. For example, a person who has an acting-in-concert agreement or arrangement with a SPAC Promoter or with a controlling shareholder of the SPAC or the De-SPAC Target or with a founder of the De-SPAC Target, normally will not be considered as independent.

Sophisticated independent third party investors

16. For the purpose of MB Rule 18B.42, a SPAC must demonstrate that at least 50% of the value of the independent third party investment referred to in MB Rule 18B.41 is contributed by no fewer than three sophisticated investors. The Exchange will assess whether an investor is sophisticated on a case-by-case basis by reference to its relevant investment experience, and its knowledge and expertise in the relevant field of the De-SPAC Target, which could be demonstrated by its net assets, assets under management (**AUM**), size of its investment portfolio or track record of investments, where applicable.

17. For illustrative purposes only, the Exchange would generally consider the following as examples of the types of investors that would be considered sophisticated for the purpose of paragraph 16:

    (i) An asset management firm with AUM of, or a fund with a fund size of, at least HK$8 billion;

    (ii) A company with a diverse investment portfolio size of at least $8 billion; or

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5 The modification will apply from 1 September 2024 to 31 August 2027. See the "Joint Announcement of the SFC and the Exchange in relation to Temporary Modifications to Requirements for Specialist Technology Companies and De-SPAC Transactions" dated 23 August 2024 on the Exchange's website.

6 As defined in MB Rule 18B.01 with respect to the core connected persons of the SPAC, or as defined in MB Rule 1.01 with respect to the core connected persons of the De-SPAC Target.

(iii) A key participant in the relevant upstream or downstream industry of the De-SPAC Target, with a meaningful market share and size, as supported by appropriate independent market or operational data.

18. "Investment portfolio" for the purpose of paragraph 17(ii) means the aggregate value of investments in investee companies as determined under the prevailing accounting standards. The Exchange may consider other measures of investment values that may not be reflected in the investor's financial statements, such as the fair value of an investment supported by an independent valuation. The Exchange would not consider consolidated subsidiaries to be investee companies.

19. A fund managed by a fund manager that has AUM of an amount that meets the threshold set out in paragraph 17(i), or a wholly-owned subsidiary of an entity referred to in paragraph 17(i) or (ii), would qualify as a sophisticated investor.

20. The Exchange may still consider investors of a type that is not included in the illustrative examples in paragraph 17 above as sophisticated, on a case-by-case basis, considering the specific circumstances of an applicant. The applicant should demonstrate that these investors have relevant investment experience, knowledge and expertise.

21. The applicant must disclose the size (and the basis for determination) of the AUM, the fund or the investment portfolio (as the case may be) and any other information relevant to the sophisticated independent third party investors in (i) the announcement of the De-SPAC Transaction (**De-SPAC Announcement**) referred to in MB Rule 18B.44; and (ii) the listing document issued for the De-SPAC Transaction referred to in MB Rule 18B.49 to substantiate that they have the relevant investment experience, knowledge and expertise to be considered sophisticated. Where the above information cannot be disclosed in detail for confidentiality reasons, the Exchange may accept alternative disclosures appropriate to the circumstances on a case-by-case basis, taking into account the factors set out in the relevant guidance that the Exchange has published[7]. Such information should be given as of:

(i) A date which is no more than six months prior to the date of signing of the definitive agreement for the investors' relevant investment in the De-SPAC Transaction; and

(ii) A date which is no more than six months prior to the date of the listing application of the Successor Company.

Commitment of independent third party investments

22. The independent third party investments required under MB Rules 18B.41 and 18B.42 must have been committed by the time of the De-SPAC Announcement.

[7] See Chapter 3.14 of the Guide and any other relevant guidance as implemented by the Exchange from time to time for guidance on alternative disclosure on the background and investment experience of the sophisticated independent investors.

VIII. De-SPAC Announcement

23. A De-SPAC Announcement must include the following information in addition to the requirements set out in MB Rules 18B.44 to 18B.48:

    (i) A description of all the independent third party investors referred to in MB Rule 18B.41, including the sophisticated investors referred to in paragraph 16, and the principal terms of their investments;

    (ii) The identities of, and amounts committed by, the independent third party investors;

    (iii) The negotiated value of the De-SPAC Target and the basis upon which such value was determined;

    (iv) The board of directors' opinion confirming the satisfaction of the "fair market value" requirement in MB Rule 18B.39 and the basis of such opinion (in a form acceptable to the Exchange[8]); and

    (v) The material terms of any earn-out rights referred to in Note 1 to MB Rule 18B.29(1).

IX. Participation by a SPAC Promoter in a SPAC's initial offering and De-SPAC Transaction

24. The Existing Shareholders Conditions referred to in Chapter 4.15 of the Guide are dis-applied to permit a SPAC Promoter to participate in: (1) an offering of SPAC Shares at the initial listing of a SPAC; and/or (2) the financing of a De-SPAC Transaction, subject to the below conditions:

    (i) The SPAC Promoter meets the definition of a Professional Investor;

    (ii) The SPAC or the Successor Company (as the case may be) complies with all applicable open market requirements, including MB Rule 18B.05 or 18B.65 (as applicable);

    (iii) The price and terms of subscription of shares by the SPAC Promoter must be substantially the same as, or are not more favourable to the SPAC Promoter, than those available to other investors who are investing in the SPAC or the Successor Company (as the case may be) at the same time as the SPAC Promoter, and any such participation increases the SPAC Promoter's "capital at risk" to align its interests more closely with the interest of ordinary shareholders;

    (iv) The SPAC or the Successor Company (as the case may be) and the sponsor must confirm to the Exchange that no preferential treatment has been, nor will be, given to the SPAC Promoter other than the preferential treatment of assured entitlement; and

    (v) The participation is disclosed prominently in the listing document produced for the purpose of the SPAC's listing or the De-SPAC Transaction (as the case may be).

[8] In assessing the above, the Exchange will adopt a holistic approach and take into account factors such as (i) the basis of the opinion, (ii) the negotiated value of the De-SPAC Target as agreed by parties; (iii) the sponsor's opinion; (iv) the amount committed by, and involvement of and validation by the independent third party investors; and (v) the valuation of comparable companies.

X. Forward purchase agreements

25. A SPAC may enter into a forward purchase agreement with the SPAC Promoters or other institutional investors before the initial listing of the SPAC, under which the purchaser would commit to subscribe, and the SPAC would commit to issue, equity in connection with the De-SPAC Transaction at a specified amount. It may also contain an option for the purchaser to subscribe for additional equity up to a specified amount, exercisable at the discretion of the purchaser.

26. As a SPAC Promoter would be a connected person of a SPAC[9], any such forward purchase agreement entered into by the SPAC Promoter or its associate with a SPAC would constitute a connected transaction under the Listing Rules.

27. A SPAC wishing to apply for a modification or waiver of these Listing Rules for the purpose of entering into such a forward purchase agreement before the initial listing must provide the Exchange with full details of the proposed agreement at the earliest opportunity. The Exchange will consider such applications on a case-by-case basis and on the individual merits of each case.

XI. Loans granted by a SPAC Promoter to a SPAC

28. It is common for a SPAC to receive loans from its SPAC Promoter to meet the SPAC's working capital needs, normally through promissory notes.

29. The following table sets out the treatment of loans with terms that permit settlement by issuance of securities:

Terms of the loan	Treatment
Permit settlement (in full or in part) through conversion of the loan into SPAC securities at the discretion of the SPAC or SPAC Promoter	(i) This is prohibited to ensure that a SPAC Promoter is not able to avoid the risk of non-completion of a De-SPAC Transaction that is normally borne by the beneficial owners of SPAC securities.
Permit settlement by the issuance of the securities of the SPAC without discretion of the SPAC or SPAC Promoter	**Application of relevant requirements:** (i) The terms of settlement must comply with all requirements relating to the issue of the relevant SPAC securities (e.g. restrictions on terms and issue price) as set out in MB Chapter 18B[10]. (ii) The SPAC securities to be issued to settle the loan will be counted in the relevant dilution cap[11]. (iii) The SPAC Promoter that will receive the SPAC securities to be issued to settle the loan is required to comply with the conditions set out in paragraph 24 above (if applicable).

9 See MB Rule 18B.01.
10 Including MB Rules 18B.07, 18B.22, 18B.30 and 18B.31.
11 MB Rules 18B.23 (with respect to warrants) and 18B.29 (with respect to Promoter Shares).

30. As a SPAC Promoter is a connected person of a SPAC[12], loans granted by SPAC Promoters to a SPAC would be subject to the connected transaction requirements of MB Chapter 14A:

    (i) If the loan will not be settled by the securities of the SPAC, such a loan will be fully exempt from the connected transaction requirements only if such financial assistance is (a) conducted on normal commercial terms or better; and (b) not secured by the assets of the SPAC[13]; or

    (ii) If the loan will be settled by the securities of the SPAC, such a loan will be subject to compliance with all applicable connected transaction requirements under MB Chapter 14A, including the requirements relating to independent shareholders' approval[14]. The SPAC is also reminded to consider other Listing Rules implications (including those of MB Chapters 13 and 15) in relation to the issuance of such securities.

XII. Additional connected transaction requirements

31. If a De-SPAC Transaction is a connected transaction under MB Chapter 14A, a SPAC must comply with the applicable requirements in MB Chapter 14A as well as the additional connected transaction requirements under MB Rule 18B.56.

32. Where a De-SPAC Transaction constitutes a connected transaction solely by virtue of MB Rule 14A.28, the Exchange will consider waiving the additional requirements under MB Rule 18B.56 provided that (i) all shareholders of the De-SPAC Target are not connected persons of the SPAC and are independent of the SPAC and its connected persons[15]; and (ii) a substantial shareholder of the De-SPAC Target will, as a result of the De-SPAC Transaction, become a controller or an associate of a controller of the Successor Company.

33. For the avoidance of doubt, the Exchange will continue to apply the applicable connected transaction requirements under MB Chapter 14A in such circumstances, and the SPAC must appoint an independent financial adviser to make recommendations to the independent board committee and shareholders on the De-SPAC Transaction. The additional requirements under MB Rule 18B.56 also apply to a De-SPAC Transaction that may confer benefits on connected persons through their interests in the entities involved in the transaction.

XIII. Trustee or custodian

34. MB Rule 18B.17 is to ensure that sufficient protections are placed around the funds raised by SPACs, so that they are available to return to shareholders who choose to redeem their shares or to return to shareholders if and when the SPAC is liquidated. If the funds held in the escrow account are required to be returned to the SPAC shareholders, the trustee/custodian should remit them to the SPAC shareholders directly.

35. A trustee or custodian that operates the escrow account of a SPAC must possess the qualifications and comply with the general obligations[16] below:

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12 MB Rule 18B.01.
13 See MB Rule 14A.90.
14 See MB Rules 14A.36 to 14A.39.
15 The SPAC should confirm that (i) all shareholders of the De-SPAC Target are not connected persons of the SPAC and are independent of the SPAC and its connected persons; and (ii) there is no agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) between any shareholders of the De-SPAC Target and any connected persons of the SPAC with respect to the De-SPAC Transaction.
16 These are consistent with paragraphs 4.5 and 4.6 of Chapter 4 of the Code on Unit Trusts and Mutual Funds, as amended from time to time. For the avoidance of doubt, the obligations set out in paragraph 35 are the only obligations applicable to the trustee or custodian regarding the operation of the escrow account of a SPAC under MB Rule 18B.17.

Qualifications

(i) Accepted by the SFC in respect of existing Collective Investment Schemes authorised by the SFC.

(ii) Based in Hong Kong as the escrow account is required to be domiciled in Hong Kong under MB Rule 18B.16.

(iii) Independent of the SPAC and its connected persons, including the SPAC Promoters.

Obligations

(i) Take into its custody or under its control the property of the SPAC in the escrow account referred to in MB Rule 18B.16 in accordance with MB Rules 18B.16 to 18B.20.

(ii) Register cash and registrable assets in the name of or to the order of the trustee/custodian.

(iii) Be liable for the acts and omissions of nominees, agents and delegates in relation to assets forming part of the property of the SPAC in the escrow account[17].

(iv) For an escrow account to be ring-fenced under MB Rule 18B.16, segregate the property of the SPAC in the escrow account from the property of:

(a) The SPAC and its core connected persons;

(b) The trustee/custodian and any nominees, agents or delegates throughout the custody chain; and

(c) Other clients of the trustee/custodian and nominees, agents or delegates throughout the custody chain, unless held in an omnibus account with adequate safeguards in line with international standards and best practices to ensure that the property of the SPAC in the escrow account is properly recorded with frequent and appropriate reconciliations being performed.

(v) Put in place appropriate measures to verify ownership of the property of the SPAC in the escrow account.

(vi) Take reasonable care to ensure that:

(a) Any payments or distributions from the escrow account are carried out in accordance with MB Rules 18B.19 and 18B.20;

(b) The investment limitations set out in MB Rule 18B.18 (including paragraph 12 of this letter in relation to “cash equivalents”) are complied with; and

(c) The cash flows of the escrow account are properly monitored.

[17] Nominees, agents and delegates can be appointed for the custody and/or safekeeping of the property of the SPAC in an escrow account as long as these entities are subject to prudential regulation and supervision by authorities such as The Hong Kong Monetary Authority. Such nominees, agents or delegates can be unaffiliated with the trustee/custodian.

	(vii) Exercise reasonable care, skill and diligence in the selection, appointment and ongoing monitoring of any nominees, agents and delegates appointed for the custody and/or safekeeping of the property of the SPAC in the escrow account; and be satisfied that the nominees, agents and delegates retained remain suitably qualified and competent on an ongoing basis to provide the relevant services. (viii) Exercise due skill, care and diligence in discharging its obligations and duties appropriate to the nature of the escrow account. (ix) Establish clear and comprehensive escalation mechanisms to deal with potential breaches detected in the course of discharging its obligations and report material breaches[18] to the Exchange in a timely manner. (x) Update the SPAC and report to the Exchange (either directly or via the SPAC) any material issues or changes that may impact its eligibility/capacity to act as a trustee/custodian of the escrow account.
Change of trustee/ custodian 	(i) A SPAC must appoint a new trustee/custodian as soon as possible (in any case, no later than one month) after it becomes aware that the existing trustee/custodian is or will become ineligible to act as a trustee/custodian for the escrow account for the purpose of MB Rule 18B.17. (ii) The appointment of a new trustee/custodian must be subject to the prior approval of the Exchange. (iii) A trustee/custodian must not retire except upon the appointment of a new trustee/custodian. The retirement of the trustee/custodian should take effect at the same time as when the new trustee/custodian takes up office.
Undertaking 	(i) Prior to its appointment, a trustee/custodian must enter into an undertaking with the Exchange to comply with the "Obligations" section and point (iii) under "Change of trustee/custodian" section in this table.

[18] The trustee/custodian is expected to inform the Exchange promptly of any material breach of the Listing Rules and this letter in relation to the operation of the escrow account that has come to its knowledge, which has not been otherwise reported to the Exchange by the SPAC. An example of "material breach" includes acquisition of securities which fall outside the scope of cash equivalents for the purpose of MB Rule 18B.18 as set out in paragraph 12 of this letter.

Special Purpose Acquisition Companies

SPAC Promoter structures

1. If SPAC Promoter A holds the Promoter Shares through a special purpose vehicle (SPV), should the SPV itself also be regarded as a SPAC Promoter?

No, as long as the SPV's sole purpose is to hold Promoter Shares on behalf of SPAC Promoter A (as permitted under the Note to MB Rule 18B.27).

The SPV is expected to give an undertaking to the Exchange and the SPAC that so long as it has any direct or indirect interest in any Promoter Shares and/or Promoter Warrants, it will comply with the provisions of the Listing Rules which apply to SPAC Promoter A.

MB Rule 1.01, 18B.26 and 18B.27
First released: September 2022; last updated: May 2024

2. Should an entity be regarded as a SPAC Promoter if it controls the beneficial ownership of Promoter Shares? If so, should all levels in the control chain be regarded as a SPAC Promoter, or are SPACs permitted to identify which entity it believes should be treated as a SPAC Promoter within the control chain?

In general, holding a controlling stake in an identified SPAC Promoter in itself would not result in that controlling shareholder being regarded as a SPAC Promoter. A SPAC should identify the entities in its shareholding structure that should be regarded as SPAC Promoters for the purpose of the Listing Rules, and such entities must satisfy the suitability and eligibility requirements set out in MB Rule 18B.10.

In addition, according to MB Rule 18B.27, a SPAC must only allot, issue or grant Promoter Shares or Promoter Warrants to a SPAC Promoter, which may hold these securities through SPVs. As such, a SPV holding Promoter Shares on behalf of a SPAC Promoter should not have any minority shareholders who are not SPAC Promoters.

SPAC Promoters and SPVs holding Promoter Shares and Promoter Warrants should undertake to the Exchange and the SPAC that they will comply with the relevant provisions of the Listing Rules for so long as they hold any direct or indirect interests in any Promoter Shares and/or Promoter Warrants.

MB Rule 1.01, 18B.10, 18B.26 and 18B.27
First released: September 2022; last updated: May 2024

3. Can multiple SPAC Promoters beneficially own Promoter Shares through a common SPV?

Yes. The Exchange may impose additional conditions on the multiple SPAC Promoters having regard to the specific facts and circumstances of each case, for example, any departure or change in shareholding by the multiple SPAC Promoters in the common SPV will be regarded as a material change of SPAC Promoter under MB Rule 18B.32.

MB Rule 1.01, Note 1 to 18B.32
First released: September 2022; last updated: May 2024

4. Can a SPAC Promoter set up a trust to hold part of its Promoter Shares for the purpose of an equity incentive plan to benefit the SPAC Promoter's nominated SPAC Directors and certain of its other senior management and employees (Plan Participants)? If not, would this be permissible if the Plan Participants only received SPAC Shares that result from the conversion of the Promoter Shares following a De-SPAC Transaction and the listing of the Successor Company?

No. The proposed equity incentive arrangement would circumvent the requirement of MB Rules 18B.26 to 18B.27 that Promoter Shares must only be granted to SPAC Promoters. Also, the Plan Participants will not have made a corresponding economic contribution to justify the grant of Promoter Shares to them.

The grant of SPAC Shares (converted from Promoter Shares) to Plan Participants would also be prohibited as this would represent only a difference in the form in which the benefit is granted and would not change the fact that the Plan Participants: (a) are not SPAC Promoters; and (b) did not contribute commensurate "capital at risk" to be entitled to the benefits of the Promoter Shares.

MB Rule 18B.26 and 18B.27
First released: September 2022; last updated: May 2024

Disclosure of SPAC Promoters' investment management experience

5. To what extent the investment experience of a SPAC Promoter should be disclosed in the listing document under MB Rule 18B.10 and paragraph 6 of Chapter 2.4 of the Guide for New Listing Applicants (Guide)?

The sponsor(s) and the applicant should take into account the following when disclosing the investment experience of a SPAC Promoter:

- A balanced and fair view should be presented, instead of cherry picking of information (e.g. only disclosing the relevant funds' performance over a particular investment period in which the funds have better performance, or disclosing the performance of selected funds with positive returns and omitting those funds with negative returns);

- Fund performance (e.g. internal rate of return (IRR), multiple on invested capital (MOC), distributions to paid-in capital (DPI) for private equity funds) should be presented on a year-to-year basis, specifying the launch date of each fund. When comparing the funds' performance with industry performance indexes, comparison should be made on a year-to-year basis over the same investment period; and
- For private equity funds, where the fund portfolio includes realised and unrealised/partially realised positions, disclosure should include the relative size of the respective positions and their valuation methods and their respective time of investment and divestment.

