

▶ **Responsibilities of Directors of Companies Listed on the Main Board of the Stock Exchange of Hong Kong Limited**



January 2016

CHARLTONS
易周律師行

The Major Sources of Directors' Obligations

- 1) common law and applicable legislation, including the Companies Ordinance and the Securities and Futures Ordinance (“SFO”);
- 2) the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”), including the Corporate Governance Code (the “Code”) and the Model Code for Securities Transactions by Directors of Listed Issuers contained therein;
- 3) the Code on Takeovers and Mergers and the Code on Share Buy-backs;
- 4) the directors’ Declaration and Undertaking to the Exchange; and
- 5) the Companies Registry’s Guide on Directors’ Duties.

Directors' Obligation to Ensure Issuers' Compliance with Listing Rules

- ▶ A listed issuer undertakes in its application for listing to comply with the Listing Rules once its securities are listed on the Exchange.
- ▶ Under Listing Rule 13.04, the directors of a listed issuer are collectively and individually responsible for ensuring that the listed issuer complies fully with the requirements of the Listing Rules.
- ▶ Directors are required to file a Form B Declaration and Undertaking with the Exchange (Form H for PRC companies).

Directors' Declaration and Undertaking

A director undertakes that he will:

- ▶ comply to the best of his ability with the Listing Rules and use his best endeavours to ensure that the **listed issuer** complies with the Listing Rules;
- ▶ comply to the best of his abilities with the requirements of **Parts XIVA** (in relation to disclosure of inside (i.e. price sensitive) information and **XV of the SFO** (in relation to the disclosure of interests in the shares and debentures of the listed issuer and its associated companies), the Code on Takeovers and Mergers, the Code on Buy-backs and all other securities laws and regulations from time to time in force in Hong Kong **and** use his best endeavours to ensure that **the listed issuer** so complies; and
- ▶ cooperate in any investigation conducted by the Listing Division and/or the Listing Committee of the Exchange.

Fiduciary Duties of Directors

Main Board Rule 3.08 requires directors to fulfil fiduciary duties and duties of skill, care and diligence to at least the standard required under Hong Kong law. Listing Rules summarise duties as:

- 1) Duty to act honestly and in good faith in the interests of the company as a whole
- 2) Duty to act for a proper purpose
- 3) Duty to be answerable to the listed issuer for the application or misapplication of its assets
- 4) Duty to avoid actual and potential conflicts of interest and duty
- 5) Duty to disclose fully and fairly his interests in contracts with the listed issuer
- 6) Duty to apply such degree of skill, care and diligence as may reasonably be expected of a person with his knowledge and experience and acting as a director of a listed issuer (Rule 3.08)

Rule 3.08 also requires directors to take an active interest in the issuer's affairs, obtain a general understanding of its business and follow up anything untoward that comes to his/her attention. Delegating these functions is permissible but does not absolve directors from his/her responsibilities or from applying the required skill, care, and diligence.

Duties summarised in the [Companies Registry's Guide on Directors' Duties](#).

CHARLTONS
易周律师行

Statutory Duty under New Companies Ordinance

Directors' duty of skill, care and diligence is codified in s465(1) of the new Companies Ordinance (Cap. 622).

Standard under old case law – subjective test – considered too low.

s465(2) adopts mixed objective and subjective standard: standard of skill, care and diligence required is that of a **reasonably diligent person** with:

- a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company (objective test); and
- b) the general knowledge, skill and experience that the director has (subjective test).

Objective test in (a) is minimum standard. Subjective test in (b) means that if director has special skill/knowledge, a higher standard is required.

s465(2) doesn't apply directly to companies incorporated outside Hong Kong, but applies indirectly under Rule 3.08 - directors of non-HK companies must fulfil duty of skill, care and diligence to the standard required by HK law.

CHARLTONS
易周律师行

Consequences of Non-Compliance with Main Board Rules

If there has been a breach of the Listing Rules, the Exchange may:

- ▶ issue a private reprimand;
- ▶ issue a public statement which involves criticism;
- ▶ issue a public censure;
- ▶ report offender's conduct to a regulatory authority (e.g. the SFC) or an overseas regulatory authority;
- ▶ require a breach to be rectified or other remedial action taken within a stipulated period; or
- ▶ take (or refrain from taking) such other action as the Exchange thinks fit. (Rule 2A.09)

If the Exchange considers the issuer failed in a material manner to comply with the Listing Rules, it can suspend dealings in, or cancel the listing of, the issuer's securities (Rule 6.01(1)).

Consequences of Non-Compliance with Main Board Rules (Cont'd)

It is a criminal offence to intentionally or recklessly provide information which is false or misleading in a material particular in any public disclosure document filed with the Exchange or SFC (section 384 of the SFO). The maximum penalty is 2 years' imprisonment and a fine of HK\$1 million.

Under section 214 of the SFO, a person can be disqualified from being a director of any corporation for up to 15 years if he is wholly/ partly responsible for the misconduct of a company's affairs. Misconduct includes where shareholders are not given all the information with respect to the company which they might reasonably expect. In 2010, the SFC disqualified two directors for failing to inform the company's shareholders that the company was in a substantially depleted financial position.

Directors' Liability for Misstatements in Prospectus

The Listing Rules require an issuer's directors to take full responsibility for the contents of a prospectus. The prospectus must contain a responsibility statement which states that:

“the directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this document is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this document misleading.”

Directors' Liability for Misstatements in Prospectus (Cont'd)

Untrue statements contained in a prospectus or the omission of material information (“**Misstatements**”) may result in criminal and/or civil liability for the issuer’s directors. The principal areas of liability include:

- ▶ **Section 342E Companies (Winding Up and Miscellaneous Provisions) Ordinance (CWUMPO)** – imposes civil liability for prospectus misstatements on specified persons (including directors)
- ▶ **Section 342F CWUMPO** – imposes criminal liability for prospectus misstatements on persons who “authorized the issue of a prospectus” (which may include the directors)
- ▶ **Section 108(1) SFO** – imposes civil liability for making any fraudulent, reckless or negligent misrepresentation which induces others to invest money
- ▶ **Sections 277 & 281 SFO** – impose civil liability for disclosing false or misleading information to induce dealings in securities
- ▶ **Section 391 SFO** – imposes civil liability for false or misleading public communications to induce dealings in securities

Directors' Liability for Misstatements in Prospectus (Cont'd)

Untrue statements contained in a prospectus or the omission of material information (“**Misstatements**”) may result in criminal and/or civil liability for the issuer’s directors. The principal areas of liability include (Cont’d):

- ▶ **Section 107 SFO** – imposes criminal liability for making any fraudulent or reckless misrepresentation to induce others to deal in securities
- ▶ **Section 298 SFO** – imposes criminal liability for disclosure of false or misleading information to induce dealings
- ▶ **Section 384 SFO** – imposes criminal liability for provision of false or misleading information in a prospectus or other document filed with the Exchange or the SFC

Liability can also arise: (i) under the Misrepresentation Ordinance or the Theft Ordinance; (ii) in tort; or (iii) under contract.

For further information, please see Charltons’ note “Potential Liabilities under Hong Kong Law in Connection with the Publication of a Prospectus on the Listing of a Company on the Stock Exchange of Hong Kong”.

Restriction on Disclosure of Material Information to Analysts

The Hong Kong prospectus is the sole document by which the Company sells its shares in the Hong Kong IPO.

Any other additional document by which securities are offered to the public (or members of the public) could constitute a “prospectus” under Hong Kong law, in which case:

- ▶ the prospectus content requirements will apply;
- ▶ the translation requirements will apply; and
- ▶ the registration requirement will apply.

Breach of the prospectus laws is a criminal offence.

