

HKEx REJECTION LETTER
Cite as HKEx-RL18-07 (February 2007)

[Withdrawn in March 2019]

Summary	
Listing Rule	GEM Listing Rule 11.06
Reason for rejection and the subsequent disposal of the case on review	<p>The GEM Listing Committee rejected the listing application of the Company for the reason that the Group should not be considered suitable for listing under GEM Listing Rule 11.06 in light of the various issues arising from an anonymous complaint relating to the Company's borrowings from its employees.</p> <p>The GEM Listing (Review) Committee decided to overturn the decision of the GEM Listing Committee, subject to certain specified conditions.</p>
Contents	<p><u>LETTER 1:</u> Extracts of the decision letter of the Secretary to the GEM Listing Committee</p> <p><u>LETTER 2:</u> Extracts of the decision letter of the Secretary to the GEM Listing (Review) Committee on hearing of the Company's application to review the decision of the GEM Listing Committee</p>

LETTER 1

[Date]

[Name and Address of Sponsor]

Dear Sirs

Re: Application for new listing of a GEM listing applicant
(the "Company" together with its subsidiary, the "Group")

We refer to your application Form 5A dated *[*day*month*year]* made on behalf of the Company (the "Application") and the hearing proof of the Company's prospectus dated *[*day*month*year]* (the "Prospectus"). Capitalised terms used herein shall have the same meanings as defined in the Prospectus, unless the context otherwise requires.

The Company's listing application was originally considered by the GEM Listing Committee on *[*day*month*year]*. Subsequent to the meeting, the Listing Division received an anonymous complaint relating to the Company's borrowings from its employees (the "Complaint") which gave rise to new information to be considered.

At the GEM Listing Committee meeting held on *[*day*month*year]* which *[names of members purposely omitted]* attended, the GEM Listing Committee reconsidered the Company's listing application and resolved that the Group should not be considered suitable for listing under GEM Listing Rule 11.06 in light of the various issues arising from the Complaint. The analysis and conclusion are set out below.

Relevant Facts

As disclosed in the Prospectus, during the Track Record Period (comprising *[Year 1, Year 2 and Year 3]*) the Group had borrowings aggregating approximately HK\$200 million as at 31 December *[Year 1]* from approximately 2,000 employees to partly finance the Group's operation and development. Such borrowings did not comply with the relevant PRC laws and the relevant loan agreements were not legally enforceable. The Group fully repaid such borrowings during *[Year 2]*.

Subsequent to the GEM Listing Committee meeting of *[*day*month*year]* when the Company's listing application was approved in-principle, the Listing Division received the Complaint. Upon enquiries with the Sponsor on the allegations therein, additional information not disclosed in the Prospectus nor submitted to the Listing Division previously was revealed as follows:

- (a) Upon repayment of the HK\$200 million employee loans in *[Year 2]*, some employees voluntarily made certain investment arrangements with *[Entity X]* in the aggregate amount of HK\$150 million and designated the sum for *[Entity X's]* on-lending to the Company. The Company's subsequent borrowings from *[Entity X]* up to approximately HK\$300 million as at 31 December *[Year 3]* were wholly funded by the Group's employees in the form of such designated loans;
- (b) A number of employees entered into the investment arrangements with *[Entity X]* on behalf of approximately 2,000 employees based on verbal agreement and personal relationship among them; and
- (c) A separate loan agreement was entered into between *[Entity X]* and the Company.

The Applicable GEM Listing Rules

GEM Listing Rule 11.06 states that *"Both the issuer and its business must, in the opinion of the Exchange, be suitable for listing."*

GEM Listing Rule 11.12(1) states that a new applicant must demonstrate that, throughout the period specified in Rule 11.12(2), it has actively pursued one focused line of business and must make a statement in the listing document concerning that business which complies with the requirements of Rules 14.15 to 14.18.

Note 3 to GEM Listing Rule 11.12 further provides that a new applicant must be able to demonstrate that it has a business of both substance and potential. A business will, subject to Rule 11.14, only be regarded as having the requisite substance if the applicant can show that it has spent at least the 24 month period prior to the issue of the listing document

making substantial progress in building up that business. Examples of measurements of progress have been given under Note 4 to Rule 14.15. Among other things, item (h) under Note 4 to Rule 14.15 cites “funding arrangement (such as the equity and debt finance previously obtained)” as a relevant measurement of progress.

GEM Listing Rule 2.18 states that “*The directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief:-...there are no other matters the omission of which would make any statement in this document misleading...*”

GEM Listing Rule 5.01 states that “*The board of directors of an issuer is collectively responsible for the management and operations of the issuer. The Exchange expects the directors, both collectively and individually, to fulfil fiduciary duties and duties of skill, care and diligence to a standard at least commensurate with the standard established by Hong Kong law. This means that every director must, in the performance of his duties as a director:- act honestly and in good faith in the interests of the company as a whole,...*”

GEM Listing Rule 5.02 states that “*Every director must satisfy the Exchange that he has the character, experience and integrity and is able to demonstrate a standard of competence commensurate with his position as a director of an issuer...The Exchange expects every director of an issuer: - (1) to be cognizant of the GEM Listing Rules and reasonably familiar with the obligations and duties imposed upon him and the issuer pursuant to the GEM Listing Rules...*”

The Analysis and Conclusion

Substance and Potential

In order to comply with GEM Listing Rule 11.12, an applicant must, inter alia, demonstrate that it has a business of both substance and potential, which means that it has spent at least 24 months making substantial progress in building up that business. Funding arrangements are an example of measurement of progress pursuant to GEM Listing Rule 14.15. The Company’s borrowings from its employees (directly or indirectly in the form of designated loans) had increased from HK\$200 million at the end of [Year 1] to HK\$250 million and HK\$300 million at the end of [Year 2] and [Year 3], representing 35% or more of the Group’s total borrowings at the end of [Year 1], [Year 2] and [Year 3] respectively.