MB Rule 18B.10, HKEX-GL113-22
First released: September 2022; last updated: May 2024

Funding of a SPAC's expenses

6. Is it acceptable for the funding for SPAC expenses to be separated from the obligations of a SPAC Promoter? For example, can a SPAC be established by a group that obtains the funding for its expenses from an affiliate within the group that is not a SPAC Promoter?

No. A SPAC Promoter must incur all (or a pro rata portion of) the expenses to establish and maintain a SPAC. SPAC Promoters should regard this as their "capital at risk" to help ensure that their interests are aligned with the interests of SPAC shareholders, and such expenses should therefore not be recoverable if a De-SPAC Transaction is not completed.

The amount provided by a SPAC Promoter to fund the SPAC's expenses should also be commensurate with its beneficial interest in the Promoter Shares.

A SPAC Promoter can obtain a loan from its affiliate or use a capital contribution from its own shareholders (if any) to fund a SPAC's expenses. However, the entities granting the loans or injecting capital to the SPAC Promoter should not have any rights to request repayment of the loan from, or make any claims against, the SPAC.

MB Rule 18B.10
First released: September 2022; last updated: May 2024

SFC licensed SPAC Promoter

7. Will the requirement for the SFC-licensed SPAC Promoter to hold at least 10% of the Promoter Shares be satisfied if it has only voting control of a 10% (or more) interest in the SPAC's Promoter Shares without a commensurate beneficial economic interest in the Promoter Shares?

No. The SFC-licensed SPAC Promoter must have a corresponding economic interest to help ensure that its interests are aligned with the interests of SPAC shareholders.

MB Rule 18B.10 and 18B.11
First released: September 2022; last updated: May 2024

8. If a SPAC has multiple SPAC Promoters, must the SFC lisenced SPAC Promoter(s) have relevant management/investment experience (required by paragraph 6 of GL113-22) or is it sufficient for other SPAC Promoter(s) to meet this requirement?

The Exchange takes a holistic approach in determining the suitability and eligibility of SPAC Promoter.

For example, if the key SPAC Promoter (e.g. holding a significantly large and dominant interest in the Promoter Shares) has demonstrated extensive management/investment experience, while the SFC licensed SPAC Promoter holding a minority interest in the Promoter Shares has a relatively short operating history with a strong management team, the Exchange will consider all the relevant information, including the experience and competence of the board/management of the SPAC Promoters.

The Exchange might impose additional conditions on the SFC licensed SPAC Promoter, for example, any departure of the responsible officer with relevant management/investment experience from the SFC licensed SPAC Promoter will be regarded as a material change in SPAC Promoter under MB Rule 18B.32.

MB Rule 18B.10(1), 18B.32, HKEX-GL113-22
First released: September 2022; last updated: May 2024

Independence of independent non-executive directors

9. Can a SPAC issue SPAC Shares at nil consideration for the purpose of remunerating the independent non-executive directors (INEDs)?

No. Subject to the provisions under MB Rule 3.13, an INED of a SPAC may subscribe for SPAC Shares with his own resources, provided that the INED is a Professional Investor.

MB Rule 3.13 and 18B.07
First released: September 2022; last updated: May 2024

Obligations of a trustee/custodian regarding the operation of the escrow account of a SPAC

10. What is the obligation of the SPAC and/or trustee/custodian in terms of managing the total value of cash or cash equivalents held in the escrow account, in particular, in circumstances of market movements or currency fluctuation?

Under the note to MB Rule 18B.18, upon listing of the SPAC, it is the SPAC's responsibility to ensure that funds are held in a form that allows them to meet the requirement to give full redemption to its shareholders under MB Rules 18B.57 and 18B.74. This generally includes proper management of any exposure to:

(i) currency fluctuations, for example, minimising conversion of the proceeds raised to other currencies; and

(ii) market condition related risk, for example, ensuring compliance with the requirements on "cash and cash equivalents" under MB Rule 18B.18 and the Guidance Letter HKEX-GL113-22.

MB Rule 18B.18, 18B.57 and 18B.74
First released: September 2022; last updated: May 2024

Other matters

11. Can a trustee accepted by the SFC as a trustee of a REIT be considered as having the qualifications required under MB Rule 18B.17?

The Exchange will take a case-by-case approach to determine whether a trustee or custodian would be considered as having the qualifications required under MB Rule 18B.17.

Further, item (i) under "Qualification" in paragraph 35 of Chapter 2.4 of the Guide provides that a trustee or custodian that has already been accepted by the SFC in respect of existing Collective Investment Schemes authorised by the SFC will be considered as having the qualifications required under MB Rule 18B.17. Generally, a custodian/trustee that has been accepted by the SFC in respect of a REIT authorised by the SFC will be considered as having the qualifications required under MB Rule 18B.17.

MB Rule 18B.17
First released: September 2022; last updated: August 2024

12. Would the independence of third party investors who invest in a De-SPAC Transaction be affected by: (i) the third party investor having participated in the initial offering of the SPAC; or (ii) co-investments with a SPAC Promoter in transactions unrelated to the SPAC or the De-SPAC Transaction?

(i) Subject to the independence requirements set out in paragraph 15 of Chapter 2.4 of the Guide being met and absent other factors, an investor who has participated in the SPAC's initial offering would be allowed to invest in a De-SPAC Transaction if the conditions for placing shares to existing shareholders as set out in paragraph 13 of Chapter 4.15 of the Guide are met.

(ii) Participation in co-investments would not normally, by itself, result in a failure to meet the independence requirement. However, the Exchange retains the discretion to deem any investor to be not independent based on the facts and circumstances of an individual case.

MB Rule 13.84(4) and 18B.40
First released: September 2022; last updated: August 2024

13. The Fees Rules state that the initial listing fee for a new applicant must be calculated on the basis of the "monetary value of the equity securities to be listed". Should the applicant assume that the SPAC Warrants have a monetary value of zero for the purpose of calculating this fee?

The monetary value of SPAC Warrants will be zero if there is no issue price. Accordingly, the initial listing fee for SPAC Warrants will be HK$150,000 based on the Fees Rules.

MB Fees Rules paragraph 1
First released: September 2022; last updated: May 2024

Guidance on disclosure by management companies of SFC-authorised Exchange Traded Funds

The Exchange and the Securities and Futures Commission jointly issued a "Circular to Management Companies of SFC-authorised Exchange Traded Funds ("ETFs")(Revised as of 1 January 2024)" to assist management companies of ETFs to comply with the disclosures obligations under the Code on Unit Trusts and Mutual Funds and the Listing Rule requirements for collective investment schemes. The circular is reproduced below.

Appendix

SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

HKEX
香港交易所

Revised as of 1 January 2024

Circular to Management Companies of SFC-authorised Exchange Traded Funds ("ETFs")[1]

List of Potential Events Triggering Ongoing Disclosure

1. Under 11.1B of the Code on Unit Trusts and Mutual Funds ("UT Code"), management companies should provide holders with reasonable prior notice, or inform holders as soon as reasonably practicable of any information concerning the scheme which is necessary to enable holders to appraise the position of the scheme.

2. Under Appendix E3 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules"), a scheme shall inform the Exchange immediately of, among other things, any other information necessary to enable the holders of interests to appraise the position of the scheme and to avoid the establishment of a false market in the interests of the scheme.

3. To assist management companies of ETFs to comply with the disclosure obligations under the UT Code and Listing Rules and without prejudice to the notification obligation under 11.1A of the UT Code, the following are non-exhaustive examples of events that may trigger the above on-going disclosure requirements where any of them would have a **material** impact on an ETF:

   (a) Changes falling within 11.1 or 11.1B of the UT Code;

   Note: This includes, for example, changes in the replication strategy of the ETF; changes in the collateral policy from that disclosed in the offering document of the ETF; and changes in the financial conditions or the regulatory status of the key operators of the ETF.

   (b) Filing of winding up petitions, the issuing of winding up orders or the appointment of receivers or provisional liquidators, or the institution of disciplinary proceedings in respect of its licence or registration to conduct any regulated activity, or proceedings analogous to the above, against any of the trustee, custodian, or management company;

   (c) Replacement of the underlying index or indices, or changes of the index calculation methodology;

   (d) Litigation brought against the ETF or any of the trustee, custodian, or management company;

   (e) Where the ETF adopts a synthetic replication strategy:

[1] Unless otherwise specified, the term "ETF" used in this circular shall cover passive ETF, active ETF, leveraged product, inverse product and fund with listed share class.

1

SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

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(i) default of any derivative instruments held by the ETF,

(ii) filing of winding up petitions, the issuing of winding up orders or the appointment of receivers or provisional liquidators against any derivative counterparty or guarantor of such counterparty, or

(iii) any material adverse change in the financial conditions or business of any derivative counterparty or guarantor of such counterparty;

Note: This may, for example, include any credit downgrade or any change in the concentration of the default risks of the counterparties to products used by the derivative counterparty or its guarantor that could result in a material adverse change in the financial conditions or business of such derivative counterparty or guarantor of the ETF.

(f) The cessation of market making activity (including the resignation of the last market maker) for units (traded in any counter) of the ETF;

(g) Suspension of creation and / or redemption of units in the ETF;

(h) Changes in tax or regulatory requirements that may impact upon the net asset value of the ETF; or

(i) Material breaches of the constitutional documents of the ETF.

4. Please note that the obligations to disclose information depend upon the facts of each case and as the management company of the ETF, you have the duty and should make your own judgements as to what and when such information is required to be disclosed. The above examples are not meant to be exhaustive.

5. You are welcome to contact the relevant case officer of the SFC and the HKEX should you have any questions on the above.

Investment Products Division
Securities and Futures Commission

Listing Division
The Stock Exchange of Hong Kong Limited

Guidance on authorised collective investment schemes

I. Purpose

1. This letter provides guidance for authorised collective investment schemes (**CIS**) under MB Chapter 20. The guidance is also set out in Chapter 5.2 of the Guide for New Listing Applicants.

2. The SFC is the primary regulator for CIS including (i) authorisation of CIS and their offering documents in accordance with the applicable laws and regulations; and (ii) monitoring compliance with these authorisation conditions and applicable requirements.

3. The Exchange's primary role in CIS regulation is to maintain a fair, orderly and efficient market in the trading of CIS in accordance with the Listing Rules and the applicable trading rules of the Exchange.

II. Appointment of listing agent and other intermediaries

4. The listing agent must demonstrate that it has relevant experience handling a CIS listing application. The CIS Operator, or other qualified persons (e.g. legal advisers, financial advisers or persons with appropriate licences under the SFO) with the relevant experience who are authorised by the CIS Operator to handle the authorisation and listing process are normally acceptable to the Exchange to act as a listing agent.

5. Where the CIS applicant conducts an IPO of its CIS interests, or in other circumstances as the Exchange or the SFC may otherwise determine, the Exchange will require a listing agent to have all the necessary licences and qualifications to oversee the management of the listing process as required under MB Rule 20.06(2)(a) to (e).

6. According to the Code on Real Estate Investment Trusts, the listing agent for a new REIT applicant is in effect assuming the responsibilities of, and discharging a function no different from, the sponsor of an IPO. Accordingly, where the CIS applicant is a REIT or where the Exchange or the SFC may otherwise requires, the listing agent must have the requisite licences and qualifications to act as a sponsor.

7. Under MB Rule 20.23A, in the case of offerings involving bookbuilding activities (as defined under the Code of Conduct) of interests in a REIT by a new REIT applicant or an existing authorised REIT, MB Chapter 3A and other Listing Rules provisions relating to sponsor-overall coordinator (**OC**), OC and other capital market intermediaries shall apply. A CIS applicant involved in such an offering must therefore appoint at least one sponsor-OC in compliance with MB Rule 3A.43, and where a CIS applicant appoints any other OC or capital market intermediary, the relevant requirements under MB Chapter 3A shall also apply.

III. Early consultation with HKSCC for applications involving foreign elements

8. CIS applicants who are applying to list CIS interests in the form of (i) an entity incorporated outside of Hong Kong; or (ii) a trust organised under any law other than Hong Kong law, or other contractual form, the terms and conditions of which are governed by any law other than Hong Kong law, are encouraged to consult HKSCC in advance. The process for review by HKSCC will take time depending on the complexity of the issues raised. The consultation should be addressed to: Manager, Stock Admission, 30/F, One Exchange Square, 8 Connaught Place, Central, Hong Kong, and with a copy to Co-Heads of IPO Vetting, 12th Floor, Two Exchange Square, 8 Connaught Place, Central, Hong Kong.

9. The CIS applicants should satisfy HKSCC that:

   (i) The laws of the relevant jurisdiction to which such securities/interests/instruments are subject to (which govern the creation of such securities/interests/instruments) recognise the concept of beneficial ownership under the existing custody structure operated by HKSCC and the transfer of such beneficial interests as envisaged under the CCASS Rules such that CCASS clearing participants transacting in and custodying such securities/interests/instruments on behalf of their clients are able to acquire proprietary interests in such securities/interests/instruments;

   (ii) All perfection requirements in the relevant jurisdictions (if any) can be complied with by CCASS clearing participants as the CCASS Rules envisage that clearing participants may provide such securities/interests/instruments as collateral for their exchange transactions in satisfaction of their margin requirements;

   (iii) There are no other legal or regulatory implications arising from the clearing and custody of such securities/interests/instruments by or on behalf of HKSCC which may have an impact on the performance of HKSCC's role as a central clearing counterparty and central securities depository in accordance with the CCASS Rules; and

   (iv) There are no other issues which may have a legal or regulatory impact on The Stock Exchange of Hong Kong Limited as a legal entity.

10. The Exchange expects CIS applicants to provide a formal legal opinion addressed to, and which may be relied upon by, HKSCC which addresses the issues set out in paragraphs 9(i) and (ii) above.

IV. Publication of Application Proof (**AP**) and Post-hearing Information Pack (**PHIP**)

11. Where a CIS applicant's listing agent is required to discharge functions equivalent to those of a sponsor, the applicant is required to publish an AP and a PHIP in accordance with MB Rules 20.25 and 20.26, respectively.

V. Application process

12. Following acceptance of a new listing application, the Exchange will issue a letter to notify the CIS applicant of the stock code allocation arrangements. The drawing of the stock code can take place prior to the issue of the approval-in-principle letter (**AIP**) and a confirmation of the stock code will be issued when the Exchange issues the AIP. An AIP should be issued within five clear business days if all documentation is in order and there are no material comments.

13. Where there is an IPO and the CIS applicant and its listing agent outsource the process of reviewing the application forms for the subscription of CIS interests to a third party service provider (e.g. a share registrar), the CIS applicant and its listing agent must discuss with the service provider the reasonable steps to identify and reject multiple or suspected multiple applications. Outsourcing to a third party service provider would not release the CIS applicant or the listing agent from their responsibilities to identify and reject multiple or suspected multiple applications.

VI. Documentary and administrative requirements

14. The documentary and administrative requirements are set out in MB Rules 20.14, 20.15, 20.17, 20.25 and 20.26 (where applicable) as well as the checklists and forms available on the Exchange's website. The following table sets out additional documentary and administrative matters during the application process (unless otherwise specified, the documents should be in text searchable PDF format and submitted through HKEX-ESS):

Stages	Requirements
Before Form A2 submission	(i) A listing agent must register as a HKEX-ESS user at least three business days before any submission or publication of documents through HKEX-ESS. (ii) A listing agent who is required to discharge the functions of a sponsor must submit a sponsor engagement letter. (iii) A listing agent must obtain a company case number (Form CN001 (CIS)) from the Listing Division – IPO Vetting Department, at least one business day before filing the SFC authorisation application to the Exchange. (iv) Submit Form A2 (e-Form CIS002[1]) through HKEX-ESS in advance of the expected filing date. The Exchange will only accept a scanned copy of the completed and signed version as the final listing application form.

[1] e-Form CIS002 "Listing Application Form".

<table>
<tr><th>Stages</th><th>Requirements</th></tr>
<tr><td>At the time of Form A2 submission</td><td>(i) Initial listing fee should be deposited/transferred to the Exchange's designated bank accounts by cheque, electronic transfer or Faster Payment System (FPS). The payment record (i.e. the scanned/ electronic copy of cheque, bank-in slip and/or bank transfer confirmation) should be uploaded to the HKEX-ESS:

<table>
<tr><th>Payment</th><th>Details</th></tr>
<tr><td>Cheque</td><td>Name of Payee: The Stock Exchange of Hong Kong Limited
Bank: Hang Seng Bank Limited
Account no.: 262-008113-001</td></tr>
<tr><td>Electronic Transfer</td><td>Bank account number: 024-262-008113-001
Account name: The Stock Exchange of Hong Kong Limited
Bank: Hang Seng Bank Limited
Bank address: 83 Des Voeux Road Central Hong Kong
Swift code (for non-local transfer only): HASEHKHH</td></tr>
<tr><td>FPS</td><td>FPS email address: sedn@hkex.com.hk</td></tr>
</table></td></tr>
<tr><td>At least 4 clear business days before the expected date of issue of the approval-in-principle letter by the SFC</td><td>(i) In case of a placing involving bookbuilding activities (as defined under the Code of Conduct) in connection with a new listing, information under MB Rule 9.11(23a).</td></tr>
<tr><td>On or before the issue of the listing document</td><td>(i) A listing agent's letter or email notifying the Exchange if the CIS applicant will not adopt the standard transfer form.</td></tr>
<tr><td>After the issue of the listing document but before dealings commence</td><td>(i) Submit a "ready-to-publish" electronic copy of the CIS Disclosure Document for publication through HKEX-ESS.

For CIS applicant with IPO:

(ii) Submit a "ready-to-publish" electronic copy of any application form for the subscription of CIS interests (in sample format) for publication through HKEX-ESS. A "SAMPLE" watermark (i.e. ghost text) or text to like effect should be printed on each page of the electronic copy of the application form.

(iii) A draft allotment results for vetting according to the e-Submission System User Manual which should include "Search by Identity Card" function if the CIS applicant proposes to raise HK$1.5 billion or more in the Hong Kong offering.

(iv) Relevant placee information and marketing statement in specified forms.

(v) Receiving banks' staffs should be made aware that potential investors are permitted to obtain both English and Chinese versions of the CIS Disclosure Document during the offer period.</td></tr>
</table>

VII. Stamp duty remission

15. With effect from February 2015, stamp duty is waived for the transfer of units of all Exchange Traded Funds (**ETF**), regardless of their underlying portfolios, dates of listings or whether stamp duty has been remitted in respect of them. Procedures to facilitate CIS applicants to obtain the stamp duty remission are not necessary.

VIII. Post-listing requirements

Listing of additional interests after listing

16. Close-ended listed CIS issuers (e.g. REIT) must submit a listing application to the Exchange as required under MB Rule 20.15. This requirement does not apply to an open-end listed CIS issuer (e.g. ETF) as listing approval granted at the time of new listing covers any additional interests it may issue after listing.

Change in trading arrangements

17. A listed CIS issuer should consult the Exchange on any proposal to change its arrangements for trading in its interests on the Exchange (e.g. a consolidation or subdivision of the CIS interests in the form of units). It should agree its proposed change and timetable with the Exchange before it announces the proposal.

15

Spin-offs

Guidance to issuers contemplating (i) a spin-off and separate listing of businesses or assets on the Exchange; or (ii) a reverse takeover where the issuer is deemed a new listing applicant

A. Purpose

1. This letter provides guidance to issuers contemplating (i) a spin-off to effect a separate listing of businesses or assets on the Exchange; or (ii) a reverse takeover where the issuer is deemed a new listing applicant. In these circumstances, the issuer group (or the enlarged group) may have to fulfil both requirements applicable to listed issuers and to new applicants under the Listing Rules.

