

## HKEx LISTING DECISION

Cite as HKEx-LD45-1 (First Quarter of 2005)

**[Streamlined and incorporated into the Guide for New Listing Applicants in January 2024]**

<b>Summary</b>	
<b>Name of Party</b>	Company A – a Main Board listed issuer and its subsidiaries (the “Group”)
<b>Subject</b>	Whether the requirement for management continuity under Listing Rule 8.05(1)(b) and Paragraph 2 of Practice Note 3 could be satisfied when only one director had remained on the board of directors throughout the three financial year track record period up to the time of listing ?
<b>Listing Rules</b>	Listing Rule 8.05(1)(b); Paragraph 2 of Practice Note 3
<b>Decision</b>	The Exchange determined that the requirement for management continuity was satisfied when it was demonstrated that a group of individuals on the board of directors and in senior management of Company A and its operating subsidiaries, who constituted the core management group responsible for the track record results of Company A, had been in place for the required three-year period and up to the time of listing.

### SUMMARY OF FACTS

1. In the first year of the three financial year track record period of Company A (‘Year 1’), there was a major shareholding change in Company A’s predecessor where Shareholder X replaced Shareholder Y as the majority shareholder.
2. The change in share ownership had also caused major changes in the composition of the board of directors of Company A’s predecessor. The board of directors constituted the top management of Company A’s predecessor under its articles of association. Except for Mr. Q, no other director had remained on the board throughout the three financial year track record period up to the time of listing. Mr. Q was the only director holding office since the time of Company A’s predecessor. Mr. Q had been responsible for the business, strategy and operational management of Company A and its predecessor throughout the relevant period.
3. At the second tier of management, the level immediately below the board of directors, an identified group of senior officials who made up the Management Committee of Company A and its predecessor remained largely unchanged throughout the relevant period. The Management Committee had been responsible for the daily management of Company A and its predecessor, including carrying out the decisions of the board through Mr. Q, overseeing the production process,

the sales and financial aspects of management of the business and other essential operations. All these activities resulted in the most substantial portion of the track record results of Company A and its predecessor.

4. For the purpose of demonstrating management continuity under Listing Rule 8.05(1)(b) and Paragraph 2 of Practice Note 3, the sponsor of Company A submitted that throughout the track record period up to the time of listing, the management of Company A had been carried out through the core management group comprising Mr. Q, the only executive director, and the Management Committee.
5. The sponsor of Company A further demonstrated to the satisfaction of the Exchange that the numbers of directors appointed by each shareholder (Shareholder X and Shareholder Y) were reflective of the respective shareholdings in Company A and its predecessor during the relevant periods. Apart from Mr. Q, all other directors of Company A were non-executive directors. The board of directors seldom convened meetings. In the event that board meetings were convened, they were for the purposes of satisfying the formal requirements of the articles of association, for example, receiving, discussing reports and endorsing business plans and budget and dividend distribution, etc. prepared or recommended by the core management group. Throughout the relevant track record period, none of the directors had sought to interfere with the management and operational decisions of the core management group through their influence in the board of directors or through other channels.

#### **THE ISSUE RAISED FOR CONSIDERATION**

6. Whether the requirement for management continuity under Listing Rule 8.05(1)(b) and Paragraph 2 of Practice Note 3 could be satisfied when only one director had remained on the board of directors throughout the three financial year track record period up to the time of listing?

#### **APPLICABLE LISTING RULES OR PRINCIPLE**

7. Listing Rule 8.05(1)(b) provides that in order to meet the profit test, a new applicant must have an adequate trading record under substantially the same management and ownership. This means that the new applicant or its group must, among other criteria, satisfy *'management continuity for at least the three preceding financial years.'*
8. Paragraph 2 of Practice Note 3 of the Listing Rules gives further guidance on the interpretation of the requirement for substantially the same management as follow:

*'In all cases the trading record period of a new applicant must enable the Exchange and investors to make an informed assessment of the management's ability to manage the applicant's business and the likely performance of that business in the future. In order to make this assessment the applicant must be able to satisfy the Exchange that its main business or businesses, as at the time of listing, have normally been managed by substantially the same persons throughout the period of the qualifying trading record and that such persons are the management of the new applicant.'*

## **THE ANALYSIS**

9. The Exchange ordinarily considers management continuity under Listing Rule 8.05(1)(b) and Paragraph 2 of Practice Note 3 to be a question of fact.
10. In the Consultation Paper on Proposed Amendments to the Listing Rules Relating to Initial Listing Criteria and Continuing Eligibility published in July 2002 (the 'Consultation Paper'), paragraph 31 clearly stated that the Exchange has interpreted the management continuity requirement to mean that applicants must demonstrate that there has been no change in the majority of the applicant's board of directors and senior management of its principal operating subsidiaries during the three financial year track record period. Paragraph 2 of Practice Note 3 requires that management continuity must continue up to the date of listing.
11. Based on this interpretation of the Listing Rules, when examining whether Company A and its predecessor satisfied the management continuity requirement, the Exchange followed the practice of concentrating on a review of the substance of the management, particularly considering whether:
  - a. an identifiable group of individuals most relevant and responsible for the track record results of a listing applicant remained in positions of responsibility with the enterprise under review throughout the relevant track record period; and
  - b. such group of individuals would form the core management of the applicant at the time of listing and thereafter.
12. When assessing the relevance of individual members of a management team to the track record results of Company A and its predecessor, the Exchange followed the practice of ordinarily attributing proportionately greater responsibility to officers with more senior positions than those with more junior positions. This practice is intended to reflect the formal responsibilities of senior officers in their corporate roles. In its determination process, the Exchange ordinarily considers special facts and circumstances of an individual case to enable appropriate adjustments to be made in its final conclusion.

13. In the present case, the Exchange accepted submissions from the sponsor of Company A that the numbers of directors that were appointed by each shareholder were reflective of the respective shareholdings in Company A's predecessor. Based on the submitted facts, the Exchange accepted that, although under the relevant articles of association the board of directors was the organ with the highest authority, the management of the actual operation of Company A and its predecessor that contributed directly to the track record results had been entrusted to Mr. Q, the only executive director at the board level, and the Management Committee.
14. Following the above analysis, the Exchange therefore determined that the requirement for management continuity was satisfied in the present case. This conclusion was arrived at notwithstanding that the core management of Company A and its predecessor most responsible for the results during the three financial year track record period and at the time of listing constituted a minority in numbers in their respective boards of directors.

#### **THE DECISION**

15. Based on the above facts and the circumstances of the case and the Exchange's analysis of the Listing Rules, the Exchange determined that the requirement for management continuity under Listing Rule 8.05(1)(b) and Paragraph 2 of Practice Note 3 was satisfied when it was demonstrated that management continuity within a group of individuals on the board of directors and in senior management of Company A and its operating subsidiaries (that is, Mr. Q and the Management Committee), who constituted the core management group responsible for the track record results of Company A, had been in place for the required three-year period and up to the time of listing.