Restriction on Disclosure of Material Information to Analysts (Cont'd)

To avoid the risk of liability, the directors and senior management of the Company must ensure that no material information about the Company or its securities is provided to any investment research analyst, unless the information is reasonably expected to be included in the prospectus or is publicly available.

When assessing whether any such information is “material” information, the test that should be applied is whether the information is material to an investor in forming a valid and justifiable opinion of the Company and its financial condition and profitability.

This restriction covers any information provided to an analyst, directly or indirectly, formally or informally, in writing or verbally. It covers all communications in a meeting, during a presentation, site visit or interview, or in any other context.

Restriction on Disclosure of Material Information to Analysts (Cont'd)

It is of utmost importance that no additional material non-public information is provided to other persons, including analysts.

- ▶ In case of disclosure (whether intentional or not) to analysts, the Company may be compelled to disclose the same information in the prospectus;
- ▶ Such information may not be appropriate for a prospectus and may not be verifiable.

Restriction on Disclosure of Material Information to Analysts (Cont'd)

Consequences of putting such a statement in the prospectus

- ▶ any untrue statement (including any statement that is false, misleading or deceptive) in a prospectus may give rise to criminal and civil liability, including personal liabilities of each director and any other person who authorised the issue of the prospectus; and
- ▶ the directors must likewise take personal liability for the truthfulness, accuracy and completeness of any information the Company may be compelled under the SFC rules to insert into the prospectus under the above circumstances.

The restriction covers any information provided to an analyst, directly or indirectly, formally or informally, in writing or otherwise.

The Company is strongly advised to seek the guidance and assistance of its sponsor(s), its Hong Kong legal advisers and those of the sponsor if there are any uncertainties.

Statutory Regime for Disclosure of PSI - Key Features

- ▶ **Statutory obligation under Part XIVA SFO** on corporations to disclose price sensitive information (referred to as “inside information”) to the public as soon as reasonably practicable after inside information has come to their knowledge;
- ▶ Breaches of the inside information disclosure requirement will be dealt with by the **MMT**;
- ▶ A number of civil sanctions will be imposed incl. **a maximum fine of HK\$ 8 million** on the corporation, its directors/chief executive;
- ▶ The SFC has published [Guidelines on Disclosure of Inside Information \(SFC Guidelines\)](#) to assist compliance with the new requirements;
- ▶ SFC can institute proceedings directly before the MMT (without referral to the Financial Secretary);

Statutory Regime for Disclosure of PSI - Key Features (Cont'd)

- ▶ The application of an **objective test** in determining whether information is inside information: whether a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.
- ▶ Statutory obligation to disclose inside information **as soon as reasonably practicable** upon knowledge.
- ▶ An obligation on directors and officers to take all reasonable measures to ensure **proper safeguards** exist to prevent corporations' breach of statutory requirements.

Statutory Regime for Disclosure of PSI - Key Features (Cont'd)

- ▶ Individual liability on directors/officers for corporation's breach of the requirement if such breach is a result of their intentional, reckless or negligent conduct or failure to ensure proper safeguards.
- ▶ The provision of “**safe harbours**” for legitimate circumstances where non-disclosure or late disclosure is permitted.
- ▶ The SFC can **investigate** suspected breaches and **institute proceedings** before the MMT.
- ▶ Civil sanctions: a **fine** up to **HKD 8 million** or **disqualification** order up to **5 years**.
- ▶ Liability to pay compensation to persons who suffer financial loss as a result of the breach.

Definition of “Inside Information”

Inside Information is

- ▶ **specific** information about the listed corporation, a shareholder or officer of the listed corporation or its listed securities or their derivatives
- ▶ which is **not generally known** to that segment of the market which deals or which would likely deal in the corporation’s securities and
- ▶ would, if generally known, be **likely to have a material effect on the price of the corporation’s securities.**

The 3 key elements of the definition are:

- ▶ **specific information;**
- ▶ **“not generally known”;** and
- ▶ **“likely to have a material effect on the price of the listed securities”.**

SFC Guidelines provide guidance on interpretation.

Definition of “Inside Information” (Cont’d)

Specificity of Information

- ▶ The information must be capable of being **identified, defined and unequivocally expressed**.
- ▶ The information **need not be precise**; information may be specific even though the particulars or details are not precisely known.
- ▶ Information on a transaction that is only contemplated or under negotiation, while not yet subject to a final agreement, can be specific information.
- ▶ Vague exchanges of ideas or “fishing expeditions” are not specific information.
- ▶ Negotiations or contracts may be specific information if they have reached a concrete stage where there is substantial commercial reality to them and the parties intend to negotiate with a realistic view to achieving an identifiable goal.
- ▶ Mere rumours, vague hopes, or worries, wishful thinking and unsubstantiated conjecture are not specific information.

Definition of “Inside Information” (Cont’d)

Generally known to the market

- ▶ Clear distinction drawn between market having actual knowledge through proper disclosure and speculation/expectation on an event which require proof.
- ▶ Rumours, media speculation and market expectation about an event cannot be equated with information generally known to the market.
- ▶ Regarding information that is the subject of media comments/analysts’ reports, the corporation should consider the accuracy/completeness/reliability of the information in determining whether it is “generally known to the market”.
- ▶ Should material omissions/doubts as to its bona fides exist, the information is not generally known to the market and requires full disclosure.

Definition of “Inside Information” (Cont’d)

Likely to have a material effect on the price of the listed securities

- ▶ Test: whether the inside information would influence persons who are accustomed to or would be likely to deal in the corporation’s shares, in deciding whether to buy or sell the securities.
- ▶ The test must be applied at the time the information becomes available, and is therefore hypothetical.

Timing of Disclosure

Inside information has come to the corporation's knowledge if:

- a) the inside information has, or ought reasonably to have, come to the knowledge of an officer of the corporation in the course of performing functions as an officer of the corporation; **and**
- b) a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation (section 307B(2) of the SFO).

Corporations must therefore have effective systems and procedures in place to ensure that any material information which comes to the knowledge of any of their officers is promptly identified and escalated to the board to determine whether it needs to be disclosed.

Meaning of “as soon as reasonably practicable”

According to SFC Guidelines, the corporation should immediately take all steps necessary to disclose the information to the public, which may include:

- ▶ Ascertaining sufficient details;
- ▶ Internal assessment of the matter and its impact;
- ▶ Seeking professional advice; and
- ▶ Verification of the facts.

The corporation must ensure that the information is kept strictly confidential until it is publicly disclosed. If the corporation believes that confidentiality cannot be maintained or has been breached, it should immediately disclose the information publicly.

The SFC also raises the possibility for a corporation to issue a “holding announcement” to give the corporation time to clarify the details and likely impact of an event before a full announcement.

Who Is An “Officer”?

- ▶ Officer: a director, manager or company secretary of a corporation or any other person involved in its management (Part 1 of Schedule 1 to the SFO).
- ▶ A “manager” generally connotes a person who, under the immediate authority of the board, is charged with management responsibility affecting the whole or a substantial part of the corporation.
- ▶ Only information being known in situations **where the officer is acting in the capacity as an officer** is subject to the inside information disclosure requirement.

Manner of Disclosure

- ▶ Disclosure must be made in a manner that can provide equal, timely and effective access by the public (s307C(1) SFO).
- ▶ Publication via the electronic publication system operated by the Exchange will meet the above requirements (s307C(2)).
- ▶ Inside information discloseable under Part XIVA SFO must be announced under Rule 2.07C.
- ▶ On top of publication on the Exchange's website and its own website, press releases issued through news, wire services and/or press conferences are also allowed.
- ▶ If a corporation is listed on more than one stock exchange, the corporation must ensure information disclosed in overseas markets is simultaneously disclosed in HK. If the HK market is closed, the corporation must issue an announcement in HK before the HK market opens.
- ▶ Suspension of trading may be requested, if necessary.
- ▶ The information contained in the disclosure announcement must be complete and accurate in all material respects and not be misleading or deceptive.