B. Background

2. Practice Note 15 of the Main Board Rules (Practice 3 to the GEM Rules) sets out the principles that an issuer should comply when proposing a spin-off of its businesses or assets. Where the company to be spun-off (**Newco**) is to be listed on the Exchange, it must satisfy all the new listing requirements under the Listing Rules.

3. Under Chapter 14 of the Main Board Rules (Chapter 19 of the GEM Rules), an issuer proposing a reverse takeover will be treated as if it were a new listing applicant (**Deemed New Applicant**).

4. Under Chapter 9 of the Main Board Rules (Chapter 12 of the GEM Rules), the Application Proof submitted by a new listing applicant must be substantially complete. The Application Proof must be posted on the Exchange's website at the same time the new listing applicant files its listing application with the Exchange.

C. Guidance

Spin-off

5. In a spin-off, the issuer must comply with Practice Note 15 and the continuing listing obligations under the Listing Rules, and Newco must also meet new listing requirements. Where there are ongoing relationships/transactions between the two entities, issues may arise relating to potential conflicts between interests of the two groups of shareholders. The issuer should give due consideration to these conflict issues, and resolve the matters before it submits the Application Proof.

6. The following are examples of conflicts issues commonly found in new listing application of Newco:

   - competition, including the degree of overlapping business with its parent company and clear business delineation with its parent company;
   - reasons for exclusion of overlapping business of its parent company;
   - extent of future potential/actual competition with its parent company;
   - corporate governance measures to manage future potential/actual conflicts with its parent company; and
   - how the listing applicant can function independently of its parent company including management, operational and financial independences.

7. Under Practice Note 15, an issuer must submit its spin-off proposal to the Exchange for approval. After receipt of the spin-off proposal, the Exchange will comment on the issuer's compliance with the Listing Rules. Where necessary, Newco should make a pre-IPO enquiry to address its position on compliance with the new listing requirements.

8. The Exchange will approve the spin-off proposal after these compliance issues have been addressed. However, Newco's new listing application will be subject to review by the Exchange and approval by the Listing Committee and this approval may or may not be granted.

Reverse takeovers

9. In the case of reverse takeovers, the issuer must ensure that the assets to be acquired must meet the suitability requirement and the track record requirements for a new listing and the enlarged group must meet all the new listing requirements (except the track record requirements) under the Listing Rules (see Main Board Rule 14.54(1)/GEM Rule 19.54(1)). Under Main Board Rule 14.54(2) (GEM Rule 19.54(2)), where the issuer has failed to comply with Main Board Rule 13.24(1) (GEM Rule 17.26(1)), the acquisition targets must also meet the sufficient public interest requirement for a new listing. Since the Application Proof must be substantially complete, the Deemed New Applicant should make pre-IPO enquiries on any issues relating to its compliance with the new listing requirement before submission of the Application Proof (see paragraph 6 above for examples of potential issues).

Whether a listed issuer's proposal for its subsidiary to seek admission of shares to trading on an overseas over-the-counter securities exchange constituted a spin-off under Practice Note 15

Parties

- **Company A** – a Main Board issuer
- **Company B** – Company A's non wholly owned overseas subsidiary

Facts

1. Company B proposed to seek admission of its shares to trading on an overseas over-the-counter securities exchange. Company A inquired as to the applicability of Practice Note 15 to the proposal.

2. Company A submitted that Practice Note 15 was not applicable to the proposal on the basis that Company B was only seeking admission to trading on an overseas over-the-counter securities exchange, not a full listing on the main board of an overseas stock exchange.

Analysis

3. Company A needed to place down its interest in Company B in order for Company B to meet the public float requirement of the overseas over-the-counter securities exchange. As such, there would be a dilution of Company A's interest in Company B. In light of this, the proposed application for admission to trading on the overseas over-the-counter securities exchange by Company B should be considered a separate listing elsewhere of businesses within the existing group of Company A and therefore subject to Practice Note 15 of the Listing Rules.

Conclusion

4. Practice Note 15 of the Listing Rules applied. The Company was to submit a spin-off proposal for approval by the Listing Committee.

Whether a listed issuer's proposal for its overseas listed subsidiary to seek a dual listing on the Exchange constituted a spin-off under Practice Note 15

Parties

- **Company A** – a Main Board issuer
- **Company B** – Company A's subsidiary, with its shares listed on an overseas stock exchange

Facts

1. Company A was conducting one of its principal businesses through Company B.

2. Company B's shares had been listed on an overseas stock exchange for some years. Company A had complied with Practice Note 15 when it spun off Company B for listing on the overseas stock exchange.

3. Company B proposed to list its shares on the Main Board through a global offering of some new shares. After that, its shares would be dually listed on the Main Board and the overseas stock exchange.

4. There was a question whether the proposed listing of Company B on the Main Board was a "spin-off" by Company A subject to the requirements of Practice Note 15.

Relevant Listing Rules

5. Paragraph 2 of Practice Note 15 states that:

   This Practice Note is intended to set out the Exchange's policy with regard to proposals submitted by issuers to effect the separate listing on the Exchange or elsewhere of assets or businesses wholly or partly within their existing groups ("spin-off"). …

Analysis

6. Practice Note 15 applies to an issuer's proposal to effect a separate listing of its group's assets or businesses, whether the listing is on the Exchange or elsewhere.

7. Here, Company B was spun off by Company A under Practice Note 15 some time ago and had since then been listed on the overseas stock exchange. While the current proposal would achieve a listing of Company B on the Main Board, Company A would not be required to re-comply with Practice Note 15.

Conclusion

8. Practice Note 15 would not apply to the proposal.

Whether a listed issuer's proposal to spin-off its core business for listing in the PRC was subject to Practice Note 15 if the proposed spin-off was conditional on the withdrawal of listing of the issuer from the Main Board and its new listing on GEM

Parties

- **Company A** – a Main Board issuer, incorporated overseas
- **Company B** – a company listed on a Mainland stock exchange

Facts

1. Company A proposed to:

   a. sell its main business (**Business**) to Company B in exchange for a controlling interest in Company B (**Disposal**). This would be a very substantial disposal. After the Disposal, Company A would hold Company B as a subsidiary; and

   b. withdraw its listing from the Main Board under Rule 6.12 and list its shares on GEM.

   These arrangements would be inter-conditional.

2. Company A submitted that the purpose of the Disposal was to achieve a listing of the Business on the Mainland stock exchange.

3. After the Disposal, it would operate the Business through Company B and retain another business (**Remaining Business**). The Remaining Business, acquired by Company A about a year ago, was substantially smaller than the Business.

4. Company A acknowledged that the Disposal was a spin-off under PN15. The Remaining Business could not meet the profit requirements under Rule 8.05 and therefore paragraph 3(c) of PN15.

5. However, Company A considered that PN15 should not apply in this case because it would cease to be a Main Board issuer upon completion of the proposal.

Relevant Listing Rules

6. Rule 6.12(4) states that subject to Rule 6.15, if an issuer has no alternative listing under 6.11, it may not voluntarily withdraw its listing on the Main Board without the Exchange's permission unless:

   the shareholders and holders of any other class of listed securities, if applicable, other than the directors (excluding independent non-executive directors), chief executive and controlling shareholders, are offered a reasonable cash alternative or other reasonable alternative.

7. Paragraph 2 of PN15 states that:-

   … This Practice Note sets out the principles which the Exchange applies when considering spin-off applications. Issuers are reminded that they are required to submit their spin-off proposals to the Exchange for its approval. …

8. Paragraph 3(c) of PN15 states that:-

   The Listing Committee must be satisfied that, after the listing of Newco, the Parent would retain a sufficient level of operations and sufficient assets to support its separate listing status. In particular, it would not be acceptable to the Listing Committee that one business (Newco's) supported two listing statuses (the Parent's and Newco's). In other words, the Parent itself would be required to retain, in addition to its interest in Newco, sufficient assets and operations of its own, excluding its interest in Newco, to satisfy independently the requirements of Chapter 8 of the Exchange Listing Rules.

Analysis

9. The Disposal was a spin-off under PN15. Company A, as a Main Board issuer, was required to submit its spin-off proposal to the Exchange for approval despite its intended withdrawal of listing. It had to satisfy the Exchange at the time of its spin-off application that it could comply with all the requirements in PN15. However, Company A was unable to do so.

10. The reason for Company A's proposal to withdraw its listing from the Main Board and apply for a listing on GEM was to facilitate a spin-off without complying with the PN15 requirements. The Exchange considered this unacceptable and had a concern about the company's suitability for listing on GEM.

Conclusion

11. PN15 applied to Company A's proposal and the Exchange did not consider the proposal acceptable.

Whether a listed issuer's remaining business in securities investment and securities trading could meet the new listing requirements after the proposed spin-off

Parties

- **Company A** – a Main Board issuer
- **Company B** – a Main Board issuer in which Company A had a significant investment
- **Newco** – Company A's subsidiary wishing to seek a separate listing on the Exchange

Facts

1. Company A proposed to inject its business in manufacturing and sale of certain electronic products into Newco and seek a separate listing of Newco on the Exchange.

2. After the proposed spin-off, Company A (excluding Newco) (**Remaining Group**) would continue to carry on the business in securities investment and trading (**Securities Business**) and a number of other businesses (**Other Businesses**) (together, **Remaining Businesses**).

3. Company A submitted that during the immediately preceding 3 year (track record) period, the Remaining Group recorded an aggregated profit of about HK$150 million for the first two years of the track record period, and a profit of about HK$300 million for the latest financial year.

4. It was also noted that:

   (a) During the immediately preceding 3 year (track record) period, the Securities Business was the largest business segment of the Remaining Group in terms of revenue, profit and asset value. Its investment portfolio comprised primarily securities in Company B (which was a subsidiary of Company A until about three years ago). It also held a few other investments but the investment amounts were small.

   (b) The Remaining Group's revenues and profits during the track record period were mainly attributable to the gains derived from the investment in Company B in the last two financial years. The Other Businesses segments were small and were either loss-making or had only generated minimal profits.

   (c) Company A had sold all its investment in Company B during the track record period. The value of its investment portfolio therefore decreased significantly from about HK$10 billion to less than HK$20 million.

(d) After the track record period, Company A had made further investments in two listed companies with an aggregated value of HK$10 million. It also set aside a budget of HK$300 million for future investments.

5. Company A was of the view that the Remaining Group could independently satisfy the new listing requirements of Chapter 8 of the Rules, including the profit requirement of Rule 8.05(1)(a), and other requirements under Practice Note 15. It sought the Exchange's approval for the spin-off proposal.

Relevant Listing Rules

6. Rule 8.04 states that:

"Both the issuer and its business must, in the opinion of the Exchange, be suitable for listing."

7. Rule 2.06 states that:

"Suitability for listing depends on many factors. Applicants for listing should appreciate that compliance with the Exchange Listing Rules may not of itself ensure an applicant's suitability for listing. The Exchange retains a discretion to accept or reject applications and in reaching their decision will pay particular regard to the general principles outlined in rule 2.03. Prospective issuers (including listed issuers) are therefore encouraged to contact the Exchange to seek informal and confidential guidance as to the eligibility of a proposed application for listing at the earliest possible opportunity."

8. Paragraph 3(c) of Practice Note 15 to the Main Board Rules states that:

"The Listing Committee must be satisfied that, after the listing of Newco, the Parent would retain a sufficient level of operations and sufficient assets to support its separate listing status. In particular, it would not be acceptable to the Listing Committee that one business (Newco's) supported two listing statuses (the Parent's and Newco's). In other words, the Parent itself would be required to retain, in addition to its interest in Newco, sufficient assets and operations of its own, excluding its interest in Newco, to satisfy independently the requirements of Chapter 8 of the Exchange Listing Rules..."

Analysis

9. Rule 8.04 provides that both the issuer and its business must, in the Exchange's opinion, be suitable for listing. Rule 2.06 further states that suitability for listing depends on many factors. Compliance with the Rules may not of itself ensure an issuer's suitability for listing / continued listing.

10. Suitability is a broad and flexible concept that applies in a wide range of circumstances. The Exchange has a broad discretion to interpret and apply this concept for maintaining market confidence with reference to the currently acceptable standards in the market place. This facilitates the Exchange to meet its regulatory objectives and its obligations to act in the best interest of the market as a whole and in the public interest.

11. For example, the Exchange may question an issuer's suitability for listing if, given its specific business model and the specific facts and circumstances, the issuer may not be operating a business of substance, giving rise to a concern that the issuer is carrying on its activities for the purpose of maintaining a listing status rather than genuinely developing its underlying business. In these circumstances, the issuer may be a "blue sky" company[1] susceptible of speculative activities and market manipulation. This raises a concern about the impact of such activities on the orderliness, quality and reputation of the market.

12. In the case of a spin-off, the Exchange retains its discretion to accept or reject the listed issuer's proposal having regard to, among other factors, the suitability of the remaining group and its business for listing under Rule 8.04[2].

13. In this case, the Remaining Group would rely on its Securities Business to meet the new listing requirements under Paragraph 3(c) of Practice Note 15. The Exchange was not satisfied that the Remaining Group was suitable for listing because:

    (a) The Securities Business primarily invested in one company (i.e. Company B) during the track record period. Its investment portfolio was highly concentrated. The revenues and profits of the Securities Business segment were almost entirely generated from the investment in Company B. This business model raised a concern that the Remaining Group was not carrying on a business of substance. This impacted on the Remaining Group's suitability for listing.

    (b) In addition, the whole investment in Company B was sold during the track record period. Company A's subsequent investments in two listed companies amounted to HK$10 million only and there was no detail about its future investment plans. The Remaining Group's track record was not representative of its business performance going forward. This called into question whether investors had adequate information to make an informed assessment of the Remaining Group's business after the proposed spin-off.

    (c) The scale of the Other Businesses was small and could not have met the profit requirement under Rule 8.05(1)(a). Company A had not demonstrated that there would be substantial improvement in these businesses after the proposed spin-off.

Conclusion

14. The Exchange rejected the spin-off proposal as Company A could not demonstrate that the Remaining Businesses would be suitable for listing after the proposed spin-off.

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1 "Blue sky companies" are those where public investors have no or little information about their business plans and prospects, leaving much room for the market to speculate on their possible acquisitions. These activities create opportunities for market manipulation.

2 In any case, a listed issuer must ensure that it and its business are suitable for continued listing, failing which the Exchange may cancel its listing under Rule 6.01(4).

Whether the results of a previously spun-off entity should be excluded when assessing whether the remaining group could meet the profit requirement under Main Board Rule 8.05

Parties

- **Company A** – a listed company and the parent of Company B and Company C
- **Company B** – a subsidiary of Company A spun off from Company A the previous year
- **Company C** – a subsidiary of Company A proposed to be spun off

Facts

1. Company A had spun off Company B the previous year and proposed to spin off Company C.

2. The three-year pro forma combined profits of Company A excluding the results of both Company B and Company C would not be able to meet the profit requirement of Rule 8.05.

3. The three-year pro forma combined profits of Company A excluding the results of only Company C would be able to meet the profit requirement of Rule 8.05.

4. The sponsor submitted that Paragraph 3(c) of Practice Note 15 only required exclusion of the results of the entity to be spun off and not the results of entities already spun off.

5. Furthermore, the three-year pro forma combined profits of Company A excluding the results of Company C included an exceptional gain arising from the spin-off of Company B. The sponsor submitted that the gain arose in the ordinary and usual course of business of Company A and should therefore not be excluded from the profit calculation. Without the inclusion of the exceptional gain, Company A would not be able to meet the profit requirement of Rule 8.05.

Analysis

6. Practice Note 15 requires that Company A itself has to satisfy independently the requirements of Chapter 8 of the Listing Rules. The remaining business of Company A had to be assessed on a stand-alone basis.

7. The fact that the three-year results of Company A excluding the results of both Company B and Company C would not be able to meet independently the profit requirement of Rule 8.05 showed that Company A could not support its own listing status. If the spin-off were to proceed, Company A would become mainly an investment holding company with interests in two spun-off companies. It would not be acceptable for two businesses (i.e. that of Company B and Company C) to support three separate listings (i.e. that of Company A, Company B and Company C).

8. As for the gain arising from the spin-off of Company B, this was also recognised as an exceptional item in the consolidated profit and loss account of Company A. Since a spin-off is a one-off event which should not be regarded as an activity in the ordinary and usual course of business of Company A, the exceptional gain should be excluded from the calculation of profits for the purposes of Rule 8.05.

Conclusion

9. For the purpose of Rule 8.05, the three-year results of Company A should exclude the results of both Company B and Company C. Since, by so doing, the results of Company A would not be able to meet the profit requirement of Rule 8.05, the proposed spin-off was not approved.

Whether the remaining group could rely on the unrealised fair value gains on investment properties to meet the profit requirement under Main Board Rule 8.05

Parties

- **Company A** – a Main Board issuer
- **Newco** – Company A's subsidiary proposed to seek a separate listing on the Exchange

Facts

1. Company A, through its subsidiaries, was engaged in a number of principal businesses, including the manufacture and sale of certain household products (**Manufacturing Business**) and property investment (**Property Business**).

2. Company A proposed to inject the Manufacturing Business into Newco and seek a separate listing of Newco on the Exchange. Company A (excluding Newco) (**Remaining Group**) would continue to carry out the property investment and other principal businesses. Newco would continue to be Company A's subsidiary after the proposed spin-off.

3. Company A submitted that the Remaining Group could satisfy independently the requirements under Chapter 8 of the Rules. In particular, it was of the view that the Remaining Group could meet the profit requirement under Rule 8.05(1)(a).

4. The Exchange noted that the Remaining Group's profits during the track record period were mainly attributable to the unrealized fair value gains on investment properties retained by the Remaining Group. The other businesses retained by the Remaining Group were loss making or generated minimal profits.

5. The Remaining Group held a number of properties in commercial, industrial and residential buildings in Hong Kong and the PRC for leasing and capital appreciation purposes. The Property Business generated rental income in the range of about HK$15 million to HK$30 million for each of the latest three financial years. The Remaining Group did not carry out property development or construction business during the track record period.

6. Company A submitted its plan to expand the investment property portfolio in the next few years, including some potential property acquisitions under negotiation.

7. There was an issue whether the Remaining Group could rely on the fair value gains on investment properties to meet the profit requirement under Rule 8.05(1)(a).

Relevant Listing Rules

8. Paragraph 3(c) of Practice Note 15 states that:-

"The Listing Committee must be satisfied that, after the listing of Newco, the Parent would retain a sufficient level of operations and sufficient assets to support its separate listing status. In particular, it would not be acceptable to the Listing Committee that one business (Newco's) supported two listing statuses (the Parent's and Newco's). In other words, the Parent itself would be required to retain, in addition to its interest in Newco, sufficient assets and operations of its own, excluding its interest in Newco, to satisfy independently the requirements of Chapter 8 of the Exchange Listing Rules."

9. Rule 8.05(1)(a) provides that a new applicant must have:

"a trading record of not less than three financial years (see rule 4.04) during which the profit attributable to shareholders must, in respect of the most recent year, be not less than HK$20 million and, in respect of the two preceding years, be in aggregate not less than HK$30 million. The profit mentioned above should exclude any income or loss of the issuer, or its group, generated by activities outside the ordinary and usual course of its business."

(The financial requirement under Rule 8.05(1)(a) was amended on 1 January 2022. See Note 1 below.)

