

**HKEx LISTING DECISION**  
Cite as HKEx-LD47-4 (July 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 listing applicant and its subsidiaries (the "Group")
<b>Subject</b>	Whether the issue of shares in Company A upon conversion of convertible notes issued by Company A prior to listing on the Exchange should be regarded as a deemed disposal of interest prohibited under Listing Rules 10.07 and 10.08, where such conversion would occur upon or shortly after listing and at a price identical to the IPO price?
<b>Listing Rules</b>	Listing Rules 10.07 and 10.08
<b>Decision</b>	The Exchange determined that the issue of Company A's shares upon or shortly after listing upon conversion of the convertible notes should be allowed and the shares so issued would not be subject to lock-up.

**SUMMARY OF FACTS**

1. More than six months prior to the hearing of Company A's listing application, Company A issued a certain amount of convertible notes ('Convertible Notes') to pre-IPO investors ('Pre-IPO Investors'). The terms of the Convertible Notes provided that unless otherwise redeemed by Company A, all the outstanding principal amount and accrued interest would automatically be converted into shares of Company A ('Shares') at the IPO share offer price on the third business day after delivery of a written notice by Company A to the Pre-IPO Investors confirming that the Exchange had approved the listing of the Shares. In other words, the conversion would take place upon or shortly after the listing of the Shares.
2. Based on the representations of the sponsor and Company A, the Exchange noted the following relevant material facts:
  - a. a substantial portion of the proceeds from the issuance of the Convertible Notes had been used in the acquisition of a company by the Group;
  - b. the Pre-IPO Investors decided to invest in Company A because of the investment return of the Convertible Notes and the business potential of the Group;

- c. the directors of Company A considered that the issue of the Convertible Notes was a strategic step to enhance the Group's relationship with the Pre-IPO Investors; and
- d. all the Pre-IPO Investors (and their respective directors and shareholders) were independent of and not connected with Company A within the meaning of the Listing Rules.

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

- 3. Whether the issue of shares in Company A upon conversion of convertible notes issued by Company A prior to listing on the Exchange should be regarded as a deemed disposal of interest prohibited under Listing Rules 10.07 and 10.08, where such conversion would occur upon or shortly after listing and at a price identical to the IPO price?

### **APPLICABLE LISTING RULES OR PRINCIPLES**

- 4. Listing Rule 10.07 (1)(a) states 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 and shall procure that the relevant registered holder(s) shall not:-

- (a) 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 from the date on which dealings in the securities of a new applicant commence on the Exchange, dispose of, nor enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of those securities of the issuer in respect of which he is or they are shown by that listing document to be the beneficial owner(s); or'

- 5. Listing Rule 10.08 states that:

'[N]o further shares of securities convertible into equity securities of a listed issue (whether or not of a class already listed) may be issued or form the subject of any agreement to such an issue within 6 months from the date on which securities of the listed issuer first commence dealing on the Exchange (whether or not such issue of shares or securities will be completed within 6 months from the commencement of dealing), except for:

- (4) the issue of shares or securities pursuant to an agreement entered into before the commencement of dealing, the material terms of which have been disclosed in the listing document issued in connection with the initial public offering.'

## **THE ANALYSIS**

6. The Exchange ordinarily interprets Listing Rule 10.07(1)(a) to apply to a deemed disposal situation where there is a dilution of the controlling shareholders' interest as a result of the issue of new shares during the first six months of the listing of an issuer's shares. However, the Exchange ordinarily considers that an issue of new shares pursuant to an agreement entered into before the commencement of dealing is allowed under Listing Rule 10.08 provided that the material terms of the agreement have been disclosed in the prospectus.
7. On the question of whether the issue of Shares upon conversion of the Convertible Notes should be disallowed in the present case and whether there should be a lock up of the Shares so issued, the Exchange considered the following:
  - a. the material terms of the Convertible Notes including the reasons for the issue and the use of the proceeds were prominently disclosed in the prospectus in accordance with the Exchange's expectations under Listing Rule 10.08;
  - b. the Convertible Notes were issued more than six months before the date of the hearing of Company A's listing application; and
  - c. the Pre-IPO Investors were independent third parties and there was no evidence to suggest that the Pre-IPO Investors had any connection with the controlling shareholders such that they would constitute a group of controlling shareholders for the purpose of Listing Rule 10.07.
8. Based on the facts and circumstances of the case, the Exchange did not consider the proposed conversion to be barred by Listing Rule 10.07 although it would result in a deemed disposal of controlling shareholders' interest in Company A. Furthermore, as the material terms had been disclosed in the prospectus as expected by the Exchange, no lock up of the Shares after conversion was required.

## **THE DECISION**

9. Based on the above analysis and having regard to the material facts of the case, the Exchange determined that the issue of Shares upon or shortly after listing

upon conversion of the Convertible Notes in favour of the Pre-IPO Investors should be allowed and the Shares so issued would not be subject to lock-up.