Safe Harbours

- ▶ Safe Harbours: 4 situations where corporations are permitted to not disclose or delay disclosing inside information (s307D SFO).
- ▶ Except for Safe Harbour A, corporations may only rely on the safe harbours if they have taken reasonable precautions to preserve the confidentiality of the inside information and the inside information has not been leaked.

Safe Harbour A

Corporations are granted safe harbour if disclosure would **breach an order by an HK court or any provisions of other HK statutes.**

Safe Harbours (Cont'd)

Safe Harbour B

Corporations are granted safe harbour for information relating to an **incomplete proposal or negotiation**.

Examples:

- ▶ when a contract is being negotiated but has not been finalised;
- ▶ when a corporation decides to sell a major holding in another corporation;
- ▶ when a corporation is negotiating a share placing with a financial institution; or
- ▶ when a corporation is negotiating the provision of financing with a creditor.

Safe Harbours (Cont'd)

Safe Harbour C

Corporations are granted safe harbour for information being a **trade secret**. Trade secret generally refers to proprietary information owned by a corporation:

Examples:

- ▶ used in a trade or business of the corporation;
- ▶ which is confidential (i.e. not already in the public domain);
- ▶ which, if disclosed to a competitor, would be liable to cause real or significant harm to the corporation's business interests; and
- ▶ the circulation of which is confined to a limited number of persons on a need-to-know basis.

Trade secrets may concern inventions, manufacturing processes or customer lists. However a trade secret does not cover the commercial terms and conditions of a contractual agreement or the financial information of a corporation.

Safe Harbours (Cont'd)

Safe Harbour D

Corporations are granted safe harbour for information concerning the provision of **liquidity support** from the Government's Exchange Fund or a Central Bank (or institution performing such functions, inside or outside HK).

The purpose of this safe harbour is to ward off financial contagion.

Safe Harbours (Cont'd)

Safe harbour condition of confidentiality:

Except for Safe Harbour A, the safe harbours are only available if and so long as:

- ▶ Reasonable precautions for preserving confidentiality are taken; and
- ▶ The confidentiality is preserved.

If confidentiality is lost or information leaked, the safe harbour will cease to be available and disclosure is required as soon as practicable.

If confidentiality is lost, the corporation will not be regarded as in breach of the disclosure requirement in respect of inside information if it can show that it:

- ▶ Has taken reasonable measures to monitor the confidentiality of information in question; and
- ▶ Made disclosure as soon as reasonably practicable.

SFC's Power to Grant Waiver

- ▶ The SFC can grant waivers where the disclosure of inside information in Hong Kong would be prohibited under a court order or legislation of another jurisdiction or would contravene a restriction imposed by a law enforcement agency or government authority in another jurisdiction (section 307E(1)SFO). The SFC will grant waivers on a case-by-case basis and may attach conditions.
- ▶ During an application for a waiver, confidentiality must be maintained. Should an information leakage occur, the corporation would be obliged to suspend trading prior to making a disclosure. The waiver application fee will be HK\$24,000.
- ▶ A corporation must copy to the Exchange any application to the SFC for a waiver from disclosure under Part XIVA and the SFC's decision.

SFC's Power to Grant Waiver (Cont'd)

The officers of a corporation are required to take all reasonable measures to ensure that proper safeguards exist to prevent the corporation's breach of the inside information disclosure requirement (section 307G(1)).

Although an officer's breach of this provision is not actionable of itself, an officer will be regarded as having breached the disclosure obligation if the listed corporation has breached such obligation and either:

- ▶ the breach resulted from the officer's intentional, reckless or negligent conduct; or
- ▶ the officer has not taken all reasonable measures to ensure that proper safeguards exist to prevent the breach (section 307G(2) SFO).

The SFC Guidelines focus on the responsibility of officers, including non-executive directors, to ensure that appropriate systems and procedures are put in place and reviewed periodically to enable the corporation to comply with the disclosure requirement. Officers with an executive role will also have a duty to oversee the proper implementation and functioning of the procedures and to ensure the detection and remedy of material deficiencies in a timely manner.

Sanctions

Possible penalties imposed by the MMT:

- ▶ a fine of up to HK\$8 million on the corporation, a director or chief executive (but not officer);
- ▶ disqualification of the director or officer for up to 5 years;
- ▶ a “cold shoulder” order on the director or an officer for up to 5 years;
- ▶ a “cease and desist” order on the corporation, director or officer;
- ▶ an order that any body of which the director or officer is a member be recommended to take disciplinary action against him; and
- ▶ payment of costs of the civil inquiry and/or the SFC investigation by the corporation, director or officer.

Sanctions (Cont'd)

To prevent the occurrence of further breaches, the MMT may require:

- ▶ the appointment of an independent professional adviser to review the corporation's procedures for disclosure of PSI and advise it on matters relating to compliance; and
- ▶ the officer to undertake a training programme approved by the SFC on compliance with Part XIVA SFO, directors' duties and corporate governance.

The SFC could also apply to court under s213 SFO for a restoration order.

Civil Liability – Private Right of Action

A corporation or officer found to be in breach of the statutory disclosure obligation may be found liable to pay compensation to any person who has suffered financial loss as a result of the breach in separate proceedings brought by such person under Section 307Z SFO.

The corporation or officer will be liable to pay damages provided that it is fair, just and reasonable that it/he should do so. A determination by the MMT that a breach of the disclosure requirement has taken place or identifying a person as being in breach of the requirement will be admissible in evidence in any such proceedings to prove that the disclosure requirement has been breached or that the person in question has breached that requirement.

The courts may also impose an injunction in addition to or in substitution for damages.

Listing Rule Obligations

The role and duties of the SFC and the Exchange

The SFC is responsible for enforcing the statutory inside information disclosure regime, but the Exchange remains responsible for maintaining an orderly, informed and fair market.

The Exchange will not give any guidance as to the interpretation or operation of Part XIVA of the SFO or the Guidelines on Disclosure of Inside Information published by the SFC.

The Exchange will refer cases of possible breach of the statutory disclosure obligation to the SFC when the Exchange becomes aware of it.

The Exchange will not take disciplinary action unless the SFC considers it inappropriate to pursue the matter under the SFO and the Exchange considers there to have been a breach of the Listing Rules.

An issuer will not face enforcement action by the SFC and the Exchange at the same time, in respect of the same set of facts.

Listing Rule Obligations (Cont'd)

Obligation to avoid false market (MB 13.09(1))

Issuers are required to disclose information necessary to avoid a false market as soon as reasonably practicable when:

- i. in the view of the Exchange, there is or there is likely to be a false marketing in the issuer's securities; and
 - ii. after consultation with the Exchange.
-
- ▶ An issuer is also required to contact the Exchange as soon as reasonably practicable if it believes that there is likely to be a false market in its securities.
 - ▶ Under Main Board Rule 13.09(2), where an issuer is required to disclose inside information under the SFO, it must simultaneously announce the information. An issuer is also required to simultaneously copy to the Exchange any application to the SFC for a waiver from the requirement to disclose inside information and to promptly copy to the Exchange the SFC's decision whether to grant such a waiver.