10. Guidance Letter GL68-13 sets out guidance in situation where an applicant relied on unrealized fair value gains on investment properties to satisfy the profit test. The letter states that:-

"The Exchange is of the view that even if an applicant is able to satisfy the profit test under Main Board Rule 8.05(1)(a) by relying on the unrealized fair value gains of its investment properties, if the applicant is loss making after such gains are excluded and it did not have a substantive business during its track record period, the applicant would have to demonstrate that it has a sustainable business before the Exchange considers it suitable for listing.

The demonstration of a sustainable business can include the existence of property projects under development as at the date of the listing document, or significant recurring income (e.g. rental income) generated in the applicant's ordinary and usual course of business during the track record period which is expected to continue after listing."

(The guidance mentioned above is included in Chapter 1.2A of the Guide for New Listing Applicants (which came into effect on 1 January 2024) and Guidance Letter GL68-13 was archived.)

Analysis

11. In this case, property investment was one of the principal businesses of the Remaining Group. However, the Exchange was not satisfied that the Remaining Group was suitable for listing by relying on the fair value gains on investment properties to meet Rule 8.05(1)(a) because:

(a) As explained in the Guidance Letter GL68-13, where an applicant (which is a property developer/investor) meets Rule 8.05(1)(a) by relying on unrealized fair value gains arising from its investment properties, it must demonstrate that it has a substantive property business during the track record period and the business is sustainable going forward before the Exchange considers it suitable for listing under Rule 8.04.

(b) The Remaining Group held a number of properties for leasing and capital appreciation purposes, which only generated annual rental income of about HK$15 million to HK$30 million in the latest three years. The Exchange did not consider this business substantive during the track record period.

(c) The Remaining Group did not have any property projects under development or significant recurring income to demonstrate the sustainability of the Property Business as described in GL68-13. While Company A submitted that it planned to expand the property portfolio, this was preliminary and did not demonstrate that the Property Business would generate a significant level of recurring income in the future. Company A could not demonstrate that the Remaining Group had a substantive and sustainable property business.

Conclusion

12. The Exchange rejected the proposed spin-off because the Remaining Group could not satisfy Paragraph 3(c) of Practice Note 15.

Notes

1. The financial requirement under Rule 8.05(1)(a) has been amended with effect from 1 January 2022. Under the revised Rule 8.05(1)(a), a new applicant must have an adequate trading record of not less than three financial years during which the profit attributable to shareholders must, in respect of the most recent year, be not less than HK$35 million and, in respect of the two preceding years, be in aggregate not less than HK$45 million. The profit mentioned above should exclude any income or loss of the issuer, or its group, generated by activities outside the ordinary and usual course of its business.

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

Whether the remaining group could meet the minimum market capitalisation requirement under Main Board Rule 8.09(2)

Parties

- **Company A** – a Main Board issuer
- **Newco** – Company A's subsidiary proposing to seek a separate listing on the Exchange
- **Group** – Company A and its subsidiaries
- **Remaining Group** – the Group excluding Newco

Facts

1. The Group operated two major businesses, being the development and sales of residential properties (**Residential Property Business**) and investment in commercial and industrial properties.

2. Company A proposed to inject its Residential Property Business into Newco and seek a separate listing of Newco on the Exchange. After the proposed spin-off, Newco would continue to be Company A's subsidiary. The Remaining Group would continue its business in investment of commercial and industrial properties.

3. In recent years, Company A's shares had been traded at a significant discount to the net asset value of the Group, and its market capitalisation was below HK$500 million. As the Residential Property Business represented a material part of the Group's businesses, the Exchange queried whether the Remaining Group could satisfy independently the minimum market capitalisation requirement of HK$500 million under Rule 8.09(2) as required by Paragraph 3(c) of Practice Note 15.

4. Company A submitted that under Paragraph 3(c) of Practice Note 15, "*the Parent itself would be required to retain, in addition to its interest in Newco, sufficient assets and operations of its own, excluding its interest in Newco, to satisfy independently the requirements of Chapter 8 of the Exchange Listing Rules ...*" (emphasis added). The reference to "sufficient assets and operations" inferred that the Parent was only required to satisfy the listing requirements of Chapter 8 with regard to its assets and operations after the spin-off. The minimum market capitalisation requirement under Rule 8.09(2) did not apply to the Remaining Group.

5. Company A also submitted that even if Rule 8.09(2) applied to the Remaining Group, it would be able to satisfy the requirement. In this regard, Company A submitted an independent valuation report which indicated that the valuation, using the asset-based approach, was substantially higher than HK$500 million.

Relevant Listing Rules

6. Paragraph 3(c) of Practice Note 15 states that:-

"The Listing Committee must be satisfied that, after the listing of Newco, the Parent would retain a sufficient level of operations and sufficient assets to support its separate listing status. In particular, it would not be acceptable to the Listing Committee that one business (Newco's) supported two listing statuses (the Parent's and Newco's). In other words, the Parent itself would be required to retain, in addition to its interest in Newco, sufficient assets and operations of its own, excluding its interest in Newco, to satisfy independently the requirements of Chapter 8 of the Exchange Listing Rules…"

7. Rule 8.09(2) provides that: -

"*The expected market capitalisation of a new applicant at the time of listing must be at least HK$500,000,000 which shall be calculated on the basis of all issued shares (including the class of securities for which listing is sought and such other class(es) of securities, if any, that are either unlisted or listed on other regulated market(s)) of the new applicant at the time of listing."*

(Rule 8.09(2) was amended on 11 June 2024. See Note below.)

Analysis

Whether Rule 8.09(2) applied to the Remaining Group in a spin-off case

8. The purpose of Paragraph 3(c) of Practice Note 15 is to ensure that one business will not support two listing statuses. Therefore, the Parent itself (i.e. the remaining group) must carry on a business with sufficient operations and assets to satisfy independently all the listing requirements under Chapter 8 of the Rules, including the minimum market capitalisation requirement under Rule 8.09(2).

Whether the Remaining Group could meet Rule 8.09(2)

9. Company A submitted that the Remaining Group would be able to meet Rule 8.09(2) on the basis of an independent valuation of the underlying business of the Remaining Group. However, the Exchange noted that the shares of Company A had been traded at a significant discount to the net asset value of the Group. The valuation submitted by Company A had not taken into account this discount to net asset value. Furthermore, the market capitalisation of Company A had been lower than HK$500 million before the proposed spin-off, and it was expected to decrease if the Residential Property Business (being a material part of the existing businesses) was excluded from the Group. The Exchange considered that a valuation of an entity's underlying business or assets does not necessarily reflect the entity's market capitalisation. The Exchange was not satisfied that the Remaining Group could meet the minimum market capitalisation requirement of HK$500 million.

Conclusion

10. The proposed spin-off did not satisfy Paragraph 3(c) of Practice Note 15 as the Remaining Group could not meet the minimum market capitalisation requirement under Rule 8.09(2).

Note: Rule 8.09(2) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the expected market capitalisation of a new applicant. The Rule amendments would not change the analysis and conclusion in this case.

Whether the remaining group could meet the minimum market capitalisation requirement under Main Board Rule 8.09(2)

Parties

- **Company A** – a Main Board issuer
- **Newco** – Company A's subsidiary proposing to seek a separate listing on the Exchange
- **Group** – Company A and its subsidiaries
- **Remaining Group** – the Group excluding Newco

Facts

1. The Group was principally engaged in the provision of software, platforms and related support services (**Software Business**), IT solutions services (**Solutions Business**), and investing activities including property investment and treasury investment in securities.

2. Company A proposed to inject its Software Business into Newco and seek a separate listing of Newco on the Exchange. After the proposed spin-off, Newco would continue to be a subsidiary of Company A.

3. The Remaining Group would continue the Solutions Business and investing activities.

    - The Solutions Business was the core business of the Remaining Group, contributing approximately 98% of the total revenue of the Remaining Group in the latest financial year.

    - The Remaining Group's investing activities generated minimal income during the latest three financial years. Its investment portfolio comprised certain investment properties (**Investment Properties**) and listed securities and other debt investments (**Financial Assets**), with an aggregated value of about HK$90 million.

    - The Remaining Group also retained cash reserves (excluding the cash required for operating the Solutions Business) of about HK$220 million (**Cash Surplus**), representing more than 60% of the Remaining Group's total assets as at the latest year end date. Company A submitted that the Group had maintained a substantial cash reserve for many years. The Cash Surplus would be retained by the Remaining Group and be applied towards potential mergers and acquisitions and other new business opportunities after the proposed spin-off.

4. The Software Business represented the majority part of the Group's business. The Exchange queried whether the Remaining Group could satisfy independently the minimum market capitalisation requirement of HK$500 million under Rule 8.09(2), having noted that the market capitalisation of Company A was in the range of HK$700 million to HK$1 billion in the last 12 months.

5. Company A submitted that the Remaining Group could meet the market capitalisation requirement, relying on an independent valuation of the Remaining Group of about HK$600 million prepared using sum-of-parts approach comprising:

   (a) a valuation of the Solutions Business of about HK$280 million using the market approach with reference to P/E and EV/EBIT multiples of comparable companies; and

   (b) the fair value of the non-operating assets (including the Cash Surplus, the Investment Properties and the Financial Assets) of HK$320 million.

Relevant Listing Rules

6. Paragraph 3(c) of Practice Note 15 states that:-

   "The Listing Committee must be satisfied that, after the listing of Newco, the Parent would retain a sufficient level of operations and sufficient assets to support its separate listing status. In particular, it would not be acceptable to the Listing Committee that one business (Newco's) supported two listing statuses (the Parent's and Newco's). In other words, the Parent itself would be required to retain, in addition to its interest in Newco, sufficient assets and operations of its own, excluding its interest in Newco, to satisfy independently the requirements of Chapter 8 of the Exchange Listing Rules…"

7. Rule 8.09(2) provides that: -

   "*The expected market capitalisation of a new applicant at the time of listing must be at least HK$500,000,000 which shall be calculated on the basis of all issued shares (including the class of securities for which listing is sought and such other class(es) of securities, if any, that are either unlisted or listed on other regulated market(s)) of the new applicant at the time of listing."*

   (Rule 8.09(2) was amended on 11 June 2024. See Note below.)

Analysis

8. The purpose of Paragraph 3(c) of Practice Note 15 is to ensure that one business will not support two listing statuses. Therefore, the Parent itself (i.e. the remaining group) must carry on a business with sufficient operations and assets to satisfy independently all the listing requirements under Chapter 8 of the Rules, including the minimum market capitalisation requirement under Rule 8.09(2).

9. Based on the above, an issuer proposing a spin-off must demonstrate that the remaining group retains a substantive business to support a market capitalisation of at least HK$500 million as required under Rule 8.09(2). Assets that are not used to support its business operations are disregarded.

10. In this case, the Remaining Group would carry on the Solution Business and retain a number of non-operating assets after the spin-off. Company A submitted that the Remaining Group could meet Rule 8.09(2) on the basis of a valuation of about HK$600 million for these business and assets. The Exchange disagreed because the non-operating assets (with a valuation of about HK$320 million) were not used to support the business operations of the Remaining Group and therefore should be disregarded when considering the market capitalisation of the Remaining Group. The Exchange also noted that the Solution Business (being the core business of the Remaining Group) had an estimated value of HK$280 million, which was substantially lower than the minimum market capitalisation requirement of HK$500 million. The Exchange did not consider that the Remaining Group could meet Rule 8.09(2).

Conclusion

11. The proposed spin-off did not satisfy Paragraph 3(c) of Practice Note 15 as the Remaining Group could not meet the minimum market capitalisation requirement under Rule 8.09(2).

Note: Rule 8.09(2) was amended on 11 June 2024 to exclude treasury shares in the calculation of issued shares for the purpose of determining the expected market capitalisation of a new applicant. The Rule amendments would not change the analysis and conclusion in this case.

Whether the Exchange would waive the assured entitlement requirement for a proposed spin-off of business to a PRC stock exchange

Parties

- **Company A** – a Main Board issuer
- **Company B** – Company A's subsidiary proposed to be listed on a PRC stock exchange

Facts

1. Company A proposed to spin-off Company B for listing on a PRC stock exchange. This would involve Company B offering new A shares in the Mainland under the PRC laws and regulations. The deemed disposal of interest in Company B would be a major transaction for Company A subject to the shareholders' approval.

2. Company A would be able to comply with all the spin-off requirements except the requirement to provide its shareholders with an assured entitlement to the A shares of Company B. It submitted a waiver application from strict compliance with the assured entitlement requirement for the following reasons:

    - Based on its PRC counsel's advice, non-PRC investors (other than certain qualified investors) were not permitted to acquire the A shares in Company B under the PRC laws and regulations. As many of its existing shareholders were not qualified investors, there was a legal impediment for it to provide these shareholders with an assured entitlement to the A shares of Company B under the proposed spin-off; and

    - It would be burdensome for it to seek minority shareholders' approval to waive the assured entitlement at a general meeting as the legal restriction could not be overridden even if the resolution was voted down by its shareholders.

Relevant Listing Rules

3. Paragraph 3(f) of Practice Note 15 states that:

> "The Listing Committee expects the Parent to have due regard to the interests of its existing shareholders by providing them with an assured entitlement to shares in Newco, either by way of a distribution in specie of existing shares in Newco or by way of preferred application in any offering of existing or new shares in Newco. The percentage of shares in Newco allocated to the assured entitlement tranche would be determined by the directors of the Parent and by its advisers, and all shareholders of the Parent would be treated equally. There would be no bar to the controlling shareholder receiving his proportion of shares under such entitlement. Where Newco is proposed to be listed elsewhere than in Hong Kong, and where shares in Newco under the assured entitlement can only be made available to existing shareholders of the Parent by way of a public offering in Hong Kong, the Listing Committee would consider submissions as to why the assured entitlement requirement would not be for
>
> the benefit of the Parent or its shareholders. Further, the minority shareholders of the Parent may by resolution in general meeting resolve to waive the assured entitlement, even where Newco is to be listed in Hong Kong.
>
> *Note: In case where Newco is made subject to this Practice Note by virtue of the Note to paragraph 2, the Parent should use its best endeavours to provide its shareholders an assured entitlement to the shares in Newco. Whether such assured entitlement is available will be taken into account by the Exchange when considering whether to approve the spin-off proposal.*"

Analysis

4. Practice Note 15 sets out the Exchange's principles when considering proposals of issuers to effect separate listings on the Exchange or elsewhere of assets or businesses wholly or partly within their existing groups.

5. The purpose of Paragraph 3(f) of Practice Note 15 is to ensure that the issuer would give due regard to the interests of its shareholders by providing them with an assured entitlement to shares in the entity to be spun. Paragraph 3(f) further provides that if the issuer does not propose to offer such entitlement to its shareholders, it would need to obtain its minority shareholders' approval in general meeting.

6. When considering Company A's waiver application, the Exchange noted that Company B was proposed to be listed in the PRC and would need to comply with the PRC laws and regulation. It would be impractical for Company A to provide its shareholders with an assured entitlement to the A shares of Company B under the proposed spin-off.

Conclusion

7. The Exchange granted the waiver on the condition that Company A would disclose in its announcement for the proposed spin-off details of the waiver including the legal restrictions in providing the assured entitlement.

General waiver for the assured entitlement requirement

8. On 20 December 2016, the Exchange obtained the SFC's consent for granting waivers from Paragraph 3(f) of Practice Note 15 to the Main Board Rules (or Paragraph 3(f) of Practice Note 3 to the GEM Rules) to issuers who propose to spin-off their businesses for listing on the Shanghai Stock Exchange, the Shenzhen Stock Exchange or the National Equities Exchange and Quotations in the PRC. Such waiver will be granted on the conditions that:

   (i) the issuer has obtained a letter from its legal advisers to demonstrate that there are legal restrictions in providing its shareholders with assured entitlements to the spun-off entity's shares under the PRC laws and regulation;

   (ii) the board of directors of the issuer has provided a written confirmation to the issuer that the proposed spin-off and the waiver in respect of the assured entitlement requirement are fair and reasonable and in the interests of the issuer and its shareholders as a whole; and

   (iii) it will disclose in its announcement for the proposed spin-off details of the waiver including the reasons for not providing assured entitlement and the legal restrictions in providing the assured entitlement and the board of directors' confirmation as set out in paragraph 8(ii) above.

9. In respect of spin-off proposals for listing in other jurisdictions where there are legal restrictions in providing assured entitlements, the Exchange will consider any waiver applications for the assured entitlement requirement based on the specific facts and circumstances of individual cases.

16

Core shareholder protection standards

Core shareholder protection standards

1. Under Paragraph 14(1) of Appendix A1, a listed issuer must hold a general meeting for each financial year as its annual general meeting (AGM) and generally, a listed issuer must hold its AGM within 6 months after the end of its financial year. Does an overseas issuer (listed prior to the Rule change relating to the core shareholder protection standards on 1 January 2022) comply with this core standard if its constitutional document requires holding of an AGM each year and within 15 months from the date of the previous AGM pursuant to the relevant requirements applicable at the time of listing[1]?

Yes. See also paragraphs 87 to 89 of the Consultation Paper for Listing Regime for Overseas Issuers (the **Consultation Paper**) published in March 2021.

MB App A1 – 14(1)
GEM App A1 – 14(1)
First released: June 2022; last updated: May 2024

2. Under Paragraph 14(2) of Appendix A1, a listed issuer must give its members "reasonable written notice" of its general meetings, which generally means at least 21 days for an AGM and at least 14 days for other general meetings. Does a listed issuer comply with this core standard in the following circumstances?

(i) The constitutional document of a PRC issuer requires a minimum notice period of 20 days for an AGM and 15 days for other general meetings in accordance with the PRC company law.

(ii) The constitutional document of an overseas issuer (listed prior to the Rule change relating to the core shareholder protection standards on 1 January 2022) provides for a shorter written notice period as permitted at the time of listing.

Yes for both (i) and (ii). See also paragraphs 92, 93 and 95 of the Consultation Paper.

MB AppA1 – 14(2)
GEM App A1 – 14(2)
First released: June 2022; last updated: May 2024

[1] Paragraph 4(2) of the repealed Appendix 13A, Paragraph 4(2) of the repealed Appendix 13B, the repealed Rule 19C.07(4), and Paragraph 41 of the withdrawn Joint Policy Statement regarding the Listing of Overseas Companies (as the case may be).

3. Under Paragraph 17 of Appendix A1, the appointment, removal and remuneration of auditors must be approved by a majority of the listed issuer's members or other body that is independent of the board of directors. Does a listed issuer comply with this core standard in the following circumstances?

(i) A listed issuer's constitutional document permits the appointment of an auditor by the listed issuer's board to fill a casual vacancy. The auditor so appointed shall hold office until the next AGM and shall be eligible for re-election.

(ii) A listed issuer's constitutional document permits the auditor's remuneration to be fixed by an ordinary resolution passed at a general meeting, or in the manner specified in such a resolution.

Yes, as the provisions in the issuer's constitutional document are in line with the Hong Kong Companies Ordinance (Chapter 622, laws of Hong Kong) (**HKCO**)[2], which permits (i) appointment of auditor by the board to fill a casual vacancy until the next AGM; and (ii) determination of auditor's remuneration in the manner specified in a shareholders' resolution.

MB App A1 – 17
GEM App A1 – 17
First released: June 2022; last updated: May 2024

4. Under Paragraph 17 of Appendix A1, the appointment, removal and remuneration of auditors must be approved by a majority of the listed issuer's members or other body that is independent of the board of directors.

(i) For listed issuers incorporated in Bermuda, the company laws of Bermuda provide for this core standard, except that a super-majority vote is required to remove an auditor. Do they comply with the core standard?

Yes. A higher voting threshold for removal of auditors is acceptable if it is required by the domestic laws. See also paragraph 121 of the Consultation Paper.

