

Applicant	Background and Decision
<p><b>Company A</b> (MB applicant) (2004, updated rule reference in 2009)</p> <p>Rule reference: MB Rules 2.13, 8.04, 8.05(1)(c), 11.07</p>	<p><i>Background</i></p> <ol style="list-style-type: none"> <li>1. To prepare for the IPO of the shares of Company A (the “<b>Shares</b>”), a group reorganisation was effected shortly before the IPO.</li> <li>2. Pursuant to the reorganisation, the shares of the only operating company of Company A (the “<b>Principal Subsidiary</b>”) were exchanged for the Shares of Company A, such that, at the time of listing, Company A became the holding company of the Principal Subsidiary and the shareholders of the Principal Subsidiary became the shareholders of Company A.</li> <li>3. The pre-IPO shareholders had previously acquired the shares of the Principal Subsidiary (through share acquisitions and injections of capital) at different times during the track record period but all shortly before the IPO.</li> <li>4. The consideration paid for each of the acquisitions and injections of capital by the pre-IPO shareholders was established by reference to the total net asset valuation of the shares of the Principal Subsidiary as valued by independent valuers at the relevant time.</li> <li>5. Independent valuations were required as the transactions involved disposals of assets by vendor companies which were PRC state-owned enterprises (“<b>SOEs</b>”).</li> <li>6. There was a material difference in the net asset value shown in the accountants’ report included in the listing document prepared for the IPO and the net asset value of the Principal Subsidiary as shown in the valuation reports prepared by independent valuers for share acquisitions by pre-IPO investors shortly before the IPO. All the valuations were purported to establish the net asset value of essentially equivalent assets, yet the valuations had increased substantially within a short interval.</li> <li>7. There was a material disparity between the IPO price of the Shares and the effective cost of acquisition of the Principal Subsidiary’s shares by the pre-IPO shareholders.</li> <li>8. The material difference in the asset valuations occurring within such a short period of time gave rise to a few concerns: <ol style="list-style-type: none"> <li>(i) Whether the interests of the PRC SOE vendor companies which disposed the shares of the Principal Subsidiary might have been unfairly prejudiced, which led to the question of whether the disposals by those PRC SOEs could be legally challenged;</li> <li>(ii) The significant difference in value between the IPO price of the Shares and the effective cost of pre-IPO shareholders of the shares acquired by them meant that new purchasers of the Shares would suffer a material degree of dilution in share value (by comparing the IPO price to the pro forma adjusted combined net tangible book value of the Shares as stated in the listing document); and</li> </ol> </li> </ol>

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	<p data-bbox="421 255 1455 358">(iii) The pre-IPO shareholders would experience a gain in share value from their recent pre-IPO acquisitions of shares of the Principal Subsidiary at a price based on a substantially lower net asset valuation.</p> <p data-bbox="363 394 472 425"><i>Decision</i></p> <p data-bbox="363 463 831 495">9. The Exchange took into account:</p> <p data-bbox="421 533 1455 703">(i) The requirement that shareholders of an applicant have good title to the shares that are free from third party claims. The burden of proof is on the sponsor and the applicants' directors to demonstrate that the pre-IPO shareholders of an applicant hold the shares in good faith and in accordance with all relevant laws and regulations with supporting evidence; and</p> <p data-bbox="421 741 1455 1048">(ii) If there is a material difference in the valuations of all or a material portion of the assets of the applicant or those of its predecessor within a short period of time prior to listing, such facts would give rise to a concern of whether the title to the shares of the applicant or of its predecessor could be challenged by the vendors of those shares due to undervalued pre-IPO sale and purchase transactions. The Exchange was empowered under the Listing Rules to require a higher level of assurance from the applicant and its professional advisers to ensure the legality of all previous acquisitions of or injections of capital for shares in any member of the group before listing.</p> <p data-bbox="363 1086 1455 1393">10. In view of the above, Company A and its sponsor and professional advisers were required to demonstrate to the Exchange the legality of the various pre-IPO share acquisitions and injections of capital in the Principal Subsidiary shortly before listing that resulted in the material disparity in the valuations of the Shares within a short period of time. Based on the further submissions from the sponsor and the legal opinions of the PRC legal adviser that Company A had complied with all relevant PRC laws and regulations, the Exchange was satisfied that Company A had provided proper evidence to demonstrate legality of the pre-IPO share acquisitions and injections of capital.</p> <p data-bbox="363 1431 1455 1601">11. Given the material disparity in pricing, the Exchange expects that the applicant's directors and sponsor assume responsibility under MB Rules 2.13 and 11.07 to ensure that such material information is included prominently in the listing document. In addition, the listing document was required to include the following prominent disclosures and add corresponding risk factors, where relevant:</p> <p data-bbox="421 1639 1455 1704">(i) Statements regarding the legality of the acquisitions of shares and injections of capital in the Principal Subsidiary prior to listing;</p> <p data-bbox="421 1742 1455 1807">(ii) The historical costs paid by the pre-IPO shareholders and the valuations of the Principal Subsidiary at different points of time; and</p> <p data-bbox="421 1845 1455 2016">(iii) Quantitative disclosure of the dilution in share value that new investors purchasing Shares at the IPO would suffer. In the present case, the dilution in share value should be expressed as a comparison between the IPO price and the pro forma adjusted combined net tangible book value immediately after the IPO on a per share basis.</p>

