

## Part B Consultation Questions

Please indicate your preference by checking the appropriate boxes. Please reply to the questions below on the proposed change discussed in the Consultation Paper downloadable from the HKEx website at: <http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201304.pdf>

Where there is insufficient space provided for your comments, please attach additional pages.

### Chapter III: Plain Language Amendments to Connected Transaction Rules

1. Do you support the proposal to re-write Chapter 14A?

Yes

No

If your answer is “No”, please give reasons for your views.

2. Do you consider that the draft new Chapter 14A in Appendix I of the Consultation Paper accurately reflects the current Chapter 14A?

Yes

No

If your answer is “No”, please give reasons for your views.

3. Do you have any other comments on the draft Rule amendments in Appendix I of the Consultation Paper?

Yes

No

If your answer is “Yes”, please elaborate your views.

- Please consider if the concept of shareholders' approval set out in the note to the new Rule 13.39 should be aligned with that set out in the new Rule 14A.36.
- New Rule 14A.15(1) – We suggest clarifying that the subsidiary can be either directly or indirectly wholly-owned by the issuer for clarity purposes.
- New Rule 14A.28 – We suggest to clarify that the issuer will not be considered an "associate" of a controller (see existing Rule 14A.13).
- New Rules 14A.40(2) and 14A.45(2) – We suggest that the “in the group’s ordinary and usual course of business” requirement should only be applicable to continuing connected transactions. In practice, a lot of one-off connected transactions (e.g. acquisition/disposal of a business) are not transactions conducted “in the ordinary and usual course of business”.
- New Rule 14A.80(4) – It would be helpful if you could clarify whether the lapse of an option (upon the expiration of the option period) would be regarded as a “decision not to exercise” the option under this rule.
- New Rule 14A.91(2) and related provisions – Please consider whether there is room for relaxation of this rule on the basis that financial assistance may be provided on a secured basis but still on normal commercial terms. Further, it would be helpful if you could clarify how the size test should be calculated in case a security is granted in favour of a connected person (e.g. whether value of the assets subject to the security or only the secured amount should be taken into account for the consideration test).
- The reference to “or, if there are not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms no less favourable to the listed issuer than terms available to or from independent third parties” in the existing Rule 14A.37(2) is not reflected in the corresponding new rules. Is that intended?
- Please also see our responses to specific questions below.

## **Chapter IV: Scope of Connected Persons and Connected Transactions**

### **Part 1 – Scope of connected persons**

#### **A. Definition of connected person**

##### **A(1) Connected persons at the issuer level**

4. Do you agree that there is no need to extend the definition of connected person to the key management personnel of an issuer's controlling shareholder/holding company?

Yes

No

If your answer is "No", please give reasons for your views.

## A(2) Connected persons at the subsidiary level

5. Do you support:

- (a) the proposal described in paragraph 90(a) of the Consultation Paper to require transactions with persons connected only at the subsidiary level be subject to the approval of the issuer's board members (including independent non-executive directors) who do not have a material interest in the transaction, instead of the approval of shareholders, and disclosed to the shareholders?

Yes

No

If your answer is "No", please give reasons for your views.

- (b) the proposal described in paragraph 90(b) of the Consultation Paper to exempt all transactions between the issuer group and connected persons at the subsidiary level, other than transactions between a subsidiary (or any subsidiary below it) and the person connected with that subsidiary?

Yes

No

If your answer is "No", please give reasons for your views.

**B. The deeming provision**

6. Do you agree with the proposal to introduce principle-based tests described in paragraph 95 of the Consultation Paper for deeming a person as connected?

Yes

No

If your answer is “No”, please give reasons for your views.

**C. Exceptions to the definition of connected person**

**C(1) Insignificant subsidiary exemption (if persons connected at the subsidiary level are not excluded from the definition of connected person)**

7. Do you agree with the proposal described in paragraph 100 of the Consultation Paper to exempt all persons connected only because of its relationship with the issuer's insignificant subsidiaries?

Yes

No

If your answer is "No", please give reasons for your reviews.

**C(2) Exemption for trustee interests**

8. Do you agree with the proposal described in paragraph 105 of the Consultation Paper to exclude from the definition of associate any trustee of an employee share scheme or occupational pension scheme if the connected persons' interests in the scheme are less than 10%?

Yes

No

If your answer is "No", please give reasons for your views.

**C(3) Exemption for connected person holding an interest in an associate through the issuer**

9. Do you agree with the proposal described in paragraph 110 of the Consultation Paper to clarify that the exemption in Note 1 to Rule 14A.11(4) (paragraph 9 of the Guide) would apply if the connected person and his associate’s interests in the entity (other than those held through the issuer) are less than 10%?