(ii) For listed issuers incorporated in the Cayman Islands, the company laws of the Cayman Islands do not provide for this core standard. Does a listed issuer comply with this core standard if its constitutional document requires approval of the removal of an auditor by a supermajority vote of shareholders in general meeting?

No. The higher voting threshold stipulated in the constitutional document does not conform to this core standard. The issuer should amend its constitutional document to comply with the rule.

MB App A1 – 17
GEM App A1 – 17
First released: June 2022; last updated: May 2024

[2] Sections 397, 402 and 404 of the HKCO

5. Under Paragraph 20 of Appendix A1, a listed issuer's branch register of members in Hong Kong shall be open for inspection by members but the listed issuer may close the register on terms equivalent to section 632 of the HKCO[3]. Does a listed issuer comply with this core standard in the following circumstances?

(i) The constitutional document of an overseas issuer or the domestic laws provide for a shorter book closure period compared to that allowed under the HKCO.

(ii) A PRC issuer may close the register of members for the registration of transfer of shares[4] for a period longer than that allowed under the HKCO, but its members are still permitted to inspect the register during such period.

Yes for both (i) and (ii).

MB App A1 – 20
GEM App A1 – 20
First released: June 2022; last updated: May 2024

6. Will the Exchange consider granting a waiver from compliance with any core shareholder protection standards (Core Standards) for an overseas issuer?

This depends on the facts and circumstances of an individual case. For example, the Exchange may consider granting a waiver if a Core Standard is legally impossible for an overseas issuer to comply with because it conflicts with the laws and regulation of its place of incorporation.

Normally deviation from a Core Standard will not be granted if the Exchange considers that such variation may be detrimental to shareholder protection.

Furthermore, an overseas issuer cannot rely on the statutory minimum requirements under applicable laws that deviate materially from market norms in Hong Kong.

MB App A1
GEM App A1
First released: January 2022; last updated: May 2024

3 Section 632 of HKCO permits closure of register of members for a period(s) not exceeding in the whole 30 days in a year, which may be extended by member's resolution for a further period(s) not exceeding 30 days in the year. Section 7(2) of the Company Records (Inspection and provision of Copies) Regulation (Chapter 622I) provides that the requirement to make company records available for inspection is not applicable during the period when the register is closed under section 632 of the HKCO.

4 Article 38 of the Mandatory Provisions for Companies Listing Overseas requires that during the 30 days prior to any general meeting, there shall not be any change in the register of members of a PRC issuer resulted from share transfer.

17

Corporate governance / environmental, social and governance / securities transactions by directors

17.1 Corporate governance code

Frequently asked questions – Corporate governance code	FAQ17.1 – No.1-10	17.1 – 1

17.2 Environmental, social and governance reporting code

Frequently asked questions – Environmental, social and governance reporting code	FAQ17.2 – No. 1-20	17.2 – 1

17.3 Model code for securities transactions by directors of listed issuers

Frequently asked questions – Model code for securities transactions by directors of listed issuers	FAQ17.3 – No.1-12	17.3 – 1

Corporate governance code

Board composition and nomination

1. Code Provision (CP) B.1.2 requires the publication of an updated list of directors identifying their roles and functions. What information should be disclosed in this list of directors?

A listed issuer should identify whether each director is an executive director, non-executive director (**NED**) or independent non-executive director (**INED**) and, if applicable, specify the director's role at the listed issuer (e.g. chair of the board, chief executive, chief financial officer, Lead INED, member or chair of the audit/nomination/remuneration/other board committee(s), etc.).

MB App C1 – CP B.1.2
GEM App C1 – CP B.1.2
First released: December 2011; last updated: May 2025

Directors' responsibilities

2. CP C.1.5 states that "Generally they [INEDs and other NEDs] should also attend general meetings to gain and develop a balanced understanding of the views of shareholders". Is it a deviation from the CP if an INED or NED of a listed issuer does not attend a particular general meeting?

The Exchange expects directors to attend general meetings to understand shareholders' views to enable them to properly discharge their duties. While the absence of an INED or NED from a particular general meeting is normally not considered a deviation from CP C.1.5, persistent absence of the same individual(s) from general meetings will be a deviation from the CP.

MB App C1 – CP C.1.5
GEM App C1 – CP C.1.5
First released: December 2011; last updated: May 2025

Monthly management updates

3. If the monthly management accounts have been reviewed by directors, is there any change to the black-out period for directors regarding their dealings in the listed issuers' shares?

No, as long as the monthly management accounts do not contain inside information.

MB App C1 – CP D.1.2, App C3 – Rule A.2
GEM App C1 – CP D.1.2, GEM Rule 5.55
First released: December 2011; last updated: May 2025

4. Is there a deadline for the listed issuer to send management updates / monthly management accounts to directors?

Although CP D.1.2 does not specify a deadline, monthly updates should be provided to directors as soon as practicable after the month-end. Timely provision of this information, by management, is important to enable directors to monitor the listed issuer's financial and operating affairs and inside information disclosure.

Management should also respond in a timely manner to requests from directors for further information to facilitate their informed decision-making.

MB App C1 – CP D.1.2
GEM App C1 – CP D.1.2
First released: December 2011; last updated: May 2025

Internal audit function

5. What does the Exchange expect of a listed issuer's internal audit function? Is it a deviation from CP D.2.2 if a listed issuer outsources its internal audit function?

While the Exchange does not intend to prescribe the manner in which listed issuers carry out their internal audit function, it may be helpful for listed issuers to refer to the Institute of Internal Auditors' International Professional Practices Framework (**IAIPPF**) for guidance. The IAIPPF comprises core principles that define internal audit effectiveness, code of ethics and standards for the professional practice of internal auditing, as well as implementation guidance to assist internal auditors in applying the standards.

We understand that, in practice, it is common for listed issuers to engage competent external service providers to perform the internal audit function. This outsourcing would not be considered as a deviation from CP D.2.2.

MB App C1 – CP D.2.2
GEM App C1 – CP D.2.2
First released: December 2011; last updated: May 2025

Shareholders' meetings

6. Can a listed issuer include its proposed amendments to several articles of association in one special resolution to be considered at a general meeting?

The listed issuer should propose a separate resolution for each substantially separate issue at a general meeting. For example, a listed issuer should not bundle its proposed amendments to its articles of association to conform with a core shareholder protection standard under the Listing Rules with other amendments unrelated to such conformation.

MB App C1 – CP F.1.2
GEM App C1 – CP F.1.2
First released: December 2011; last updated: May 2025

Company secretary

7. If a company secretary serves a group of listed issuers, but is an employee of only one of these listed issuers, would this be considered a deviation from CP C.6.1?

No.

MB Rules App C1 – CP C.6.1
GEM Rules App C1 – CP C.6.1
First released: December 2011; last updated: May 2024

Useful resources

8. Where may listed issuers find more resources and guidance to help them with corporate governance practice?

Listed issuers may refer to the following resources:

- The Corporate Governance Guide for Boards and Directors issued by HKEX, as amended from time to time;
- The Exchange's Corporate Governance Practices, a one-stop platform that includes highlights on essential aspects of corporate governance, trainings / guidance and publications issued by HKEX as well as external reference materials;
- The Exchange's Board Diversity Hub, which contains guidance and data on board diversity; and
- The Exchange's INED Corner, which provides focused, practical guidance for INEDs.

MB Rule N/A
GEM Rule N/A
First released: December 2011; last updated: May 2025

Implementation of 2024 Amendments

9. The effective date of the amendments to the Rules and the Corporate Governance Code adopted in the "Consultation Conclusions on Review of Corporate Governance Code and Related Listing Rules" published in December 2024 (2024 Amendments) is 1 July 2025. When are listed issuers required to report their compliance against the 2024 Amendments?

Listed issuers are required to report their compliance against the 2024 Amendments in their corporate governance reports (**CG Report**) published in respect of financial years commencing on or after 1 July 2025. This would include, for example, compliance with MB Rule 13.92(1) / GEM Rule 17.104(1) (workforce diversity policy) and MB Rule 3.27B / GEM Rule 5.36B (terms of reference for the nomination committee), which are connected to certain mandatory disclosure requirements and/or code provisions in the Corporate Governance Code.

By way of illustration:

Listed issuer	First CG Report on 2024 Amendments
Listed issuer with a 31 December financial year-end	CG Report for reporting period covering 1 January 2026 to 31 December 2026
Listed issuer with a 30 June financial year-end	CG Report for reporting period covering 1 July 2025 to 30 June 2026

Listed issuers are encouraged to comply with the 2024 Amendments as early as possible in the spirit of good corporate governance.

MB App C1
GEM App C1
First released: May 2025

10. The 2024 Amendments include an obligation for listed issuers to immediately publish an announcement if they are unable to meet the board gender diversity requirement or if they are unable to set up the mandatory board committees. If a listed issuer fails to meet such requirement(s) after 1 July 2025, when should the listed issuer publish an announcement?

This obligation is described in relevant FAQs published by the Exchange, and this obligation will continue after the codification of the requirements into the Listing Rules via the 2024 Amendments. Therefore, the listed issuer should immediately publish the relevant announcement upon failing to meet such requirement(s).

MB Rules 3.23, 3.27, 3.27C and 13.92(2)
GEM Rules 5.33, 5.36, 5.36C and 17.104(2)
First released: May 2025

Environmental, social and governance reporting code

General

1. Can a listed issuer adopt other guidelines instead of the Environmental, Social and Governance Reporting Code (ESG Code or Code)? Where a listed issuer adopts alternative reporting guidance or international standards with comparable provisions to the Code, is it required to give any explanation / reconciliation in relation to the Code?

The Code sets out minimum parameters for reporting with a view to facilitating listed issuers' disclosure and communication with investors and other stakeholders, and is not intended to be comprehensive. The listed issuer's board may refer to or consider adopting international reporting standards or guidelines when preparing the listed issuer's ESG report, so long as the listed issuer includes comparable disclosures to those required under the ESG Code in its ESG report. This means the listed issuer's ESG report must clearly indicate where the disclosures required under the ESG Code are incorporated, for example, by way of a reference table directing readers to the relevant section of the ESG report.

MB Rule 13.91 and App C2
GEM Rule 17.103 and App C2
First released: August 2012; last updated December 2024

2. Where may listed issuers find more resources and guidance to help them with preparing the disclosures required in the ESG Code?

Listed issuers may refer to HKEX's ESG Academy on the HKEX website (**ESG Academy**), a centralised platform that provides various useful resources and further guidance for listed issuers.

Our ESG Academy includes e-learning modules, webinars hosted by the Exchange, guidance and publications issued by the Exchange as well as external reference materials by ESG topic.

For example, the external reference materials include links to two tools jointly developed by the Green and Sustainable Finance Cross-Agency Steering Group and the Hong Kong University of Science and Technology to support the calculation and estimation of GHG emissions.

When preparing climate-related disclosures pursuant to Part D of the Code, listed issuers should refer to (i) the application guidance set out in Appendix B of the IFRS S2 Climate-related Disclosures Standard (IFRS S2 Application Guidance) and (ii) implementation guidance issued by HKEX, as amended from time to time.

MB Rules App C2
GEM Rules App C2
First released: August 2012; last updated December 2024

3. Under MB Rules Appendix D2 Paragraph 28(2)(d) / GEM Rule 18.07A(2)(d), a listed issuer must include a discussion of its compliance with the relevant laws and regulations that have a significant impact on it (as set out in section 2(b)(ii) of Schedule 5 of the Companies Ordinance (Cap. 622 of the Laws of Hong Kong (Companies Ordinance)), along with a discussion of other ESG matters (as set out in sections 2(b)(i) and 2(c) of Schedule 5 of the Companies Ordinance). What should the listed issuer include in the discussion of its compliance with relevant laws and regulations?

In determining what to cover in the discussion of its compliance with relevant laws and regulations, a listed issuer should assess which laws and regulations have a significant impact on it in the context of its own specific circumstances, bearing in mind recent legislative and/or regulatory changes.

Where there are relevant laws and regulations that have a significant impact on the listed issuer, the listed issuer should specify (a) what these relevant laws and regulations are; (b) their potential impact on the listed issuer; and (c) the ways in which the listed issuer has ensured compliance.

Where there are no relevant laws and regulations that have a significant impact on the issuer, the ESG report should state so.

A blanket statement of compliance or absence of non-compliance is not sufficient.

MB Rules App D2 Paragraph 28(2)(d) and App C2
GEM Rule 18.07A(2)(d) and App C2
First released: December 2015; last updated May 2024

4. When preparing its ESG report, can a listed issuer cross-reference to disclosure in (a) ESG reports of its listed parent / subsidiary or (b) its previous ESG reports to satisfy its disclosure obligations under the ESG Code?

(a) To avoid duplications, a listed issuer may use cross-referencing in its ESG report to refer to disclosure in ESG reports of its listed parent / subsidiaries, provided that each listed company fulfils its own disclosure obligations under the ESG Code.

(b) Some ESG issues impact the listed issuer on a continuous basis with little change from year to year. In such cases, listed issuers may cross-refer to their previous ESG reports for historical information regarding the relevant ESG issue, and disclose updates to the matter in their current reports.

If cross-referencing is used, the listed issuer's ESG report is expected to have clear referencing and URL links to specific provisions in its listed parent / subsidiaries' ESG reports (or its previous ESG reports). Any cross-referenced ESG reports must be available at the time when the listed issuer publishes its ESG report.

MB Rules App C2
GEM Rules App C2
First released: November 2018; last updated May 2024

ESG Governance

5. As "governance" is part of the ESG elements, what are the governance disclosures that are required to be reflected in listed issuers' ESG reports and how should listed issuers prepare such disclosures?

Listed issuers are required to disclose their ESG governance structure by including a statement from the board containing the following elements in their ESG report:

(i) A disclosure of the board's oversight of ESG issues;

(ii) The board's ESG management approach and strategy, including the process used to evaluate, prioritise and manage material ESG-related issues (including risks to the issuer's businesses); and

(iii) How the board reviews progress made against ESG-related goals and targets with an explanation of how they relate to the listed issuer's businesses.

There is no specific requirement in the ESG Code as to the form or location of the board statement on ESG governance, and listed issuers may decide on the appropriate presentation of such statement, so long as the presentation is clear for readers to understand the board's governance of ESG issues.

Subject to the implementation timeline for the 2024 Amendments as set out in Question 16 below, for ESG reports for financial years commencing on or after 1 January 2025, listed issuers shall disclose additional information about their governance structure, processes, controls and procedures in relation to the management, oversight and monitoring of climate-related risks and opportunities.

In preparing their governance disclosures pursuant to paragraphs 13 (board statement on ESG governance) and 19 (climate-related governance disclosures) of the Code, listed issuers should avoid unnecessary duplication. If oversight of ESG-related (including climate-related) risks and opportunities is managed on an integrated basis, a listed issuer should provide integrated governance disclosures in its ESG report.

MB Rules App C1 and App C2 Paragraphs 13 and 19
GEM Rules App C1 and App C2 Paragraphs 13 and 19
First released: May 2019; last updated December 2024

Reporting boundary

6. How should a listed issuer determine the reporting boundary of its ESG report?

The Code does not prescribe which entities in a listed issuer's group and/or which operations should be included in the ESG report. A listed issuer's board should have its own criteria for determining the scope with respect to its own business and circumstances. For example, a listed issuer may follow the scope that used in its annual report / related financial statements, or apply a financial threshold (e.g. inclusion of subsidiaries or operations contributing to a certain percentage of the listed issuer group's total revenue or more) or risk level (e.g. inclusion of operations exceeding a certain risk level despite being a non-major business sector of the listed issuer's group) in determining the scope of the ESG report.

In some cases, a listed issuer may adopt different scopes for different Aspects / provisions.

Listed issuers are required to explain the reporting boundaries of the ESG report and describe the process used to identify which entities or operations are included in the ESG reports. If there is a change in the scope, listed issuers should explain the difference and reason for the change. If different scopes are adopted for different Aspects / provisions, listed issuers should also disclose such information in the ESG report.

MB Rules App C2
GEM Rules App C2
First released: August 2012; last updated May 2024

Reporting principles

7. How does a listed issuer determine "materiality" and what is the board's involvement in the process?

"Materiality" is defined in the Code as "the threshold at which ESG issues determined by the board are sufficiently important to investors and other stakeholders that they should be reported". The definition is sufficiently wide to encompass a range of materiality considerations, including but not limited to financial materiality.

Whether a particular ESG issue is material is a matter of judgment for the board. The board may determine that an ESG issue is material based on different considerations, for example, the facts involved, the circumstances of the listed issuer with reference to the views of its key stakeholders and/or the impact of the ESG issue on the listed issuer's financial performance or financial position. Listed issuers should bear in mind that materiality can have different meanings for different stakeholder groups, and should disclose the board's involvement, the identification process and the criteria for the selection of material ESG factors in the ESG report.

For the purpose of making climate-related disclosures under Part D of the Code, listed issuers must disclose information about climate-related risks and opportunities that could reasonably be expected to affect their cash flows, access to finance or cost of capital over the short, medium or long term. To assess the materiality of a climate-related risk or opportunity, listed issuers should consider both quantitative and qualitative factors, and assess the nature or magnitude of the relevant risk or opportunity.

Listed issuers may disclose information that is material to investors (based on financial materiality) as well as information that is material to other stakeholders (based on other materiality considerations) in their ESG report. Where they do so, listed issuers must ensure that the material information for investors is not obscured and is clearly identified and distinguishable from the information provided for other stakeholders.

MB Rules App C2
GEM Rules App C2
First released: August 2012; last updated December 2024

8. Is it a requirement for listed issuers to conduct a stakeholder engagement every year? Where no stakeholder engagement took place specifically for the purpose of preparing the ESG report during the relevant financial year, is the listed issuer required to disclose this fact?

The description of, or explanation on, the application of the materiality principle should focus on the identification process and selection criteria of material ESG factors. Stakeholder engagement only serves as one of the tools to enable an issuer to understand the reasonable expectations and interests of stakeholders, as well as their information needs. Since stakeholder engagement should be part of a listed issuer's everyday operations, it is not necessary to conduct a stakeholder engagement specifically for the purpose of preparing an ESG report; thus the absence of a specific stakeholder engagement need not be disclosed in the ESG report.

A stakeholder engagement may take different forms and does not necessarily mean a large-scale exercise. For example, it may be conducted through daily contact with clients / suppliers / employees.

If a stakeholder engagement was conducted, listed issuers should include a description of the significant stakeholder identified as well as the process and results of the stakeholder engagement.

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated May 2024

9. The quantitative reporting principle states that a listed issuer "should set targets (which may be actual numerical figures or directional, forward-looking statements) to reduce a particular impact". Does this mean that listed issuers are required to set and disclose targets for all KPIs in Part C of the ESG Code in the ESG report, and how does this relate to the provisions on setting climate-related targets in Part D of the Code?

While listed issuers may set targets for all KPIs that are material to them, Part C of the Code only expressly requires disclosure of emission targets (KPI A.1.5), waste reduction targets (KPI A.1.6), energy use efficiency targets (KPI A.2.3) and water efficiency targets (KPI A.2.4) on a "comply or explain" basis.

The targets may be actual numerical figures or directional, forward-looking statements.

The climate-related targets that listed issuers have set (or are required to meet by law or regulation) and disclosed pursuant to Part D of the Code may or may not be those required under Part C of the Code.

Listed issuers may set climate-related targets beyond those required under Part C of the Code. Where a listed issuer has set climate-related targets, regardless of whether such targets are those required under Part C of the Code or other additional climate-related targets, it should disclose the information set out in paragraphs 37 to 40 of Part D of the Code regarding each climate-related target.