Listing Rule Obligations (Cont'd)

Obligation to respond to the Exchange's enquiry

- ▶ Main Board Rule 13.10 requires an issuer that receives an Exchange enquiry concerning unusual movements in the price or trading volume of an issuer's listed securities, the possible development of a false market in its securities, or any other matters, to respond promptly in one of two ways:
 - provide (and announce, if so required by the Exchange) any information it has that is relevant to the subject matter of the enquiry, so as to inform the market or to clarify the situation; or
 - if appropriate and if requested by the Exchange, issue a standard announcement confirming that the directors, **having made such enquiry with respect to the issuer as may be reasonable in the circumstances**, are not aware of any information that is or may be relevant to the subject matter of the enquiry or of any inside information that needs to be disclosed under the SFO.
- ▶ The latter response should be made in a standard form that is set out in Note 1 to Main Board Rule 13.10.

Listing Rule Obligations (Cont'd)

“This announcement is made at the request of The Stock Exchange of Hong Kong Limited.

We have noted [the recent increases/decreases in the price [or trading volume] of the [shares/warrants] of the Company] or [We refer to the subject matter of the Exchange’s enquiry]. Having made such enquiry with respect to the Company as is reasonable in the circumstances, we confirm that we are not aware of [any reasons for these price [or volume] movements] or of any information which must be announced to avoid a false market in the Company’s securities or of any information which must be announced to avoid a false market in the Company’s securities or of any inside information that needs to be disclosed under Part XIVA of the Securities and Futures Ordinance.

This announcement is made by the order of the Company. The Company’s Board of Directors collectively and individually accept responsibility for the accuracy of this announcement.”

- ▶ A note to Rule 13.10 – an issuer does not need to disclose inside information under the Rules if disclosure of the information is exempt under the statutory regime.

Trading Halts

Trading Halts or Trading Suspension (MB Rule 13.10A)

Main Board Rule 13.10A requires a listed issuer to request a trading halt or trading suspension if an announcement cannot be made promptly in any of the following circumstances:

- a) an issuer has information which must be disclosed under Main Board Rule 13.09;
 - b) an issuer reasonably believes that there is inside information which must be disclosed under Part XIVA SFO; or
 - c) an issuer reasonably believes or it is reasonably likely that confidentiality may have been lost in respect of inside information which is : (i) the subject of an application to the SFC for a waiver; or (ii) exempt from the statutory disclosure obligation (except if the exemption concerns disclosure prohibited by Hong Kong law/court order).
- ❖ *“Trading halts” are defined as an interruption of trading in an issuer’s securities requested or directed pending disclosure of information under the Rules*

Announcements

The Listing Rules require listed companies to publish announcements in a wide range of situations. The Exchange's Guide on Pre-vetting Requirements and Selection of Headline Categories for Announcements (effective 1.04.2015) ("**Pre-Vetting Guide**")^[1] sets out the situations in which an announcement is required under the Main Board Rules, whether or not the announcement is required to be vetted by the Exchange before publication and the headline categories which will generally apply. The following is a summary of the main situations in which a listed issuer is required to inform the Exchange and publish an announcement.

[1] http://www.hkex.com.hk/eng/rulesreg/listrules/guidref/guide_pre_vetting_req.htm

Announcements (Cont'd)

- ▶ **Price-sensitive information** – any price sensitive information which is discloseable as inside information under Part XIVA SFO must be announced and kept strictly confidential until a formal announcement is made.
- ▶ **Notifiable transactions** – any notifiable transaction within Chapter 14 of the Main Board Rules.
- ▶ **Connected transactions** – any connected transaction (unless an exemption is available) within Chapter 14A of the Main Board Rules.

Announcements (Cont'd)

Advances and financial assistance to third parties – the listed issuer or any of its subsidiaries makes a “relevant advance to an entity” which:

- ▶ exceeds 8% of the total assets of the listed issuer (Main Board Rule 13.13); or
- ▶ is greater than the previously disclosed relevant advance by 3% or more of the listed issuer’s total assets (Main Board Rule 13.14).

The expression “relevant advance to an entity” means the aggregate of amounts due from and all guarantees given on behalf of an entity, its controlling shareholder, its subsidiaries and affiliated companies. An advance to a subsidiary of the listed issuer, or between subsidiaries of the listed issuer, is not regarded as a relevant advance to an entity.

Announcements (Cont'd)

Financial assistance to affiliated companies - financial assistance and guarantees of financial assistance given by the listed issuer or any of its subsidiaries to affiliated companies (being those which are equity accounted for by the issuer) of the listed issuer together exceed 8% of the listed issuer's total assets (Main Board Rule 13.16).

Pledge of controlling shareholder's interest - the controlling shareholder of the listed issuer has pledged its interest in shares of the issuer to secure debts of the issuer or to secure guarantees or other support of obligations of the issuer (Main Board Rule 13.17).

Announcements (Cont'd)

Loan agreements – where:

- ▶ the listed issuer (or any of its subsidiaries) enters into a loan agreement that imposes specific performance obligations on any controlling shareholder (e.g. a requirement to maintain a specified minimum holding in the share capital of the listed issuer) and breach of such obligation will cause a default in respect of loans that are significant to the operations of the listed issuer (Main Board Rule 13.18); or
- ▶ the listed issuer or any of its subsidiaries breaches the terms of a loan that is significant to the operations of the listed issuer, such that the lender may demand immediate repayment and the breach has not been waived by the lender (Main Board Rule 13.19).

Takeover offers – an announcement must be made once a takeover offer is made or accepted, as required by the Takeovers Code.

Announcements (Cont'd)

Accounts and auditors

Board meeting for approval of results – an issuer must inform the Exchange and publish an announcement at least 7 clear business days in advance of the date fixed for any board meeting at which the profits or losses for any period are to be approved for publication (Main Board Rule 13.43).

Annual and half-year results – must be published by way of announcement under Main Board Rule 13.49.

Change in auditor or financial year end – any change in a listed issuer's auditors or financial year end, the reason(s) for the change and any other matters that need to be brought to the attention of holders of the company's securities. The issuer's announcement must state whether the outgoing auditors have confirmed that there are no matters that need to be brought to the attention of holders of the company's securities (Main Board Rule 13.51(4)). The issuer must appoint an auditor at each annual general meeting ("**AGM**") to hold office until the next AGM. Any proposal to remove an auditor before the end of its term of office must be approved by shareholders in general meeting (Main Board Rule 13.88).

Announcements (Cont'd)

Company matters

Change of company name – once the board decides to change the company name (Main Board Rules 13.51).

Memorandum and Articles of Association – any proposed alteration of the memorandum or articles of association of the listed issuer (Main Board Rule 13.51(1)).

Registered office – any change in the company's registered address, agent for service of process in Hong Kong or registered office or registered place of business in Hong Kong (Main Board Rule 13.51(5)).

Share registrar – any change of the company's share registrar (including any overseas branch share registrar) (Main Board Rule 13.51(5)).

Announcements (Cont'd)

Company matters (Cont'd)

Dividends – an issuer must inform the Exchange and publish an announcement at least 7 clear business days in advance of the date fixed for any board meeting at which the declaration, recommendation or payment of a dividend is expected to be decided (Main Board Rule 13.43). Any decision of the board to declare, recommend or pay a dividend or not to do so must be announced immediately, and include the rate, amount and expected payment date (Main Board Rules 13.45(1) and (2)).

Change in nature of business – an announcement must be published of any decision to change the general character or nature of the issuer or the group (Main Board Rule 13.45(5)).

Winding-up or Liquidation – the appointment of a receiver or manager, the presentation of any winding-up petition or the passing of any resolution authorising the winding up of the listed issuer, its holding company or any of its major subsidiaries (i.e. a subsidiary representing 5% under any of the percentage ratios (please see “Notifiable Transactions” below) or any similar insolvency events (Main Board Rule 13.25(1)).

Decision to withdraw listing – a proposed withdrawal of listing must be notified to shareholders by way of publication of an announcement (Main Board Rule 6.15).