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	<p>12. It is the general practice for the cost of investment in the shares of the applicant, in total and in per share basis, to be disclosed in tabular format.</p>
<p><b>Company B</b> (MB applicant) (2011)</p> <p>Rule reference: MB Rules 2.03(2), 2.03(4)</p>	<p><i>Background</i></p> <ol style="list-style-type: none"> <li>1. Company B entered into a loan agreement with independent third parties (<b>"Lenders"</b>).</li> <li>2. The loan was conditional on the controlling shareholders issuing Warrants A and Warrants B (<b>"Warrants"</b>) to the Lenders.</li> <li>3. The terms of the Warrants enabled the Lenders to exercise Warrants A in whole or in part to purchase up to 12% of Company B's enlarged issued share capital at a pre-determined price upon listing.</li> <li>4. The Lenders could also exercise Warrants B to acquire less than 1% of Company B's enlarged issued share capital for free once the IPO price of Company B's shares was finalised.</li> <li>5. The Lenders could also opt for cash settlement in lieu of shares.</li> <li>6. More than 28 days before Company B submitted its listing application, the loan had been fully drawn down but the Warrants remained exercisable on the date of the listing application.</li> </ol> <p><i>Decision</i></p> <ol style="list-style-type: none"> <li>7. The Exchange considered the following and determined that the Pre-IPO Investment Guidance (as defined in <b>Chapter 4.2</b>) was applicable to the issue of shares upon exercise of the Warrants:             <ol style="list-style-type: none"> <li>(i) The Warrants would entitle the Lenders to Company B's shares shortly before its listing and thus constituted a pre-IPO investment;</li> <li>(ii) The loan and the Warrants were separate transactions, although the issue of the Warrants was one of the conditions precedent to the loan agreement;</li> <li>(iii) The injection of the loan was not a settlement of the consideration for the shares under the Warrants; and</li> <li>(iv) As the Lenders had not settled the consideration for the shares under the Warrants more than 28 days before Company B submitted its listing application, the pre-IPO investment in Company B was not considered completed as the funds had not been irrevocably settled and received by Company B.</li> </ol> </li> </ol> <p><i>Developments after the decision</i></p> <ol style="list-style-type: none"> <li>8. The Exchange requested Company B to adjust the terms of the pre-IPO investment to comply with MB Rules 2.03(2) and 2.03(4) or defer its listing date to six months after the payment date.</li> </ol>

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	<ol style="list-style-type: none"> <li data-bbox="360 259 1455 394">9. The Lenders and the controlling shareholders cancelled the Warrants, with the latter compensating the Lenders with cash. As Company B would not be the party to compensate the Lenders, the Exchange considered that the interests of the investing public were not prejudiced.</li> <li data-bbox="360 427 1455 562">10. Since an interest expense arising from the Warrants had been recognised and was reflected in Company B's profit forecast, the Exchange requested Company B to make prominent disclosure of the expense in its listing document, including a subsequent event disclosure in the accountants' report.</li> </ol>