From the above, while the GEM Listing Committee noted that the Company has over the years built up an established business, it is of the view that the Company made less progress during the active business pursuits period in obtaining sufficient bank financing than had been considered at the time the original approval in-principle was granted.

Omissions of Material Information in the Prospectus

Although the legal forms of the investment arrangement between the employees and [Entity X] and the loan agreement between the Company and [Entity X] appeared to entail separate obligations and commitments, they were in essence a tailor-made arrangement to enable the Company to obtain financing indirectly from its employees without violating the relevant PRC laws. Therefore, the two transactions together form material information for potential investors to assess the true financial position of the Group and should be

disclosed together to reflect the substance of the arrangement. Simply disclosing the loans from [Entity X] and the repayment of the employee loans in [Year 2] without stating the link between them was considered to be incomplete and possibly misleading to potential investors, who would not be able to assess fully the operational and financial position of the Company as the current disclosure in the Prospectus would give investors an impression that the Group was able to obtain sufficient funding from financial institutions and no longer relies on the funding from its employees.

Directors' Suitability

Pursuant to GEM Listing Rule 2.18, the directors of the Company are collectively and individually responsible for the accuracy and completeness of the contents of the Prospectus.

Based on the above analysis that there has been omission of material information in the Prospectus, the GEM Listing Committee considered that the directors' integrity as required under GEM Listing Rules 5.01 and 5.02 would be questionable.

Conclusion

The GEM Listing Committee, having considered the following relevant issues in totality:

- (a) substance and potential of the Company's business;
- (b) omission of material information in the Prospectus; and
- (c) suitability of directors of the Company,

is of the view that the Company is not suitable for listing pursuant to GEM Listing Rule 11.6.

Pursuant to Rule 4.07(1) of the GEM Listing Rules, the Company has the right to have this decision reviewed by the GEM Listing (Review) Committee.

[Portion of Letter Purposely Omitted]

Yours faithfully,
For and on behalf of
The Stock Exchange of Hong Kong Limited

[Signed]

Secretary to the GEM Listing Committee

LETTER 2

[Date]

[Name and Address of Sponsor]

Dear Sirs,

Re: Review Hearing of the GEM Listing (Review) Committee
(the "Review Hearing") regarding the Company
Date of the Review Hearing: [* day* month * year]

On [*day*month*year], the GEM Listing (Review) Committee of The Stock Exchange of Hong Kong Limited conducted a review hearing (the "Review Hearing") to consider an application from the Company for a review of the decision of the GEM Listing Committee of [*day*month*year] and set out in the [LETTER 1] dated [* day*month* year] (the "First Decision").

The Review Hearing was conducted before the GEM Listing (Review) Committee comprising [names of members purposely omitted] (the "Review Committee").

Decision

The Review Committee considered the submissions (both written and oral) made by the relevant parties to the review. The Review Committee remained troubled by the failure of the Company, and the failure of the Company's advisers in advising the Company, to make timely disclosure of the investment arrangements involving the Company's employees when, clearly, the Company's advisers were in possession of details of these arrangements at an early stage. However, based on the submissions, the Review Committee decided to overturn the First Decision, subject to the following conditions which should be complied with to the satisfaction of the Listing Division:

1. The Company should make more prominent and full disclosure in the prospectus of the relevant investment arrangements between the Company's employees and [Entity X] and the relevant loan agreement between the Company and [Entity X]. The Review Committee was of the view that the disclosure made in the draft prospectus dated [*day*month*year] (hearing proof), in particular in the "Risk Factors" section and pages [*,] was wholly inadequate; and
2. The Board of Directors of the Company should receive appropriate training and familiarisation from [the Sponsor and Legal Advisers to the Company] before the listing of the Company. The scope of the training should include ongoing role and responsibilities of directors under the GEM Listing Rules and compliance with the relevant rules and regulations applicable to companies listed in Hong Kong. A copy of the relevant training materials prepared by [the Legal Advisers to the Company] should be provided to the Listing Division as evidence of the training. The Review Committee also wished to highlight the importance of Rule 6A.24 relating to the responsibilities of a Compliance Adviser.

For the avoidance of doubt, should the Company decide to proceed with its application for new listing, such application will be treated strictly on its merits at the material time, and no representation is given, whether express or implied, as to the acceptability of such application if pursued. The new listing application of the Company in its entirety will be subject to the final approval of the GEM Listing Committee.

The Review Committee wishes to emphasise that this decision is specific to this particular instance and shall not serve to create a precedent for any other companies.

Yours faithfully
For and on behalf of
The Stock Exchange of Hong Kong Limited

[Signed]

Secretary to the GEM Listing (Review) Committee