CHARLTONS
易周律师行

Announcements (Cont'd)

Corporate governance

Audit committee – if the issuer fails to set up an audit committee or does not meet the membership requirements (Main Board Rule 3.23).

Remuneration committee – if the issuer fails to set up a remuneration committee or does not comply with the requirements as to its composition or terms of reference (Main Board Rule 3.27)

Directors and officers

Board composition and independent non-executive directors – an announcement must be made if the number of the issuer's independent non-executive directors (“INEDs”) is less than 3 or one-third of the number of directors on the board or if it does not have at least one INED with appropriate professional qualifications or accounting or related financial management expertise; (Main Board Rule 3.11).

Change in company secretary – an announcement must be made once the board has decided to change the company secretary (Main Board Rule 13.51(5)).

Announcements (Cont'd)

Corporate governance (Cont'd)

Change in compliance adviser – an announcement must be made as soon as a compliance adviser resigns, and arrangements must be made immediately to appoint a new compliance adviser. Once a new compliance adviser has been appointed, another announcement must be made (Main Board Rules 13.51(6) and 3A.29).

Change in directors – any change of directors or the chief executive, including, in the case of the resignation or removal of a director or the chief executive, the reasons given by or to him for his resignation or removal (Main Board Rule 13.51(2)). An announcement of the appointment of a new director or chief executive or re-designation of a director or the chief executive must include the information specified in Main Board Rule 13.51(2).

Announcements (Cont'd)

Corporate governance (Cont'd)

Change in disclosed information about directors – any change to the information specified in paragraphs (h) to (v) of Main Board Rule 13.51(2) previously disclosed about a director must be announced (Main Board Rule 13.51B). Such information relates mainly to matters which may cast doubt on the integrity of the directors involved and their suitability for continuing to serve as directors. Any change in the information specified in paragraphs (a) to (e) and (g) of Main Board Rule 13.51(2) must be set out in the next published annual or interim report. The Rules include an obligation for directors to immediately inform the issuer of any information specified in Main Board Rule 13.51(2) and any change to such information (Main Board Rule 13.51C).

Announcements (Cont'd)

Meetings

Notice of general meetings – notice of an issuer's annual general meeting and other general meetings must be announced (Main Board Rules 13.37 and 13.73).

Results of general meetings – the poll results must be published before commencement of trading on the business day following the meeting (Main Board Rule 13.39(5)).

Shares

Issues of securities – an issue of securities (including convertible securities or warrants, options or similar rights) will almost always require an announcement (except an exercise of options under an employee share scheme) either as inside information under Main Board Rule 13.09(2)(a) or under Chapter 14 or 14A, or under Main Board Rule 13.28.

Changes in the number of issued shares – certain changes in the number of issued shares must be reported to the Exchange for publication on the Exchange's website on the following business day (Main Board Rule 13.25A). Issuers must also submit a monthly return of changes in their equity securities, debt securities and other securitised instruments (Main Board Rule 13.25B).

Announcements (Cont'd)

Shares (Cont'd)

Share option schemes – an employee share option scheme must be approved by shareholders in general meeting and a listed issuer must publish an announcement of the outcome of the meeting as soon as possible and no later than the business day following the meeting (Main Board Rule 17.02(1)). Further announcements must be published on the grant of share options pursuant to a share option scheme specifying the information required by Main Board Rule 17.06A.

Basis of allotment of securities – the basis of allotment of any securities offered to the public for subscription or sale or an open offer and of the results of any rights issue and, if applicable, of the basis of any acceptance of excess applications. The company must notify the Exchange of such matters no later than the morning of the next business day after the allotment letters or other relevant documents of title are posted (Main Board Rule 13.30).

Announcements (Cont'd)

Shares (Cont'd)

Public float – the company must inform the Exchange immediately if it becomes aware that the number of listed securities required to be held by the public has fallen below the prescribed minimum percentage (i.e. 25% unless a lower percentage of between 15% and 25% was approved by the Exchange on listing for a company having an expected market capitalisation at the time of listing of more than HK\$10 billion) (Main Board Rule 13.32(1)(a)).

Lack of genuine open market – if the Exchange believes that the issuer's securities lack a genuine open market or are concentrated in the hands of a few shareholders, it may require the issuer to publish an announcement (Main Board Rule 13.34(a)).

Share Repurchases – any purchase, sale, drawing or redemption by the issuer or its group members of its listed securities (whether on the Exchange or not) (Main Board Rule 13.31). The company should also be aware of the provisions of the Code on Share Buy-backs which sets out detailed rules governing any offer to purchase, redeem or otherwise acquire the shares of a listed issuer made by or on behalf of the listed issuer to any of its shareholders.

Announcements (Cont'd)

Announcements which Require Pre-vetting by the Exchange

Announcements of the following matters or transactions must be submitted to the Exchange for review and approval before publication under Main Board Rule 13.52(2):

- a) very substantial acquisitions, very substantial disposals or reverse takeovers under Main Board Rules 14.34 and 14.35;
- b) transactions or arrangements within 12 months after listing which would result in a fundamental change in principal business activities under Main Board Rules 14.89 to 14.91; and
- c) cash companies under Main Board Rules 14.82 and 14.83.

Announcements other than those specified in Main Board Rule 13.52(2) do not need to be pre-vetted by the Exchange, although companies may consult the Exchange regarding rule compliance issues. The Exchange also reserves the right under Main Board Rule 13.52A to require listed companies to submit for review any draft announcement, circular or other document in individual cases.

See the [Exchange's Guide on Pre-vetting and Selection of Headline Categories for Announcements](#) at

http://www.hkex.com.hk/eng/rulesreg/listrules/guidref/guide_pre_vetting_req.htm.

CHARLTONS
易周律師行

Matters Requiring Prior Consultation with Exchange Prior to Announcement

There are a number of Rule compliance issues relating to notifiable transactions or issues of securities which need the Exchange's prior consent or confirmation prior to publication of an announcement. These include, but are not limited to, the following:

- i. whether the Exchange will allow the listed issuer to adopt alternative size test(s) to classify a notifiable transaction under Main Board Rule 14.20;
- ii. whether the Exchange will deem a party to a transaction to be a connected person of the listed issuer under Main Board Rules 14A.07(6), 14A.75 or 14A.07(4). Main Board Rule 14A.22 requires a listed issuer to notify the Exchange of any proposed transaction with the parties described in such rules unless the transaction is exempt;
- iii. whether the transaction/matter falls under the special or exceptional circumstances described in the Listing Rules, e.g. a rights issue or open offer proposed by a Main Board issuer without underwriting under the notes to Main Board Rule 7.19 or 7.24; a proposed issue of securities for cash under general mandate at a price representing a discount of 20% or more to the benchmarked price under Main Board Rule 13.36(5); or a proposed issue of warrants that would not meet certain specific requirements under Main Board Rule 15.02; and

CHARLTONS
易周律师行

Matters Requiring Prior Consultation with Exchange Prior to Announcement (Cont'd)

- iv. In the case of matters affecting trading arrangements (including suspension or resumption of trading, and cancellation or withdrawal of listing), Main Board Rule 13.52B requires that:
 - a) listed issuers must consult the Exchange before issuing the relevant announcement; and
 - b) the announcement must not include any reference to a specific date or timetable which has not been agreed in advance with the Exchange.

Announcement (Cont'd)

Publication of Announcements under Rule 2.07C

- ▶ Announcements must be published on the website of the Exchange and on the listed issuer's own website.
- ▶ Listed companies must submit an electronic copy of the announcement through the Exchange's electronic submission system.
- ▶ When doing so, companies must select all appropriate headlines from the list of headline categories which are set out in Appendix 24 to the Main Board Rules.
- ▶ Unless stated otherwise in the Rules, all announcements must be in English and Chinese.