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated December 2024

10. The Code requires the description of, or explanation on, the application of the quantitative reporting principle to include information on the standards, methodologies, assumptions and/or calculation tools used. Please clarify the level of detail required to fulfill this disclosure requirement.

A description of or reference to the standards (e.g. Greenhouse Gas Protocol for greenhouse gas (**GHG**) emissions), methodologies (e.g. whether consumption of reused water is counted as water consumption), major assumptions and/or calculation tools adopted in the ESG report suffices.

There is no need to explain the methodologies or assumptions underlying a well-established standard.

Where specific disclosure is required under the Code, listed issuers will need to provide further details. For example, Part D of the Code requires listed issuers to disclose the measurement approach, inputs and assumptions that they use to measure their GHG emissions (paragraph 29(b)(i)).

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated December 2024

11. Where there is no change to the methods or KPIs used or any other relevant factors affecting a meaningful comparison of the ESG report with previous reports, are listed issuers required to disclose this fact in the ESG report?

Inclusion of a statement to confirm no change may be useful for readers in terms of transparency. This also enables readers to compare information contained in the ESG report with that in previous reports.

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated May 2024

Social aspects

12. Please clarify whether Aspect B2: Health and Safety covers physical safety of employees only.

Aspect B2: Health and Safety covers both physical and non-physical aspects, such as the mental well-being of employees. For example, in respect of KPI B2.3, listed issuers may disclose their employee wellness programmes (which may include mental wellness or financial wellness seminars).

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated May 2024

13. KPI B5.4 requires description of practices used to promote environmentally preferable products and services when selecting suppliers, and how they are implemented and monitored. What is the definition of "environmentally preferable products"?

Environmentally preferable products may be defined with reference to the listed issuer's internal classification.

In Hong Kong, the Government maintains a green procurement list with green specifications for commonly used items, which may provide a useful reference. See Green Procurement by EPD: https://www.eeb.gov.hk/en/susdev/green_procure/green_procure.html

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated May 2024

14. Where may listed issuers find resources for reporting of Aspect B7: Anti-corruption?

Listed issuers may refer to "Tips for Good Environmental, Social and Governance Reporting under the Anti-Corruption Aspect" published by the Independent Commission for Anti-Corruption's Corruption Prevention Advisory Service.

In addition to reporting on the general disclosures and KPIs prescribed under Aspect B7, listed issuers may disclose results of their corruption risk assessment in their ESG reports. Listed issuers may also upload important anti-corruption policy documents, including the codes of conduct for directors and staff, integrity requirements for business partners, and their whistle-blowing policy and procedures to their websites.

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated May 2024

Independent assurance

15. Paragraph 9 of the ESG Code encourages listed issuers to seek independent assurance for ESG reports, and where independent assurance is obtained, requires the issuer to describe the level, scope and processes adopted for the assurance given in the ESG report.

(a) What should a listed issuer consider when selecting an assurance provider?

A listed issuer should consider whether the assurance provider:

- is independent from the listed issuer and its controlling shareholders, and therefore able to reach an objective and impartial opinion about the ESG report;
- is demonstrably competent in both the subject matter and assurance practices; and

- will issue a written report which includes: an opinion or set of conclusions; a description of the responsibilities of the report preparer and the assurance provider; and a summary of the work performed, which explains the nature of the assurance conveyed by the assurance report. For the avoidance of doubt, listed issuers are not required to disclose the text of this report in the ESG report.

(b) What should be the scope of assurance?

Listed issuers may choose to obtain external assurance for all or part of its ESG report, so long as the scope of assurance is clearly set out in the ESG report.

(c) Which assurance framework should listed issuers adopt?

Assurance for ESG and sustainability reporting is a developing area. In November 2024, the International Auditing and Assurance Standards Board published the General Requirements for Sustainability Assurance Engagements (**ISSA 5000**). The ISSB 5000 is designed to be a global baseline for sustainability assurance engagements. It addresses both limited and reasonable assurance engagements and can be applied to assurance engagements in respect of sustainability disclosures prepared under different reporting frameworks (including the ISSB standards). Listed issuers may wish to refer to and adopt the ISSA 5000 if they obtain independent assurance.

(d) Is the listed issuer required to state the name of the party providing assurance in the ESG report?

Listed issuers may decide whether to disclose the assurance provider's name.

MB Rules App C2
GEM Rules App C2
First released: February 2020; last updated December 2024

Climate-related disclosures

16. What is the implementation timeline for the amendments to the Rules and the Code adopted in the "Consultation Conclusions on Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework" published in April 2024 (2024 Amendments)?

The 2024 Amendments will come into effect in the following manner:

(a) For financial years commencing on or after 1 January 2025:

- All listed issuers (i.e. both Main Board listed issuers and GEM listed issuers) are required to disclose Scope 1 and Scope 2 GHG emissions on a mandatory basis;
- In addition to Scope 1 and Scope 2 GHG emissions which are required to be reported on a mandatory basis:

- all Main Board listed issuers are required to report on the climate-related disclosure requirements set out in Part D of the Code (**Climate Requirements**) on a "comply or explain" basis; and

- all GEM listed issuers are encouraged to report on the Climate Requirements on a voluntary basis.

(b) For financial years commencing on or after 1 January 2026, all Hang Seng Composite LargeCap Index (**HSCLI**) constituents are required to report on the Climate Requirements on a mandatory basis (**Mandatory Climate Disclosure Requirement**).

MB Rules App C2 Part D
GEM Rules App C2 Part D
First released: December 2024

17. Under MB Rules Appendix C2 paragraph 17(2), a listed issuer that is a HSCLI constituent shall report on the requirements set out in Part D of the Code on a mandatory basis in respect of financial years commencing on or after 1 January 2026 (FY 2026). How can a listed issuer that is a HSCLI constituent determine whether it is subject to the Mandatory Climate Disclosure Requirement in FY 2026?

The Mandatory Climate Disclosure Requirement applies to listed issuers that are HSCLI constituents throughout the year immediately prior to the reporting year (in respect of the ESG report in question).

The Mandatory Climate Disclosure Requirement comes into effect from FY 2026. Accordingly, listed issuers that are HSCLI constituents throughout their entire financial year commencing on or after 1 January 2025 will be the first batch of listed issuers subject to the Mandatory Climate Disclosure Requirement in respect of their ESG reports for FY 2026 (to be published in 2027).

MB Rules App C2 Paragraph 17(2) and Note to Paragraph 17(2)
First released: December 2024

18. Hang Seng Indexes Company Limited reviews the constituents of the Hang Seng Composite Index Series at various intervals throughout the year. Where a listed issuer is added to HSCLI during a particular year, when will it become subject to the Mandatory Climate Disclosure Requirement?

The Mandatory Climate Disclosure Requirement applies to listed issuers who are HSCLI constituents throughout the year immediately prior to the reporting year (in respect of the ESG report in question). Therefore, where a listed issuer is newly added to HSCLI, it would only become subject to the Mandatory Climate Disclosure Requirement after having been a HSCLI constituent for an entire financial year. Please refer to the illustrative examples below:

<u>Illustrative example 1</u>

Listed issuer A with a 31 December financial year end is added to HSCLI with effect from September 2025. For financial year ending on:

- **31 December 2025** (i.e. reporting period covering 1 January 2025 to 31 December 2025): Listed issuer A only becomes a HSCLI constituent with effect from September 2025, i.e. not a HSCLI constituent throughout the year.

- **31 December 2026** (i.e. reporting period covering 1 January 2026 to 31 December 2026): Listed issuer A is a HSCLI constituent for the entire financial year.

- **31 December 2027** (i.e. reporting period covering 1 January 2027 to 31 December 2027): The Mandatory Climate Disclosure Requirement starts to apply to Issuer A, and the relevant ESG report will be published in 2028.

Illustrative example 2

Listed issuer B with a 30 June financial year end is added to HSCLI with effect from March 2026. For financial year ending on:

- **30 June 2026** (i.e. reporting period of 1 July 2025 to 30 June 2026): Listed issuer B only becomes a HSCLI constituent with effect from March 2026.

- **30 June 2027** (i.e. reporting period of 1 July 2026 to 30 June 2027): Listed issuer B is a HSCLI constituent for the entire financial year.

- **30 June 2028** (i.e. reporting period of 1 July 2027 to 30 June 2028): The Mandatory Climate Disclosure Requirement starts to apply to Issuer B, and the relevant ESG report will be published in 2028.

Once a listed issuer becomes subject to the Mandatory Climate Disclosure Requirement pursuant to paragraph 17(2) of Appendix C2, such issuer will continue to be subject to the Mandatory Climate Disclosure Requirement even if it subsequently ceases to be a HSCLI constituent.

MB Rules App C2 Note to Paragraph 17(2)
First released: December 2024

19. What are the implementation reliefs provided in Part D of the Code and which Climate Requirements do these reliefs apply to?

The following implementation reliefs are provided in Part D of the Code:

- Reasonable information relief – this relief allows a listed issuer to prepare relevant disclosures based on all reasonable and supportable information that is available to it at the reporting date without undue cost or effort.

- Capabilities relief – this relief allows a listed issuer to use an approach that is informed by or commensurate with the available skills, capabilities and resources that are available to it in preparing relevant disclosures.

- Commercial sensitivity relief – this relief exempts disclosure of information about a climate-related opportunity in limited circumstances where such information is commercially sensitive and not already publicly available.

- Financial effects relief – this relief allows disclosure of qualitative instead of quantitative financial information where certain conditions are met.

The table below summarises the Climate Requirements where implementation reliefs are available:

Climate Requirement	Implementation relief			
	Reasonable information relief	Capabilities relief	Commercial sensitivity relief[1]	Financial effects relief[2]
All paragraphs with respect to climate-related opportunities *(note 2 to paragraph 20 of the Code)*			✓	
Identification of climate-related risks and opportunities *(note 1(a) to paragraph 20 of the Code)*	✓			
Determination of the scope of the value chain *(note to paragraph 21 of the Code)*	✓			
Quantification of current and anticipated financial effects *(notes 3 to 5 to paragraph 25 of the Code)*		✓ (anticipated financial effects only)		✓
Preparation of disclosures on anticipated financial effects *(note 2 to paragraph 25 of the Code)*	✓	✓		
Use of climate-related scenario analysis *(note to paragraph 26 of the Code)*	✓	✓		
Measurement approach, inputs and assumptions of Scope 3 GHG emissions *(note 1 to paragraph 29 of the Code)*	✓			
Calculation of cross-industry metrics in relation to climate-related transition risks, climate-related physical risks and climate-related opportunities *(note to paragraph 32 of the Code)*	✓			

Notes:

(1) Where a listed issuer elects to use the commercial sensitivity relief, the issuer shall, for each item of information omitted, (i) disclose the fact that it has used the exemption; and (ii) reassess, at each reporting date, whether the information qualifies for the exemption (See note 2(c) to paragraph 20 of the Code).

(2) Where a listed issuer determines that it need not provide quantitative information about the current or anticipated financial effects of a climate-related risk or opportunity, the listed issuer shall (i) explain why it has not provided quantitative information; (ii) provide qualitative information about those financial effects; and (iii) provide quantitative information about the combined financial effects of that climate-related risk or opportunity with other climate-related risks or opportunities and other factors, unless the listed issuer determines that quantitative information about the combined financial effects would not be useful (See note 5 to paragraph 25 of the Code).

MB Rules App C2 Part D
GEM Rules App C2 Part D
First released: December 2024

20. (a) What are financed emissions?

Financed emissions are defined in the IFRS S2 Climate-related Disclosures Standard as the portion of gross GHG emissions of an investee or counterparty attributed to the loans and investments made by an entity to the investee or counterparty. These emissions are part of Scope 3 Category 15 (investments) as defined in the Greenhouse Gas Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard (2011) (**GHG Protocol (Scope 3) Standard**).

(b) Are listed issuers required to disclose information regarding their financed emissions in their ESG reports?

Listed issuers are required to disclose the categories included within their measure of Scope 3 GHG emissions in accordance with the Scope 3 categories described in the GHG Protocol (Scope 3) Standard, which include financed emissions (Scope 3 Category 15 (investments) activity). An issuer should map its value chain against all 15 categories of the GHG Protocol (Scope 3) Standard and disclose the categories included in its Scope 3 GHG emissions. Where there are exclusions, issuers should justify and explain such exclusions.

(c) Note 3 to paragraph 29 of the Code provides that listed issuers which activities include asset management, commercial banking or insurance are encouraged to disclose "*additional information*" about their financed emissions. Does it mean that these listed issuers are not required to disclose their financed emissions?

No, note 3 to paragraph 29 of the Code is not an exemption to issuers within such industry sectors. "Additional information" refers to information required under paragraphs B58 to B63 of the IFRS S2 Application Guidance (**Scope 3 Additional Information**). While the Code does not require disclosure of Scope 3 Additional Information, where an issuer has disclosed such information in a document other than the ESG report (e.g. specific information about their financed emissions as required by regulators who supervise them (other than the Exchange)), the listed issuer is encouraged to include a cross-reference to such document in its ESG report.

MB Rules App C2 Paragraph 29 and Note 3 to Paragraph 29
GEM Rules App C2 Paragraph 29 and Note 3 to Paragraph 29
First released: December 2024

Model code for securities transactions by directors of listed issuers

1. A director enters into a share dealing agreement prior to the black-out period. Will the director be considered as dealing in shares if completion of the share dealing agreement takes place during the black-out period under Rule A.3(a) of Appendix C3 to the MB Rules / GEM Rule 5.56(a)?

No, provided that the pricing is fixed (in monetary terms) before the black-out period and completion takes place pursuant to the original terms of the agreement.

MB App C3 – Rule A.3(a)
GEM Rule 5.56(a)
First released: March 2004; last updated: May 2024

2. Please clarify the meaning of "beneficial ownership is transferred from another party by operation of law" under paragraph 7(d)(viii) of Appendix C3 to the MB Rules / GEM Rule 5.52(4)(h)?

This refers to the situation where the transfer occurs automatically because of applicable laws rather than any act on the part of the relevant parties. For example, the director may be entitled to receive an interest in securities as a result of the laws governing intestacy or, where the director is a joint holder of securities, the director may obtain ownership of the securities if the other joint holder dies.

MB App C3 – Paragraph 7(d)(viii)
GEM Rule 5.52(4)(h)
First released: November 2008; last updated: May 2024

3. A listed issuer has notified the Exchange of the commencement date of the black-out period under paragraph (b) of Rule A.3 of Appendix C3 to the MB Rules / GEM Rule 5.56(b). If it later decides to postpone publication, should the black-out period be based on the revised publication date?

No. The commencement date of the black-out period does not change if the listed issuer decides to postpone publishing the results after it has notified the Exchange. The black-out period will be extended and end on the date of publication.

MB App C3 – Rule A.3(b)
GEM Rule 5.56(b)
First released: November 2008; last updated: May 2024

4. When should the black-out period start if a listed issuer anticipates a delay in publishing its results announcement?

The default position is that the latest any black-out period can start is 60 days or 30 days before the publication deadline for the annual or interim results. This is so even if the listed issuer expects that the publication date will be after the deadline imposed by the Listing Rules.

MB App C3 – Rule A.3
GEM Rule 5.56
First released: November 2008; last updated: May 2024

5. Is a director permitted to deal on the actual day on which the listed issuer's financial results are published?

No. Rule A.3(a) of Appendix C3 to the MB Rules / GEM Rule 5.56(a) states that a director must not deal in any securities of the listed issuer on any day on which its financial results are published.

MB App C3 – Rule A.3(a)
GEM Rule 5.56(a)
First released: November 2008; last updated: May 2024

6. Rule A.3(a) of Appendix C3 to the MB Rules / GEM Rule 5.56(a) provides that the black-out period may commence "from the end of the relevant financial year up to the publication date of the results". Please clarify whether the period commences on the day the financial year end or the day immediately following the financial year end.

The period commences on the day immediately following the financial year end date.

MB App C3 – Rule A.3(a)
GEM Rule 5.56(a)
First released: November 2008; last updated: May 2024

7. Mr. X, a director of Company A, intends to make an offer for Company A's shares under the Takeovers Code. Does it constitute a dealing in Company A's shares by Mr. X under the Model Code when, during the black-out period:

(i) the offer document is despatched?

Yes, the despatch of the offer document during the black-out period is a dealing by Mr. X under the Model Code.

(ii) Mr. X announces his firm intention to make the offer (with terms)?

No, if the offer (i.e. the despatch of the offer document) would not take place within the black-out period. As Mr. X will be required to proceed with the offer in accordance with the Takeovers Code after he announced a firm intention to make the offer, he should apprise himself of all applicable rules and regulations before making the announcement. Please also refer to the SFC's Takeovers Bulletin – Issue No. 15.

(iii) Mr. X seeks and obtains irrecovable undertakings from Company A's shareholders to tender their shares under the offer?

No, the undertakings would not themselves be regarded as dealings by Mr. X under the Model Code.

MB App C3 – Paragraph 7 and Rule A.3
GEM Rules 5.52 and 5.56
First released: May 2011; last updated: May 2024

8. Mr. X has announced a firm intention to make an offer for Company A's shares (with terms) under the Takeovers Code before the commencement of the black-out period. If the offer document is to be despatched during the black-out period and there are no change to the offer terms, would the dealing restriction under the Model Code apply?

Yes.

MB App C3 – Paragraph 7 and Rule A.3
GEM Rules 5.52 and 5.56
First released: May 2011; last updated: May 2024

9. For the purpose of the Model Code, does dealing include a takeover of a listed issuer by way of scheme of arrangement under which the listed issuer's shares would be cancelled or transferred in exchange for cash or securities?

Yes, as a scheme of arrangement has similar effect to takeovers by way of general offer.

MB App C3 – Paragraph 7
GEM Rule 5.52
First released: May 2011; last updated: May 2024

10. An entity makes an offer to acquire a listed issuer's shares under the Takeovers Code. Mr. Y is a director of each of the listed issuer and the offeror. Would the offer be regarded as dealing by Mr. Y in the listed issuer's shares under the Model Code by virtue of his directorship in the offeror?

No. However, Mr. Y should note that under the Model Code he must not make any unauthorised disclosure of confidential information of the listed issuer to any person (even those to whom he owes a fiduciary duty).

MB App C3 – Paragraphs 6 and 7 and Rules A.3 and A.6
GEM Rules 5.51, 5.52, 5.56 and 5.59
First released: May 2011; last updated: May 2024

11. A director of a listed issuer has pledged part of his/her shares in the issuer for a margin loan. Does it constitute a dealing in the listed issuer's shares by the director under the Model Code if, during the black-out period,

(i) the director tops up the number of shares pledged to meet the margin requirements?

Yes. The dealing restriction will apply unless the director can demonstrate that the circumstances are exceptional and the proposed top-up of share pledge is the only reasonable course of action available to the director to avoid forced sale of the pledged shares and will be conducted in accordance with Rule C.14 of the Model Code.

(ii) the director repays the loan which will result in a release of the share pledge?

No.

MB App C3 – Rules A.3(a) and C.14
GEM Rules 5.56(a) and 5.67
First released: May 2024

12. A listed issuer has repurchased its shares on the Exchange for holding in treasury. One of its directors is taken to have an interest in those treasury shares for the purpose of Part XV of the SFO as the director is also a shareholder that controls over one-third of the voting power at general meetings of the issuer. In this situation, would the share repurchase or any subsequent sale, transfer or cancellation of the treasury shares by the issuer constitute a dealing in the issuer's shares by the director under the Model Code?

No, if the director has an interest in those treasury shares only because of his shareholding in the issuer.