Yes

No

If your answer is “No”, please give reasons for your views.

Let's look at Scenarios 1 and 2 in paragraph 108 (assuming the “additional shareholding” in Scenario 2 is 10% or more as proposed in paragraph 110). In Scenario 2, Company B will already be a “connected subsidiary”. In Scenario 1, Company B will be a connected person so long as it is 30% controlled by the issuer (irrespective of whether it is a subsidiary of the issuer). This represents an extension of the “connected subsidiary” concept, and we wonder if it is necessary. It is already a recognized principle that the connected person’s interest in the entity through his shareholding in the issuer is the same as other shareholders of the issuer. We query whether the fact that a controlling shareholder is holding more than 50% of the issuer (but not between 30% and 50%) really makes any difference. From a practical point of view, the new rule may complicate the connected person analysis of issuers with a controlling shareholder holding over 50% of its shares. It also means that the issuer would have to re-do its connected person analysis when a controlling shareholder acquires shares to above 50%. On balance, we suggest to simply adopt the existing “connected subsidiary” concept in Rule 14A.11, which would appear more consistent with the existing rules.

In terms of drafting, the additional language in the new Rule 14A.11 appears to suggest that if a connected person (the “Primary Connected Person”) holds 10% or more in a company (the “Relevant Company”), the Relevant Company will also become a connected person so long as the Primary Connected Person indirectly holds any interest in the Relevant Company through the issuer group (no matter how insignificant). Such interpretation would not be in line with the illustrations in Scenarios 1 and 2 in paragraph 108. Clarification may be needed.

Diagram 7 may need to be modified to provide clearer guidance as to how this provision works. Reference can be made to Scenarios 1 and 2 of paragraph 108.

## Part 2 – Scope of connected transactions

### D. Financing arrangements with a commonly held entity

10. Do you agree that we should retain the connected transaction requirements for financing arrangements with commonly held entities?

Yes

No

If your answer is “No”, please give reasons for your views.



**E. Buying or selling interests in a target company**

11. Do you agree with the proposal described in paragraph 131(a) of the Consultation Paper to restrict Paragraph (i) of Rule 14A.13(1)(b) (paragraphs 27 to 29 of the Guide) to transactions involving controllers at the issuer level?

Yes

No

If your answer is “No”, please give reasons for your views.

12. Do you agree with the proposal described in paragraph 131(b) of the Consultation Paper to exclude disposals of interests in target companies from Paragraph (i) of Rule 14A.13(1)(b) (paragraphs 27 to 29 of the Guide)?

Yes

No

If your answer is “No”, please give reasons for your views.

13. Do you agree with the proposal described in paragraph 131(c) of the Consultation Paper to remove Paragraphs (ii) to (iv) of Rule 14A.13(1)(b) (paragraphs 31 and 32 of the Guide)?

Yes

No

If your answer is “No”, please give reasons for your views.

## Chapter V: Connected Transaction Requirements

### F. Compliance framework for continuing connected transactions (“CCTs”)

14. Do you consider that information provided to shareholders regarding CCTs conducted under framework agreements contains sufficient specificity, in particular as to the methods or procedures to determine pricing for investors to make informed decisions?

Yes

No

If your answer is “No”, please also state the information that you consider should be disclosed in announcements and circulars.

Please give reasons for your views.

15. Do you consider that the current Rules governing CCTs and market practice in relation to CCTs that are conducted under framework agreements are appropriate? Do they provide sufficient safeguards to ensure that the transactions will be on normal commercial terms and will not be prejudicial to the interests of the issuers and its minority shareholders?

Yes

No

Please give reasons for your views.

## F(1) Written agreements

16. Do you agree with the proposal to codify the waiver practice to allow an issuer to obtain a shareholders' mandate (or a mandate from the board if the transactions is exempt from the shareholder approval requirement) in lieu of a framework agreement with the connected person?

Yes

No

If your answer is "No", please give reasons for your views.

17. If your answer to Question 16 is 'Yes':

- (a) Do you agree to limit the mandate period to not more than 3 years?

Yes

No

If your answer is "No", please give reasons for your views.

- (b) Do you agree with the waiver conditions described in paragraph 151 of the Consultation Paper?

Yes

No

If your answer is "No", please give reasons for your views.

## **F(2) Annual cap**

18. Do you support the proposal to allow the cap for a CCT of a revenue nature be expressed a percentage of the issuer's annual revenue or other financial items in its published audited accounts?

Yes

No

If your answer is "No", please give reasons for your views.

Should such relaxation also apply to financial assistance if it is granted as part of another continuing connected transaction on normal commercial terms (e.g. trade credit)?