Announcement (Cont'd)

Publication of Announcements (Cont'd)

With the exception of certain limited types of announcements that can be published at all times during the operational hours of the e-Submission System, announcements must only be submitted during the designated publications windows which are:

On a normal business day:

- ▶ 6.00 a.m. to 8.30 a.m.
- ▶ 12.00 p.m. to 12.30 p.m.
- ▶ 4.15 p.m. to 11.00 p.m.

On the eves of Christmas, New Year and Lunar New Year when there is no afternoon session:

- ▶ 6.00 a.m. to 8.30 a.m.
- ▶ 12.00 p.m. to 11.00 p.m.

On a non-business day preceding a business day:

- ▶ 6.00 p.m. to 8.00 p.m.

Announcement (Cont'd)

The categories of announcements which can be published during trading hours as well as outside trading hours are:

- i. suspension announcements;
- ii. announcements made in response to unusual movements in share price or trading volume;
- iii. announcements denying the accuracy of news reports or clarifying that only its published information should be relied upon; and
- iv. overseas regulatory announcements.

Listing Documents and Circulars which require Pre-Vetting

Main Board Listing Rule 13.52(1) requires the following documents to be submitted to the Exchange for review and approval before publication:

- ▶ listing documents (including prospectuses);
- ▶ circulars relating to cancellation or withdrawal of listing of listed securities;
- ▶ circulars for notifiable transactions which are subject to shareholders' approval;
- ▶ circulars for connected transactions;
- ▶ circulars to the company's shareholders seeking their approval of issues of securities that require specific mandates from the shareholders (under Main Board Rule 13.36(1));

Listing Documents and Circulars which require Pre-Vetting (Cont'd)

- ▶ circulars to the issuer's shareholders seeking their approval of transactions or arrangements that require independent shareholders' approval and the inclusion of separate letters from independent financial advisers to be contained in the relevant circulars under Main Board Rule 13.39(7), which include:
 - a) spin-off proposals;
 - b) transactions which the Rules require to be subject to independent shareholders' approval (see Main Board Rule 13.39(4)(b)) such as:
 - 1) rights issues under Main Board Rule 7.19(6) or 7.19(7);
 - 2) open offers under Main Board Rule 7.24(5) or (6);
 - 3) refreshments of general mandates before next AGM under Main Board Rule 13.36(4);
 - 4) withdrawal of listings under Main Board Rule 6.12; and
 - 5) transactions or arrangements that would result in a fundamental change in the principal business activities of the listed issuer within 12 months after listing under Main Board Rules 14.89 to 14.91;

Listing Documents and Circulars which require Pre-Vetting (Cont'd)

- ▶ circulars to shareholders seeking their approval of any matter in relation to a share option scheme which is required under Chapter 17 of the Main Board Listing Rules;
- ▶ circulars to shareholders seeking their approval of warrant proposals involving approvals by shareholders and all warrant holders under paragraph 4(c) of Practice Note 4 to the Main Board Listing Rules; and
- ▶ circulars or offer documents issued by the issuer in connection with takeovers, mergers or offers.

Disclosure of Changes in the Number of Issued Shares

Next Day Disclosure Requirements

The Listing Rules require next day disclosure on the Exchange website of **2 categories** of changes in the number of issued shares.

The first category of changes which always require next day disclosure on the next business day, include:

- ▶ placings
- ▶ consideration issues
- ▶ open offers
- ▶ rights issues
- ▶ bonus issues
- ▶ scrip dividends
- ▶ repurchases of shares or other securities
- ▶ exercise of an option under the issuer's share option scheme/other than under the issuer's share option scheme by a director of the listed issuer
- ▶ capital reorganisation
- ▶ changes in the number of issued shares not falling within any of the categories above or any of the categories requiring disclosure in specified circumstances described below.

CHARLTONS
易周律师行

Disclosure of Changes in the Number of Issued Shares

(Cont'd)

Categories of Changes Requiring Next Day Disclosure in Specified Circumstances

- ▶ exercise of an option under a share option scheme other than by a director of the listed issuer;
- ▶ exercise of an option other than under a share option scheme not by director of the issuer;
- ▶ exercise of a warrant;
- ▶ conversion of convertible securities; or
- ▶ redemption of shares or other securities.

The specified circumstances include:

- ▶ where the event results in a change of 5% or more in the number of the issuer's issued shares; or
- ▶ where the listed issuer is required to make disclosure of a first category change and an event has occurred but not been disclosed (either as a second category change or in a monthly return (e.g. because the 5% *de minimis* threshold has not been reached)).

Disclosure of Changes in the Number of Issued Shares

(Cont'd)

Monthly Return

- ▶ in relation to movements in the listed issuer's equity securities, debt securities and any other securitised instruments during the period to which the monthly return relates;
- ▶ the return must be submitted no later than 8.30 a.m. on the fifth business day next following the end of each calendar month;
- ▶ the monthly return must be submitted irrespective of whether there has been any change in the information provided in the previous monthly return.

Disclosure of Financial Information

Annual Report and Accounts

A listed issuer must send a copy of its annual report including its annual accounts (and consolidated financial statements, if it prepares them) together with a copy of the auditors' report to every shareholder of the company and every holder of the company's listed securities not less than **21 days** before the date of the company's AGM and not later than **4 months** after the end of the financial year.

The annual accounts, directors' report and auditors' report must be prepared in English and Chinese and must be laid before the AGM.

In the case of overseas shareholders, the company may mail the English version only provided that a statement is included that a Chinese language version is available from the company on request.

Disclosure of Financial Information (Cont'd)

Annual Report and Accounts

- ▶ Financial statements must include the disclosures required under the relevant accounting standards adopted.
- ▶ Financial statements must also include a statement of profit or loss and other comprehensive income, a statement of financial position and other matters specified in Appendix 16 to the Listing Rules.
- ▶ Annual financial statements must be prepared in accordance with Hong Kong Financial Reporting Standards or International Financial Reporting Standards or, in the case of a Chinese issuer, China Accounting Standards for Business Enterprises.

Disclosure of Financial Information (Cont'd)

Half-Year Reports and Accounts

- ▶ Listed companies must prepare half-year reports and must send either the half-year report or a summary half-year report to the company's shareholders and holders of the company's listed securities within 3 months of the end of the first 6 months of each financial year.
- ▶ Financial statements in the half-year report are generally unaudited. This fact must be stated. If audited, the auditors' report and any qualifications must be included.
- ▶ Half-year reports must be reviewed by the Audit Committee.

Disclosure of Financial Information (Cont'd)

Quarterly Reporting

- ▶ Quarterly reporting is a Recommended Best Practice under the Corporate Governance Code – not a mandatory obligation under the Listing Rules.
- ▶ If quarterly results are published, they should be published within 45 days of the quarter end.
- ▶ If an issuer decides to publish quarterly results for any particular quarter, an announcement should be made to disclose the reasons for any subsequent decision not to publish those results.

Disclosure of Financial Information (Cont'd)

Preliminary Announcements of Results

A preliminary announcement of the company's annual and half-year results must be published on the business day after their approval by the board and:

For Annual Results

- ▶ within 3 months of the financial year end.

For Half-year Results

- ▶ within 2 months of the financial year end.

The announcement must be published on the websites of the Exchange and the issuer.

The Exchange will normally require trading in a listed issuer's shares to be suspended if it fails to publish its financial information on time (Main Board Rule 13.50).

Board Meetings

- ▶ The board should meet regularly and at least 4 times a year (at quarterly intervals) (Code Provision A.1.1).