The Model Code is not intended to apply to an issuer's holding or cancellation of its treasury shares, or its share repurchase, issuance of new shares, or sale or transfer of its treasury shares conducted with persons independent of its directors. That said, directors are still required to observe the general principle under the Model Code that they must not make any unauthorised disclosure of confidential information to other persons (even those to whom they owe a fiduciary duty) or make any use of such information for the advantage of themselves or others. They must ensure that the issuer complies with the Listing Rule requirements applicable to the transactions, including but not limited to the dealing restrictions and moratorium periods set out in MB Rules 10.06(2) and (3) and 10.06A / GEM Rules 13.11, 13.12, 13.12A and 13.14A.

MB App C3 – Paragraphs 6 and 7 and Rule A.6
GEM Rules 5.51, 5.52 and 5.59
First released: December 2024

18

Other topics

18.1 Contractual arrangements

Guidance letter – Guidance on listed issuers using contractual arrangements for their businesses	GL77-14	18.1 – 1

18.2 Special rights

Listing decision – Whether certain special rights available to an investor under the terms of convertible bonds to be issued by a listed issuer would comply with the general principles in Rule 2.03	LD99-3	18.2 – 1

18.3 Issuers associated with gambling activities

Guidance letter – Gambling activities of new listing applicants and listed issuers	GL71-14	18.3 – 1

18.4 Stock Connect

Frequently asked questions – Offers or distributions of entitlement securities by listed issuers to Southbound Shareholders under Stock Connect	FAQ18.4 – No.1-4	18.4 – 1

18.5 Listing fees

Frequently asked questions – Listing fees	FAQ18.5 – No.1	18.5 – 1

Guidance on listed issuers using contractual arrangements for their businesses

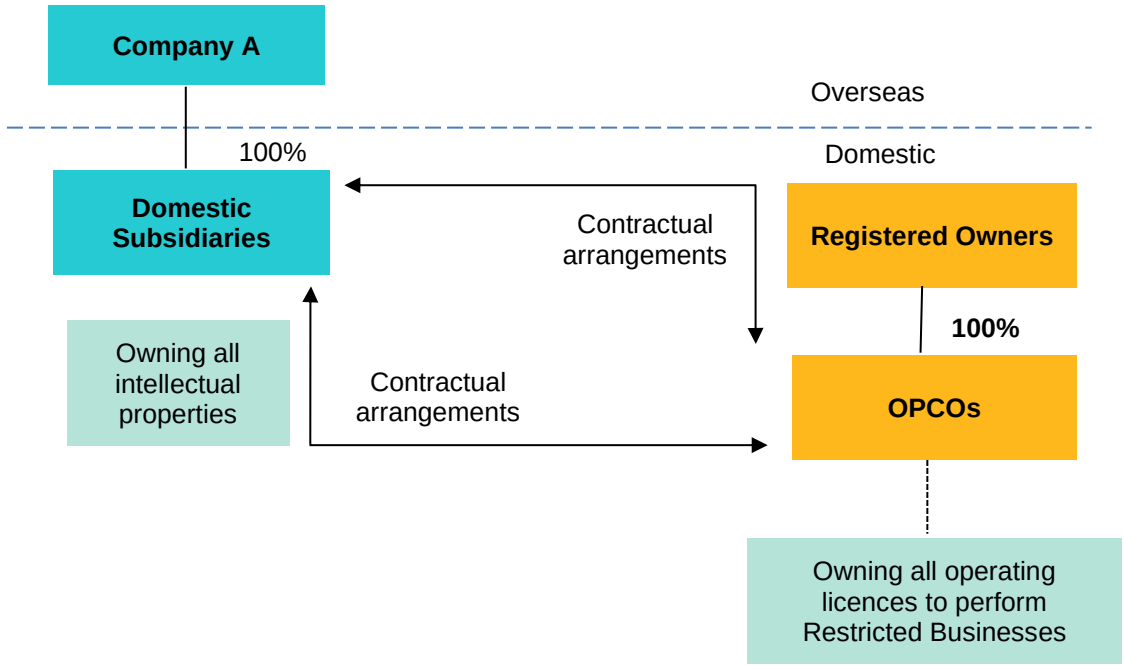
A. Purpose

1. In certain jurisdictions (e.g. Mainland China), the relevant laws and regulations specifically restrict foreign investment in certain businesses (e.g. telecommunications, healthcare and education) (**Restricted Businesses**). In such circumstance, issuers generally use contractual arrangements to hold interests in, and control over, the Restricted Businesses.

2. Chapter 4.1 of the Guide for New Listing Applicants (**Guide**) provides guidance to new listing applicants using contractual arrangements for their businesses. This letter follows the guidance in the Guide and is applicable to issuers using contractual arrangements in conducting their businesses after listing.

B. Contractual Arrangements

3. Set out below is the typical structure of the contractual arrangements adopted by a listed issuer (**Company A**) in conducting Restricted Businesses:



4. Under the contractual arrangements, the issuer has:

   (a) the right to enjoy all the economic benefits of the domestic incorporated operating company(ies) (**OPCOs**) [1] that are owned by the registered owners (**Registered Owners**)[2] and controlled by the issuer through contractual arrangements, to exercise management control over the operations of OPCOs, and to prevent leakage of assets and values to shareholders of OPCOs;

   (b) the right to all intellectual properties through assignments from OPCOs;

   (c) the right to consolidate the financial results of OPCOs as if they were wholly-owned subsidiaries of the issuer under prevailing accounting principles;

   (d) the right to acquire, if and when permitted by the domestic law, the equity interests in and/or assets of OPCOs for a nominal price or a pre-paid amount; and

   (e) a first-priority security interest over OPCO shares owned by the Registered Owners, as security for the proper performance of the contractual arrangements.

C. Relevant Listing Rules

General principles

5. MB Rule 2.03 (GEM Rule 2.06) states that:

   "The Listing Rules reflect currently acceptable standards in the market place and are designed to ensure that investors have and can maintain confidence in the market and in particular that: -

   …

   (3) investors and the public are kept fully informed by the listed issuers … of material factors which might affect their interests;

   …

   (5) directors of a listed issuer act in the interests of its shareholders as a whole … ; and

   …"

6. Section D.2 of Appendix C1 to the MB Rules (Section D.2 of Appendix C1 to the GEM Rules) provides that an issuer's board of directors is responsible for ensuring that the issuer establishes and maintains appropriate and effective risk management and internal control systems.

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1 For the purpose of this guidance letter, where the Restricted Businesses are conducted by subsidiaries of OPCO, "OPCO" should be read as "subsidiaries of OPCO" and the contractual arrangements should ensure that the interests and economic benefits of the issuer in the Restricted Businesses held through such subsidiaries are equally safeguarded.

2 The Registered Owners are usually the controlling shareholders of the issuer. Where the Registered Owners are not individuals but limited partnerships or corporates, the contractual arrangements should ensure that the interests and economic benefits of the issuer should be equally safeguarded.

Disclosure requirements for notifiable and/or connected transactions

7. Under MB Rules 14.58, 14.59, 14.60 and 14A.68 (GEM Rules 19.58, 19.59, 19.60 and 20.66), the announcement for a notifiable transaction and/or connected transaction must contain, among others, the following information:

"

- *…;*
- *the reasons for entering into the transactions, the benefits which are expected to accrue to the listed issuer as a result of the transaction and a statement that the director believe that the terms of the transactions are fair and reasonable and in the interests of the shareholders as a whole;*
- *the general nature of the transaction …;*
- *brief details of the asset(s) being acquired or disposed of, including the name of any company or business or the actual assets or properties where relevant and, if the assets include securities, the name and general description of the activities of the company in which the securities are or were held;*
- *…"*

8. Under MB Rules 14.63 and 14A.69 (GEM Rules 19.63 and 20.67), the circular for a major (or above) transaction and/or a connected transaction must provide clear and adequate explanation of its subject matter and contain all information necessary to allow the shareholders to make a properly informed decision.

9. MB Rule 14.66(10) and Paragraph 29(1)(b) of Appendix D1B (GEM Rule 19.66(11) and Paragraph 29(1)(b) of Appendix D1B) state that a circular for a major transaction must contain:

"A statement as to the financial and trading prospects of the group for at least the current financial year, together with any material information which may be relevant thereto, including all special trade factors or risks (if any) which are not mentioned elsewhere in the listing document and which are unlikely to be known or anticipated by the general public, and which could materially affect the profits."

"… reference to the group is to be construed as including any company which will become a subsidiary of the issuer by reason of an acquisition which has been agreed or proposed since the date to which the latest audited accounts of the issuer have been made up."

Disclosure requirements for annual reports

10. Paragraph 9 of Appendix D2 to the MB Rules (GEM Rule 18.10) provides that an issuer shall include in its financial statements a statement showing:

"(1) the name of every subsidiary, its principal country of operation and its country of incorporation or other establishment, and, in the case of a subsidiary established in the PRC, the kind of legal entity it is registered under the PRC law …; and

(2) particulars of the issued share capital and debt securities of every subsidiary.

9.1 …

9.2 If a listed issuer has an excessive number of subsidiaries, the statement need only include details for subsidiaries which, in the opinion of the directors, materially contribute to the net income of the group or hold a material portion of the assets or liabilities of the group."

11. Paragraph 32 of Appendix D2 to the MB Rules (GEM Rule 18.41) states that:

"A listed issuer shall include in its annual report a discussion and analysis of the group's performance during the financial year and the material factors underlying its results and financial position. It should emphasize trends and identify significant events or transactions during the financial year under review. … …"

12. Paragraph 28(2) of Appendix D2 to the MB Rules (GEM Rule 18.07A(2)) requires an issuer to include a description of the principal risks and uncertainties facing the issuer under the business review disclosed in the directors' report for the financial year.

D. Guidance

13. Under contractual arrangements, the issuer and its subsidiaries do not have direct ownership of OPCO and rely on the structured contracts to control it. In light of the legal issues and potential risks associated with these arrangements, issuers should take necessary actions to ensure the legality and validity of the structured contracts and disclose all material and relevant information about the arrangements.

14. The guidance set out below is not exhaustive. Issuers should assess their own situation to decide whether additional actions or disclosures are appropriate to ensure compliance with the Listing Rules.

Factors to consider when adopting contractual arrangements

15. When an issuer proposes to acquire or establish a business using contractual arrangements which constitutes a notifiable and/or connected transaction, it is expected to observe the following:

(a) In general, where the relevant laws and regulations specifically restrict foreign investment (e.g. the Foreign Investment Law of the People's Republic of China) or disallow foreign investors from using any agreements or contractual arrangements to gain control of or operate the Restricted Business, the issuer should demonstrate that it is able to comply with the relevant laws and regulations.

(b) The contractual arrangements should be narrowly tailored to achieve the issuer's business purpose and minimise the potential for conflict with relevant laws and regulations:

(i) "Narrowly tailored" means that contractual arrangements may only be used to the extent necessary to address any limits on foreign ownership and the issuer should directly hold the maximum permitted interest in OPCO. For the avoidance of doubt, even if the issuer is able to control OPCO through the direct equity interest held by it in OPCO (e.g. by holding a direct equity interest of more than 50%), the remaining equity interest that is not permitted to be directly held by it may still be held through contractual arrangements.

(ii) Generally, where there is no foreign ownership restriction, an issuer must not use contractual arrangements for conducting its businesses unless there are exceptional circumstances. For instance, an issuer may use contractual arrangements if its non-Restricted Businesses are inseparable from the Restricted Businesses, and/or are immaterial in terms of revenue, profit or otherwise.

(c) A legal opinion must be provided in respect of the issuer's compliance with applicable laws and regulations and the articles of association of the domestic subsidiaries for the use of contractual arrangements.

The issuer should seek legal advice and decide what measures to adopt (if any) to fully comply with the relevant laws and regulations. The legal opinion on the contractual arrangements must include a positive confirmation that the use of the contractual arrangements does not constitute a breach of those laws and regulations or that the contractual arrangements will not be deemed invalid or ineffective under those laws and regulations. The legal opinion must be supported by appropriate regulatory assurance, where possible, to demonstrate the legality of the contractual arrangements.

Where OPCO's operations are in Mainland China, there should be a positive confirmation from the issuer's PRC legal adviser that the contractual arrangements would not be deemed as "concealing illegal intentions with a lawful form" and void under the PRC contract law.

(d) If OPCO, as a result of having foreign ownership, is required to obtain regulatory approval and fulfill additional eligibility standards (**Other Requirements**), the issuer must (i) fulfil the Other Requirements; and (ii) obtain the regulatory approval to directly hold the maximum permitted interest in OPCO prior to acquiring or establishing a business using contractual arrangements. However, if the relevant regulatory authority confirms that, notwithstanding having fulfilled the Other Requirements, it will not or cannot give the regulatory approval because there are no available procedures or guidance for granting approval or for policy reasons, the issuer can directly hold less than the maximum permitted interest in OPCO, provided that it demonstrates to the satisfaction of the Exchange that it has:

(i) reasonably assessed the requirements under all applicable rules, with the support of its legal advisers, and has committed financial and other resources; and

(ii) implemented all the legal adviser's recommendations prior to acquiring or establishing a business using contractual arrangements. A mere intent, undertaking or plan to implement such recommendations is not sufficient.

(e) The issuer should ensure that the contractual arrangements:

- include a power of attorney by which OPCO's Registered Owners grant to the issuer's directors and their successors (including a liquidator replacing the issuer's directors) the power to exercise all rights of OPCO's Registered Owners, including the rights to vote in a shareholders' meeting, sign minutes, and file documents with the relevant companies registry. OPCO's Registered Owners should ensure that the power of attorney does not give rise to any potential conflicts of interest. Where OPCO's Registered Owners are officers or directors of the issuer, the power of attorney should be granted in favour of the issuer and actions in relation to the contractual arrangements must be decided by officers or directors of the issuer who are not shareholders of OPCO;

- contain dispute resolution clauses that:

  - provide for arbitration and that arbitrators may award remedies over the shares or land assets of OPCO, injunctive relief (e.g. for the conduct of business or to compel the transfer of assets) or order the winding up of OPCO;

  - provide the courts of competent jurisdictions with the power to grant interim remedies in support of the arbitration pending formation of the arbitral tribunal or in appropriate cases. The courts of Hong Kong, the issuer's place of incorporation, OPCO's place of incorporation, and the place where the issuer or OPCO's principal assets are located should be specified as having jurisdiction for this purpose; and

- encompass dealing with OPCO's assets, and not only the right to manage its business and the right to revenue. This is to ensure that the liquidator, acting on the contractual arrangements, can seize OPCO's assets in a winding up situation for the benefit of the issuer's shareholders or creditors.

(f) Where the financial results of OPCO are to be accounted for and consolidated in the issuer's consolidated accounts as if it were a subsidiary of the issuer, the issuer should discuss with its auditors or reporting accountants to confirm that it has the right to do so under the prevailing accounting principles.

(g) It should put in place effective internal controls over the domestic subsidiaries and OPCO to safeguard its assets held through the contractual arrangements.

(h) It should terminate the contractual arrangements as soon as the law allows the business to be operated without them. It should ensure that OPCO's Registered Owners (and their successors) have undertaken to it that, subject to the relevant laws and regulations, they must return to the issuer any consideration they receive in the event that the issuer acquires OPCO's shares when terminating the contractual arrangements.

16. The issuer should make disclosure if there is any deviation from the above guidance. The Exchange will consider the circumstances of the case and where necessary for the protection of shareholders, require the issuer to take all necessary actions. In the case of a major or very substantial acquisition, the issuer will need to resolve all of the Exchange's concerns before it can proceed with the transaction[3].

Disclosure in announcements and circulars

17. The announcement and circular (if required) must contain sufficient details of the arrangements to enable shareholders to make an informed assessment of the transaction. These may include:

Details of the transaction and the assets being acquired

(a) a brief description of the relevant laws and regulations governing foreign investment restrictions and prohibitions, how the contractual arrangements are "narrowly-tailored" and other matters described in paragraph 15 above;

[3] Under the Listing Rules, the issuer must submit the draft circular of the transaction (and in the case of a very substantial acquisition, the draft announcement) to the Exchange for review before the document is issued.

(b) the reasons for the use of contractual arrangements in its business operation. If contractual arrangements are used due to reasons other than addressing foreign investment restrictions under paragraph 15(b) above, the justification thereof should be included (e.g. details of the non-Restricted Businesses, how they are inseparable from the Restricted Businesses, and their materiality in terms of revenue, profit or otherwise);

(c) the basis on which the terms of the contractual arrangements (including related restrictions and undertakings) can provide the issuer with control over all of OPCOs that are regarded as subsidiairies;

(d) the basis why the directors believe that each of the agreements conferring significant control and economic benefits from OPCO to the issuer is enforceable under the relevant laws and regulations;

(e) details of OPCO's Registered Owners and a confirmation that appropriate arrangements have been made to protect the issuer's interests in the event of death, bankruptcy or divorce of OPCO's Registered Owners to avoid any practical difficulties in enforcing contractual arrangements;

(f) the extent to which the issuer has arrangements in place to address the potential conflicts of interest between the issuer and OPCO's Registered Owners, particularly in cases where these shareholders are officers and directors of the issuer;

(g) corporate structure table for the purpose of illustrating the contractual arrangements and facilitating investors' review and understanding of the arrangements;

Financial information

(h) a separate disclosure of revenue from the businesses under the contractual arrangements if the target being acquired generates revenue from other subsidiaries apart from OPCO;

Other disclosures

(i) the economic risks the issuer bears as the primary beneficiary of OPCO, in what way the issuer shares the losses of OPCO, the circumstances that could require the issuer to provide financial support to OPCO, or other events or circumstances that could expose the issuer to losses;

(j) a discussion on whether the target being acquired has, to date, encountered any interference or encumbrance from any governing bodies in operating its business through OPCO under the contractual arrangements;

(k) the limitations in exercising the option to acquire ownership in OPCO, include a separate risk factor explaining these limitations, and clarifying that ownership transfer may still subject to substantial costs;

(l) other risks regarding the nature of the contractual arrangements, including that (i) the government may determine that the contracts do not comply with applicable regulations; (ii) the contractual arrangements may not provide control as effective as direct ownership; (iii) OPCO's Registered Owners may have potential conflicts of interest with the issuer; and (iv) the contractual arrangements may be subject to scrutiny of the tax authorities and additional tax may be imposed; and

(m) details of any insurance purchased to cover the risks relating to contractual arrangements, or a prominent disclosure that those risks are not covered by any insurance.

18. The issuer is recommended to publish the contractual arrangements on its website to promote transparency.

Disclosure in annual reports

19. An issuer is expected to keep shareholders informed of its business operations through contractual arrangements (whether by way of an acquisition or a greenfield project) subsisting during or at the end of the financial period in its annual reports where these operations are in aggregate material (see also Paragraph 9 of Appendix D2 to the MB Rules (GEM Rule 18.10)). These should include:

(a) particulars of OPCO and its Registered Owners, and a summary of the major terms of the contractual arrangements;

(b) a description of OPCO's business activities and their significance to the issuer group;

(c) appropriate quantitative information including revenue and assets subject to the contractual arrangements;

(d) the extent to which the contractual arrangements relate to requirements other than the foreign investment restriction;

(e) the reasons for using the contractual arrangements, the risks associated with the arrangements and the actions taken by the issuer to mitigate the risks;

(f) any material change in the contractual arrangements and/or the circumstances under which they were adopted, and its impact on the issuer group; and

(g) any termination of the contractual arrangements or failure to terminate when the restrictions that led to the adoption of the contractual arrangements are removed.