## **F(3) Auditors' confirmation letter**

19. Do you support the proposal described in paragraph 161 of the Consultation Paper to modify the Rules relating to auditors' confirmation on CCTs in line with PN 740?

Yes

No

If your answer is "No", please give reasons for your views.

## **G. Requirements for connected transactions involving option arrangements**

### **G(1) Transfer or non-exercise of option**

20. Do you agree with the proposed alternative classification Rules for any transfer or non-exercise of an option?

Yes

No

If your answer is “No”, please give reasons for your views.

We agree to this in principle, with the following modifications:

- We suggest that the alternative classification rules should apply without the need for an express permission from the Exchange, as safeguards would be in place pursuant to the new 14A.80(4)(b).
- We suggest that the new Rules 14A.80(4)(b)(i) and (ii) should be combined – the amount payable or receivable by the group should be factored into the “exercise price” in making the calculation under (i) (and then (ii) should be removed). The current “higher of” approach would render (i) obsolete in most cases.
- The new Rule 14A.80(4)(b) – We suggest that different treatment should be accorded to a call option scenario and a put option scenario. If the exercise price for a call option held by the issuer is substantially higher than the value of the assets, the issuer board should have the power to decide whether to exercise the option and the matter should not have to be put to the shareholders for approval. The current drafting may require the issuer to meet a higher compliance standard when such premium/gap is bigger (and the other way round for a put option).

## G(2) Termination of option

21. For any termination of an option involving a connected person:

- (a) Do you agree with the proposal described in paragraph 170 of the Consultation Paper to classify the termination as if the option is exercised unless the issuer has no discretion over the termination?

Yes

No

If your answer is “No”, please give reasons for your views.

Please consider specifying in the new Rule 14A.80(4) that the provision would not apply if the issuer has no discretion over the termination. Please also clarify whether the lapse of an option (e.g. upon expiration of the option period) would be regarded as a “decision not to exercise”.

- (b) Do you agree that the proposed alternative classification Rules described in paragraph 166 of the Consultation Paper should also apply to the termination?

Yes

No

If your answer is “No”, please give reasons for your views.

Please see above.

**H. Minor changes to clarify the requirements relating to independent advice on connected transactions**

22. Do you agree with the proposed Rule change to clarify that the independent board committee also needs to advise whether the connected transaction is on normal commercial terms and in the issuer’s ordinary and usual course of business?

Yes

No

If your answer is “No”, please give reasons for your views.

New Rules 14A.40(2) and 14A.45(2) – We suggest that the “in the group’s ordinary and usual course of business” requirement should only be applicable to continuing connected transactions. In practice, a lot of one-off connected transactions (e.g. acquisition/disposal of a business) are not transactions conducted “in the ordinary and usual course of business”.

## Chapter VI: Exemptions for Connected Transactions

### I. De minimis exemptions

23. Do you agree that we should retain the monetary limit of HK\$1 million for fully exempt connected transactions?

Yes

No

If your answer is “No”, do you think that the limit should be increased to HK\$2 million, HK\$3 million, HK\$4 million, HK\$5 million, or some other amount (*please specify with reasons*)?

HK\$2 million

HK\$3 million

HK\$4 million

HK\$5 million

Other amount (*please specify*):

Please give reasons for your views.

24. Do you agree that we should retain the monetary limit of HK\$10 million for connected transactions exempt from the shareholder approval requirements?

Yes

No. The appropriate limit should be (*please specify*): **HK\$50 million**

Please give reasons for your views.

We suggest a 10 times multiple to the amount specified in question 23 above.



**J. Exemption for provision of consumer goods or services**

25. Do you support the proposal described in paragraph 181 of the Consultation Paper to remove the 1% cap on transaction value for the exemption for provision or receipt of consumer goods or services?

Yes

No

If your answer is “No”, please give reasons for your views.

**K. Exemption for provision of director’s indemnity**

26. Do you agree with the proposal described in paragraph 183 of the Consultation Paper to exempt an issuer granting indemnity to a director against liabilities that may be incurred in the course of the director performing his duties, if it does not contravene any law of the issuer’s place of incorporation?

Yes

No

If your answer is “No”, please give reasons for your views.

27. Do you agree with the proposal described in paragraph 186 of the Consultation Paper to exempt an issuer purchasing and maintaining insurance for a director against liabilities to third parties that may be incurred in the course of performing his duties, if it does not contravene any law of the issuer’s place of incorporation?

Yes

No

If your answer is “No”, please give reasons for your views.

28. Do you have any other comments or suggestions relating to the connected transaction Rules?

Yes

No

If your answer is “Yes”, please elaborate your views.

Please see our responses above.

- End -