Notice to Exchange in certain circumstances

- ▶ Issuer must inform Exchange and publish announcement at least 7 clear business days before any board meeting to approve the declaration, recommendation or payment of a dividend or the publication of financial results (Main Board Rule 13.43).

Voting at Board Meetings

- ▶ Subject to exceptions, director of a listed issuer must not vote on, or be counted in the quorum for, any board resolution approving any contract, arrangement or proposal in which he, or any of his close associates, has a material interest (Main Board Rule 13.44).

Notice to Exchange after Meetings

- ▶ Issuer must immediately inform the Exchange of any decision:
 - a) to declare, recommend or pay a dividend or make any other distribution;
 - b) not to declare, recommend or pay a dividend which would otherwise have been expected;
 - c) on preliminary announcement of profits or losses for any period;
 - d) on any proposed change in the capital structure (including a redemption of listed securities); and
 - e) on any change to the general character or nature of the business of the issuer or the group (Main Board Rule 13.45).

CHARLTONS
易周律师行

Shareholders' Meetings

Notice of General Meetings

Code Provision E.1.3 of the Corporate Governance Code requires:

- i. at least 20 clear business days' notice for AGMs; and
- ii. at least 10 clear business days' notice for all other general meetings.

Under the “comply or explain” principle underlying the Code, issuers must explain any failure to comply with these requirements in their interim and annual reports.

Notice of general meetings must be given to all shareholders (whether their address is in Hong Kong or not).

Notice of an AGM and all other general meetings of shareholders must be published on the websites of the Exchange and the issuer (Rules 13.37 and 13.73).

Shareholders' Meetings (Cont'd)

Mandatory Voting by Poll on all Resolutions at General Meetings

Voting by poll is mandatory on all resolutions at all general meetings under Main Board Rule 13.39(4). A chairman at a general meeting may exempt certain prescribed procedural and administrative matters from a vote by poll.

Listed issuers must appoint a scrutineer (who may be the issuer's auditors or share registrar or external accountants who are qualified to serve as auditors) to oversee the voting procedures.

The results of the poll must be announced as soon as possible and no later than 30 minutes before the earlier of the commencement of the morning trading session or any pre-opening session on the business day following the general meeting (Main Board Rule 13.39(5)).

The chairman of a shareholders' general meeting must ensure that the detailed procedures for conducting a poll are explained (Code Provision E.2.1).

Shareholders' Meetings (Cont'd)

Parties Required to Abstain from Voting:

Any shareholder that has a “material interest” in a transaction or arrangement to be approved at a general meeting of shareholders, is required to abstain from voting on the resolution (Main Board Rule 2.15).

Factors relevant to determining whether a shareholder has a “material interest” include:

- ▶ whether the shareholder is a party to the transaction or a close associate of such a party; and
- ▶ whether the transaction confers upon the shareholder or his close associate a benefit not available to other shareholders of the issuer (Main Board Rule 2.16).

Pre-emption Rights

Except for a pro rata offer to existing shareholders, the directors of a listed issuer are required to obtain the consent of shareholders in general meeting prior to the allotment, issue or grant of shares, securities convertible into shares or options, warrants or similar rights to subscribe for shares.

A general mandate may however be obtained from shareholders at a general meeting of shareholders to issue up to:

- 20% of the number of the company's issued shares as at the date of the resolution granting the general mandate; and
- the number of shares repurchased since the date of the mandate, if authorised separately (but no more than 10% of the number of issued shares as at the date of the resolution granting the repurchase mandate).

If a share consolidation or subdivision is conducted after the approval of the issue mandate, the maximum allowable number of securities to be issued will be adjusted accordingly

Main Board Rule 13.36 restrictions do not apply to *pro rata* offers made to all existing shareholders **excluding** those residing outside of Hong Kong, if the directors made enquiry as to the legal restrictions or requirements of any relevant regulatory authority or stock exchange in the relevant place, and consider the exclusion necessary or expedient as a result.

An EGM may be called to approve a share issue for a specific purpose.

CHARLTONS
易周律师行

Restrictions on Issues of Securities in 6 Months after Listing

A listed issuer is prohibited from issuing (or entering into any agreement to issue) any further shares or securities convertible into its equity securities within 6 months of the commencement of dealing in its securities on the Exchange (whether or not the issue will be completed within 6 months from commencement of dealing) except for:

- i. the issue of shares, the listing of which has been approved by the Exchange, under a Chapter 17 share option scheme;
- ii. the exercise of conversion rights attaching to warrants issued as part of the IPO;
- iii. any capitalisation issue, capital reduction or consolidation or sub-division of shares; and
- iv. the issue of shares or securities under an agreement entered into before the commencement of dealing, the material terms of which were disclosed in the IPO prospectus (Main Board Rule 10.08).

Issues of Securities for Cash

- ▶ An announcement containing the information required by Rule 13.28 must be published on the next business day of the directors' decision to issue securities for cash.
- ▶ In the case of a placing of securities for cash, securities cannot be issued under the general mandate if the price is at a discount of 20% or more to the benchmarked price of the securities (i.e. the higher of the closing price on the date of the agreement and the average closing price for the 5 trading days immediately before the earlier of:
 - i. the date of announcement of the transaction;
 - ii. the date of the agreement; and
 - iii. the date on which the price is fixed).

An exception applies where the issuer can satisfy the Exchange that it is in a serious financial position and can only be saved by an urgent rescue operation involving the issue of securities at a discount of 20% or more, or that other exceptional circumstances exist (Main Board Rule 13.36(5)).

Issues of Securities for Cash (Cont'd)

Where securities are issued for cash under a general mandate at a discount of $\geq 20\%$ to the securities' benchmarked price, the issuer must publish an announcement no later than 30 minutes before the opening of the morning trading session on the business day following the signing of the relevant agreement disclosing (among others):

- ▶ If there are < 10 allottees, the name of each allottee (or its beneficial owner) and confirmation of its independence from the issuer; and
- ▶ If there are > 10 allottees, the name of each allottee (or its beneficial owner) subscribing 5% or more of the issued securities and a generic description of all other allottees, and a confirmation of their independence from the issuer. In calculating the 5% limit, the number of securities subscribed by the allottee, its holding company and any of their subsidiaries must be aggregated.

Notifiable Transactions

Chapter 14 of the Listing Rules specifies certain transactions (principally acquisitions and disposals), particulars of which have to be notified to the shareholders, the Exchange and the general public. In some cases, shareholders' approval is also required. The term "listed issuer" means the listed issuer itself **and** its subsidiaries. Where a transaction is both "notifiable" and "connected", the issuer must comply with both Chapter 14 and Chapter 14A.

A transaction is widely defined and includes:

- an acquisition or disposal of assets, including a deemed disposal;
- a transaction where the listed issuer writes, accepts, transfers, exercises or terminates an option to acquire or dispose of assets or to subscribe for securities;
- entering into or terminating a finance lease where their financial effects have an impact on the listed issuer's balance sheet and/or profit and loss account;
- entering into or terminating operating leases which, by virtue of their size, nature or number, have a significant impact on the listed issuer's operations;

Notifiable Transactions (Cont'd)

- granting an indemnity or a guarantee or providing financial assistance other than to the listed issuer's subsidiaries; and
- entering into any arrangement or agreement involving the formation of a joint venture entity in any form.

The definition excludes (to the extent not specifically referred to above) transactions of a revenue nature in the ordinary and usual course of business and also the issue of new securities for cash (but these are within the definition of transaction which applies for connected transactions under Chapter 14A).