Continuing connected transactions

20. If OPCO and/or any of its Registered Owners is, or will become, a connected person of the issuer, the issuer should ensure compliance with Main Board Chapter 14A (GEM Chapter 20) for any continuing transactions with such person contemplated under the contractual arrangements unless they are exempt under the Listing Rules.

On-going developments

21. Listed issuers with contractual arrangements must continue to monitor future changes in the relevant laws and regulations and ensure compliance.

Whether certain special rights available to an investor under the terms of convertible bonds to be issued by a listed issuer would comply with the general principles in Rule 2.03

Parties

- **Company X** – a Main Board issuer
- **Investor** – an institutional investor which proposed to subscribe for convertible bonds to be issued by Company X

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**).

   c. 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.

Relevant Listing Rules

3. 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;
   ...

4. Rule 14A.36 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.

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

   4(3)[1] 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

6. 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)).

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

8. 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.

9. 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

10. 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.

[1] On 1 January 2022, paragraph 4(3) of Appendix 3 to the Rules was amended to replace the reference to "the issuer" with "members" to explicitly provide shareholders with the safeguard. The Rule amendment would not change the analysis and conclusion in this case.

Gambling activities of new listing applicants and listed issuers

I. Purpose

1. This letter provides guidance for new listing applicants and listed issuers that engaged in gambling activities. The guidance is also set out in Chapter 4.7 of the Guide for New Listing Applicants.

II. Guidance

General principles on suitability for listing

2. It would not be contrary to the public policy if an applicant's operations involve gambling activity that is not unlawful under relevant industry specific laws and regulations (e.g. the Gambling Ordinance (Cap. 148)[1]) and under the laws of the jurisdictions in which it takes place.

3. An applicant engaged in gambling activities must use its best endeavours to ensure that (i) it operates in a jurisdiction with an established licensing regime for gambling activities; and (ii) such activities comply with the applicable laws and regulations (including but not limited to regulatory requirements, licensing requirements and anti-money laundering laws), as well as government policies that regulate gambling activities (**Applicable Laws**).

4. If the applicant's operations of gambling activities fail to comply with the Applicable Laws where such activities take place; and/or contravenes the Gambling Ordinance (Cap. 148), it will be considered unsuitable for listing under MB Rule 8.04 (GEM Rule 11.06).

[1] Such gambling activity has the following features: (i) it takes place outside Hong Kong; and (ii) the bookmaking transactions and the parties to the transactions are outside Hong Kong.

Guidance on disclosure

5. An applicant should include:

(i) the types of gambling activities operated by the applicant;

(ii) the Applicable Laws, including how such laws and regulations are administered and enforced and the controls implemented by the applicant to comply with them;

(iii) confirmations from independent professional parties regarding the applicant's compliance status with all Applicable Laws, and the adequacy and effectiveness of its internal control measures implemented with respect to the operations of gambling activities and anti-money laundering; and

(iv) specific risks in relation to its gambling operations (including the risk of suspension and cancellation of listing should such gambling operations become illegal).

Post-listing requirements

6. Similar to applicants, listed issuers which invest directly or indirectly in gambling activities must use its best endeavours to ensure that, so long as its shares are listed on the Exchange, such gambling activities comply with the Applicable Laws.

7. For listed issuers acquiring or investing in a gambling business, the disclosure in paragraph 5 would be required in addition to the disclosure requirements under MB Chapters 14 and/or 14A or MB Rule 13.09 (GEM Chapters 19 and/or 20 or GEM Rule 17.10). The extent of additional disclosure would depend on the materiality of the transaction to the listed issuer.

8. Any announcement and/or circular of the listed issuer on its investment in relation to the operations of gambling activities must confirm that the gambling activities are lawful and highlight the risk of suspension and cancellation of listing should the operations of the gambling activities fail to fulfil the above legality requirement.

9. Should the operations of such gambling activities (i) fail to comply with the Applicable Laws in the jurisdictions where such activities take place; and/or (ii) contravene the Gambling Ordinance (Cap. 148), the listed issuer may be considered unsuitable for listing under MB Rule 8.04 (GEM Rule 11.06). Depending on the circumstances of the case, the Exchange may direct the issuer to take remedial actions, suspend dealings in, or may cancel the listing of, its securities pursuant to MB Rule 6.01 (GEM Rule 9.01).

Offers or distributions of entitlement securities by listed issuers to Southbound Shareholders under Stock Connect

1. When listed issuers propose pre-emptive issues (including rights issues, open offers, bonus issues and scrip dividend schemes) or distributions in specie to shareholders, should they offer or distribute entitlement securities to Mainland investors holding the issuers' securities through Shanghai and Shenzhen Connect (Southbound Shareholders)?

Yes.

MB Rule 13.36(1)(a)
First released: November 2014; last updated: May 2024

2. Are there additional PRC requirements for listed issuers to offer or distribute securities to Southbound Shareholders?

(a) Rights issues and open offers

Yes. The China Securities and Regulatory Commission (**CSRC**) has issued the Announcement [2016] No. 21 "Filing Requirements for Hong Kong Listed Issuers Making Rights Issues to Mainland Shareholders through Mainland-Hong Kong Stock Connect". The document sets out the requirements for listed issuers offering securities to their Southbound Shareholders in rights issues / open offers.

Listed issuers should also note that under Shanghai and Shenzhen Connect, China Securities Depository and Clearing Corporation Limited (**ChinaClear**) will provide nominee services for Southbound Shareholders to (i) sell their nil-paid rights on the Exchange; and/or (ii) subscribe for their entitlement securities under the rights issues / open offers in accordance with relevant laws and regulations. However, it will not support excess applications by Southbound Shareholders through Shanghai and Shenzhen Connect[1].

(b) Bonus issues, scrip dividend schemes and distribution in species

No rules or guidance has been published by the CSRC.

MB Rule 13.36(1)(a)
First released: November 2014; last updated: May 2024

[1] See Article 23 of ChinaClear's Implementing Rules for Registration, Depository and Clearing Services under Mainland-Hong Kong Stock Connect (**ChinaClear Stock Connect Implementing Rules**) 中國證券登記結算有限責任公司《內地與香港股票市場交易互聯互通機制登記、存管、結算業務實施細則》

3. MB Rule 13.36(2) states that an issuer may exclude overseas shareholders from a rights issue/open offer if, having made enquiries regarding the legal restrictions under the laws of the relevant place and the requirements of the relevant regulatory body or stock exchange, the directors of the issuer consider such exclusion to be necessary or expedient. Can Southbound Shareholders be excluded from participation in rights issues/open offers made by listed issuers?

No. Based on the CSRC Announcement [2016] No. 21 "Filing Requirements for Hong Kong Listed Issuers Making Rights Issues to Mainland Shareholders through Mainland-Hong Kong Stock Connect" which sets out the procedure for the filing of rights issue/open offer prospectus documents of listed issuers, the Listing Division does not consider that listed issuers have grounds to exclude the Southbound Shareholders from participation in the rights issues/open offers.

MB Rule 2.03 sets out the general principle expected to be upheld by listed issuers, and requires that (i) all holders of listed securities should be treated fairly and equally; and (ii) all new issues of equity securities, or sales or transfers of treasury shares, by a listed issuer should first be offered to the existing shareholders by way of rights unless they have agreed otherwise. This rule seeks to secure for holders of securities equality of treatment. Accordingly, on the basis of MB Rule 13.36, a listed issuer failing to make its rights issue/open offer available to the Southbound Shareholders will not be granted an approval for the listing of the rights/open offer shares by the Listing Division under MB Rule 2A.06.

MB Rules 2.03, 2A.06 and 13.36(2)(a)
First released: November 2014; last updated: June 2024

4. What are the additional considerations for listed issuers if the securities to be offered or distributed to shareholders are not eligible for trading under Shanghai and Shenzhen Connect?

The scope of securities eligible for southbound trading under the Shanghai and Shenzhen Connect (**Eligible Securities**) is set out in https://www.hkex.com.hk/Mutual-Market/Stock-Connect/Eligible-Stocks/View-All-Eligible-Securities?sc_lang=en[2].

Southbound Shareholders may receive different types of securities from listed issuers as entitlements under pre-emptive issues or distributions (e.g. warrants or convertible securities of the listed issuers, or shares of other entities):

- if the entitlement securities are not Eligible Securities but are listed on the Exchange, Southbound Shareholders may sell them on the Exchange through Shanghai and Shenzhen Connect, but they will not be allowed to buy such securities[3]; and

[2] The list contains securities eligible for both buy and sell through Shanghai and Shenzhen Connect.

[3] See Article 77 of SSE Stock Connect Pilot Provisions《上海證券交易所滬港通試點辦法》, Article 76 of SZSE Stock Connect Implementation Rules《深圳證券交易所深港通業務實施辦法》, and Article 24 of ChinaClear Stock Connect Implementation Rules

- if the entitlement securities are not listed on the Exchange, Southbound Shareholders will not be allowed to buy or sell the securities on the Exchange. HKSCC and ChinaClear will determine how to deal with the securities subscribed or received by Southbound Shareholders on an individual case basis[3].

Listed issuers are reminded of their obligation to treat all shareholders fairly and equally when they propose to offer or distribute securities to shareholders. They should consider making the following arrangements[4]:

- providing all shareholders with an option to receive their entitlements in cash rather than securities; and

- if the entitlement securities are not to be listed, offering a means for the shareholders to dispose of these securities.

Listed issuers should also make clear disclosures in their corporate communications about actions their shareholders need to take in respect of the offered/distributed securities.

MB Rule 2.03
First released: November 2014; last updated: May 2024

[4] See the Guide on distribution of dividends and other entitlements published on the HKEX website.

Listing fees

1. How will annual listing fees be calculated where the listed issuer's shares have no nominal value?

In the case of listed issuers whose shares cease to have a nominal value subsequent to their date of listing (**no-par event**), the nominal value per share that was used to calculate the annual listing fees immediately before the no-par event (**notional nominal value per share**), shall be used to calculate the annual listing fees from the no-par event (including any change in the annual listing fees payable under paragraphs 2(4) or 2(5) of MB Fees Rules (and the equivalent GEM Fees Rules)). If a listed issuer conducts a subdivision of shares after the no-par event, the notional nominal value per share shall be adjusted accordingly, subject to a minimum of HK$0.25 per paragraph 2(2) of MB Fees Rules (and the equivalent GEM Fees Rule).

For Hong Kong incorporated issuers listed before 3 March 2014, the notional nominal value per share from 3 March 2014 shall be the nominal value per share on 2 March 2014.

For Hong Kong incorporated issuers listed on or after 3 March 2014, we shall apply a nominal value of HK$0.25 per paragraph 2(2) of MB Fees Rules (and the equivalent GEM Rule) as we have done for other listed issuers with no nominal value per share or a nominal value per share < HK$0.25 for calculating annual listing fees.

Please see the **Appendix** for additional examples of annual listing fee calculations.

MB Fees Rules – 2(1)(a) and 2(2)
GEM Fees Rules – 1(2)(a)(i)
First released: February 2014; last updated: May 2024

Appendix

Calculating 2014 Annual Listing Fees for Hong Kong-Incorporated Issuers

Hong Kong-incorporated issuers listed before 3 March 2014
Annual listing fees for the remainder of 2014 (i.e. from 3 March 2014) and thereafter will be calculated by reference to the latest nominal value per share that was used to calculate the listed issuer's 2014 annual listing fees (i.e. the latest nominal value before the listed issuer's shares ceased to have a nominal value). Going forward, this will be known as the **notional nominal value per share**.

Hong Kong-incorporated issuers listed on or after 3 March 2014
The nominal value shall be deemed to be HK$0.25 for the purposes of calculating annual listing fees, in accordance with MB Fees Rules, paragraph 2(2). This is consistent with the current practice in respect of listed issuers with no nominal value per share or a nominal value per share less than HK$0.25.

The table below sets out examples showing the nominal value per share that will be used to calculate annual listing fees for Hong Kong-incorporated issuers on or after 3 March 2014 depending on their date of listing. These examples assume that the listed issuer does not carry out any corporate actions (e.g. subsequent issues, share subdivisions or consolidations).

Calculation of Annual Listing Fees (absent any corporate action)

Examples	Listing Date	Nominal value per share on 2 March 2014	Notional nominal value per share used to calculate annual listing fee on or after 3 March 2014	Effect of change on annual listing fee as compared to current regime
A	Before end of 2013	HK$1.00	HK$1.00	None
B	28 February 2014	HK$0.50	HK$0.50	None
C	3 March 2014	No nominal value	HK$0.25	None
D	3 July 2014	No nominal value	HK$0.25	None

Subsequent Issues

If a listed issuer conducts a placing, bonus issue, rights issue or open offer, or consideration issue on or after 3 March 2014 (when its shares cease to have a nominal value), we will calculate the annual listing fee payable for the remainder of that year based on the number of new shares issued and the notional nominal value per share.

The table below sets out examples showing the nominal value per share that will be used to calculate annual listing fees for Hong Kong-incorporated issuers from the date of a subsequent issue depending on the date of issue. Examples A, B & C are for issuers listed prior to 3 March 2014.

Calculation of Annual Listing Fees (in the event of a subsequent issue)

Examples	Date of subsequent issue	Nominal value per share at time of subsequent issue	Nominal value per share on 2 March 2014	Notional nominal value per share used to calculate annual listing fee from the date of subsequent issue	Effect of change on annual listing fee as compared to current regime
A	28 February 2014	HK$1.00	HK$1.00	HK$1.00	None
B	3 March 2014	No nominal value	HK$1.00	HK$1.00	None
C	3 September 2014	No nominal value	HK$1.00	HK$1.00	None
D: Issuer listed on or after 3 March 2014	3 October 2014[1]	No nominal value	No nominal value	HK$0.25[2]	None

[1] Note that no further issues of securities within six months of listing are generally allowed.

[2] For Hong Kong-incorporated issuers listed on or after 3 March 2014 that conduct a subsequent issue, the nominal value per share shall be deemed to be HK$0.25 for the purposes of calculating annual listing fees from the date of the issue.

Share Subdivision

If a listed issuer conducts a share subdivision on or after 3 March 2014, the notional nominal value per share will be adjusted accordingly, subject to a minimum of HK$0.25 per paragraph 2(2) of MB Fees Rules. The annual listing fee payable for the remainder of that year will be calculated based on the number of subdivided shares and this new nominal value per share.

The table below sets out examples showing the nominal value per share that will be used to calculate annual listing fees for Hong Kong-incorporated issuers from the date of a share subdivision depending on the date it is carried out. Examples A, B & C are for issuers listed prior to 3 March 2014.

Calculation of Annual Listing Fees (in the event of a share subdivision)

Examples	Date of subdivision	Nominal value per share before subdivision	Nominal value per share after subdivision	Nominal value per share on 2 March 2014	Notional nominal value per share used to calculate annual listing fee from the date of subdivision	Effect of change on annual listing fee as compared to current regime
A	28 February 2014	HK$1.00	(i) HK$0.50 (for a 2-for-1 split); or (ii) HK$0.10 (for a 10-for-1 split)	(i) HK$0.50 (for a 2-for-1 split); or (ii) HK$0.10 (for a 10-for-1 split)	(i) HK$0.50 (for a 2-for-1 split); or (ii) HK$0.25 (for a 10-for-1 split) (per Fees Rules, para 2(2))	None
B: Issuer conducts 2-for-1 split	3 March 2014	No nominal value	No nominal value	HK$1.00	HK$0.50	None
C: Issuer conducts 10-for-1 split	3 September 2014	No nominal value	No nominal value	HK$1.00	HK$0.25 Nominal value per shares after split would be HK$0.10. However, per Fees Rules, para 2(2), nominal value per share to calculate annual fee for remainder of the year would be HK$0.25.	None
D: Issuer listed on or after 3 March 2014	3 October 2014	No nominal value	No nominal value	No nominal value	HK$0.25[3]	None

[3] For Hong Kong-incorporated issuers listed on or after 3 March 2014 that conduct a share subdivision, the nominal value per share shall be deemed to be HK$0.25 for the purposes of calculating annual listing fees from the date of the subdivision.

Share Consolidation

If a listed issuer conducts a share consolidation on or after 3 March 2014, together with a capital reduction (a common market practice), the annual listing fee payable for the remainder of that year will be calculated based on the number of consolidated shares and the notional nominal value per share. Even if a listed issuer conducts a share consolidation on or after 3 March 2014 without an accompanying capital reduction, the annual listing fee payable for the remainder of that year will still be calculated by reference to the notional nominal value per share, as if the share consolidation had been carried out together with a capital reduction.

The table below sets out examples showing the nominal value per share that will be used to calculate annual listing fees for Hong Kong-incorporated issuers from the date of a share consolidation depending on the date it is carried out. Examples A1, A2, B1, B2, C1 & C2 are for issuers listed prior to 3 March 2014.

Calculation of Annual Listing Fees (in the event of a share consolidation)

Examples	Date of consolidation	Nominal value per share before consolidation	Nominal value per share after consolidation	Nominal value per share after capital reduction	Nominal value per share on 2 March 2014	Notional nominal value per share used to calculate annual listing fee from date of consolidation	Effect of change on annual listing fee as compared to current regime
A1: Issuer conducts 1-for-2 consolidation with capital reduction	28 February 2014	HK$0.50	HK$1.00	HK$0.50	HK$0.50	HK$0.50	None
A2: Issuer conducts 1-for-2 consolidation without capital reduction	28 February 2014	HK$0.50	HK$1.00	[No capital reduction carried out]	HK$1.00	HK$1.00	None
B1: Issuer conducts 1-for-2 consolidation with capital reduction	3 March 2014	No nominal value	No nominal value	No nominal value	HK$0.50	HK$0.50	None

Examples	Date of consolidation	Nominal value per share before consolidation	Nominal value per share after consolidation	Nominal value per share after capital reduction	Nominal value per share on 2 March 2014	Notional nominal value per share used to calculate annual listing fee from date of consolidation	Effect of change on annual listing fee as compared to current regime
B2: Issuer conducts 1-for-2 consolidation without capital reduction	3 March 2014	No nominal value	No nominal value	[No capital reduction carried out]	HK$0.50	HK$0.50 Under current regime, nominal value per share after consolidation would be HK$1.00. Under new regime, nominal value per share on 2 March 2014 (HK$0.50) will still be used to calculate annual listing fee from date of consolidation.	Decrease
C1: Issuer conducts 1-for-2 consolidation with capital reduction	3 September 2014	No nominal value	No nominal value	No nominal value	HK$0.25	HK$0.25	None
C2: Issuer conducts 1-for-2 consolidation without capital reduction	3 September 2014	No nominal value	No nominal value	No capital reduction carried out	HK$0.25	HK$0.25 Under current regime, nominal value per share after consolidation would be HK$0.50. Under new regime, nominal value per share on 2 March 2014 (HK$0.25) will still be used to calculate annual listing fee from date of consolidation.	Decrease

Examples	Date of consolidation	Nominal value per share before consolidation	Nominal value per share after consolidation	Nominal value per share after capital reduction	Nominal value per share on 2 March 2014	Notional nominal value per share used to calculate annual listing fee from date of consolidation	Effect of change on annual listing fee as compared to current regime
D: Issuer listed on or after 3 March 2014 conducts 1-for-2 consolidation (with/without capital reduction)	3 October 2014	No nominal value	No nominal value	Where capital reduction carried out: No nominal value	No nominal value	HK$0.25[4]	None

[4] For Hong Kong-incorporated issuers listed on or after 3 March 2014 that conduct a share consolidation, the nominal value per share shall be deemed to be HK$0.25 for the purposes of calculating annual listing fees from the date of the consolidation.