Notifiable Transactions (Cont'd)

▶ Transactions of a “Revenue Nature”

Relevant non-exhaustive factors include:

- whether previous transactions of the same nature were treated as of a revenue nature;
- historical accounting treatment of previous transactions of the same nature;
- whether the accounting treatment is in accordance with generally accepted accounting standards; and
- whether the transaction is a revenue or capital transaction for tax purposes (Note 4 of Main Board Rule 14.04(1)(g))

Transactions involving the acquisition and disposal of properties are generally not considered to be of a revenue nature unless carried out as one of the principal activities and in the ordinary and usual course of business of the listed issuer (Note 2 to Main Board Rule 14.04(1))

Notifiable Transactions (Cont'd)

▶ Transactions in the “Ordinary and Usual Course of Business”

“Ordinary and usual course of business” means the existing principal activities of the listed issuer or an activity wholly necessary for its principal activities.

Financial assistance is only provided “in the ordinary and usual course of business” by

- i. a “banking company” (i.e. an authorised financial institution under the Banking Ordinance) or
- ii. a licensed securities house providing financial assistance on normal commercial terms for a purpose specified in Main Board Rule 14.04(1)(e)(iii) (Main Board Rule 14.04(8)).

Notifiable Transactions (Cont'd)

Classification of Notifiable Transactions

Notifiable transactions are classified using the percentage ratios calculations set out in Main Board Rule 14.07.

Transaction Type	Assets ratio	Consideration ratio	Profits ratio	Revenue ratio	Equity capital ratio
Share transaction	less than 5%				
Discloseable transaction	5% or more but less than 25%				
Major transaction disposal	25% or more, but less than 75%	Not Applicable			
Major transaction acquisition	25% or more, but less than 100%				
Very Substantial Disposal	75% or more	75% or more	75% or more	75% or more	Not applicable
Very Substantial Acquisition	100% or more				

Note: The equity capital ratio relates only to an acquisition (and not a disposal) by a listed issuer issuing new equity capital.

CHARLTONS
易周律師行

Notifiable Transactions (Cont'd)

Chapter 14 sets out six categories of notifiable transactions:

- 1) A **share transaction** is an acquisition of assets (excluding cash) by a listed issuer where the consideration includes securities for which listing will be sought and where all percentage ratios are less than 5%;
- 2) A **discloseable transaction** is a transaction or a series of transactions by a listed issuer where any percentage ratio is 5% or more, but less than 25%;
- 3) A **major transaction** is a transaction or a series of transactions by a listed issuer where any percentage ratio is 25% or more, but less than 100% for an acquisition or 75% for a disposal;

Notifiable Transactions (Cont'd)

- 4) A **very substantial disposal** is a disposal or a series of disposals of assets by a listed issuer where any percentage ratio is 75% or more;
- 5) A **very substantial acquisition** is an acquisition or a series of acquisitions of assets by a listed issuer where any percentage ratio is 100% or more; and
- 6) A **reverse takeover** is “**an acquisition or a series of acquisitions** which, in the opinion of the Exchange, constitutes, or is part of a transaction or arrangement or series of transactions or arrangements which **constitute an attempt to achieve a listing of the assets to be acquired and a means to circumvent the requirements for new applicants** set out in Chapter 8 of the Listing Rules and normally refers to:
 - a) an acquisition/series of acquisitions of assets **constituting a very substantial acquisition** where there is or which will result in a **change in control** (i.e. 30% or more of the voting rights) of the listed issuer; or
 - b) an acquisition/series of acquisitions of assets **from the incoming controlling shareholder(s) or his/their associates within 24 months after the change in control** that had not been regarded as a reverse takeover, which individually or together **reach the threshold for a very substantial acquisition**.

Notifiable Transactions (Cont'd)

▶ *Reverse Takeovers (Cont'd)*

In determining whether an acquisition(s) constitute(s) a very substantial acquisition, the lower of:

- i. the latest published figures of the asset value, revenue and profits shown in the listed issuer's accounts and the market value of the listed issuer at the time of the change in control; and
- ii. the latest published figures of the asset value, revenue and profits shown in the listed issuer's accounts and the market value of the listed issuer at the time of the acquisition(s),

is used as the denominator of the percentage ratios (Main Board Rule 14.06(b))

Notifiable Transactions (Cont'd) Percentage Ratios

To determine the category into which a transaction falls, the listed issuer must calculate the following ratios:

(i) Assets ratio =
$$\frac{\text{Total assets that are the subject of the transaction}}{\text{Total assets of the listed issuer}}$$

Total assets = current assets + non-current assets + fixed assets + intangible assets (**Main Board Rule 14.04(12)**)

Intangible assets include goodwill (whether positive or negative)

(ii) Profits ratio =
$$\frac{\text{Profits attributable to the assets that are the subject of the transaction}}{\text{Profits of the listed issuer}}$$

Profits = net profits after deducting all charges except taxation and before minority interests and extraordinary items

Notifiable Transactions (Cont'd) Percentage Ratios

(iii) Revenue ratio =
$$\frac{\text{Revenue attributable to the assets that are the subject of the transaction}}{\text{Total revenue of the listed issuer}}$$

Revenue = Revenue arising from the principal activities of a company, excluding revenue and gains that arise incidentally

(iv) Consideration ratio =
$$\frac{\text{Fair value of the consideration}^*}{\text{Total market capitalization of listed issuer}^{**}}$$

*Determined at the date of the agreement according to Hong Kong Financial Reporting Standards or International Financial Reporting Standards (**Main Board Rule 14.15(1)**)

Total market capitalization = average closing price of the listed issuer's securities for the 5 business days preceding the transaction (Main Board Rule 14.07(4)**)

(v) Equity capital ratio =
$$\frac{\text{Number of shares to be issued by the listed issuer as consideration}}{\text{Total number of the listed issuer's issued shares immediately before the transaction}}$$

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd) Percentage Ratios

Regarding the equity capital ratio:

- the numerator (number of shares to be issued as consideration) includes shares that may be issued upon conversion or exercise of any convertible securities or subscription rights to be issued or granted as consideration; and
- the listed issuer's debt capital (if any), including any preference shares, is not included.

If any size test produces an anomalous result or is inappropriate to the issuer's sphere of activity, the HKEx may substitute other relevant size indicators or industry specific tests (Main Board Rule 14.20).

Notifiable Transactions (Cont'd)

Percentage Ratios

▶ Classification of Transactions

Transactions involving acquisition and disposal

- ▶ Where a transaction involves both an acquisition and a disposal, the Exchange will apply the percentage ratios to both the acquisition and the disposal. The transaction will be classified based on the larger of the acquisition or disposal, and subject to the requirements applicable to that classification.
- ▶ Where a shareholders' circular is required, each of the acquisition and disposal will be subject to the content requirements applicable to their respective transaction classification (Main Board Rule 14.24).

Notifiable Transactions (Cont'd) Aggregation of Transactions

HKEx may require a listed issuer to aggregate a series of transactions and treat as one if they were all completed within 12 months or are otherwise related (Main Board Rule 14.22).

Relevant factors include:

- are entered into by the listed issuer with the same party or with parties connected or otherwise associated with one another;
- involve the acquisition or disposal of securities or an interest in one particular company or group of companies;
- involve the acquisition or disposal of parts of one asset; or
- together lead to substantial involvement by the listed issuer in a business activity which did not previously form part of the listed issuer's principal business activities.

Notifiable Transactions (Cont'd)

Requirements: Summary of requirements for different categories of notifiable transactions

	Notification to Exchange	Short suspension of dealings	Publication of an Announcement	Circular to shareholders	Shareholder approval	Accountants' report
Share transaction	Yes	Yes	Yes	No	No ¹	No
Discloseable transaction	Yes	No, unless there is PSI	Yes	No	No	No
Major transaction	Yes	Yes	Yes	Yes	Yes ²	Yes ³
Very substantial disposal	Yes	Yes	Yes	Yes	Yes ²	No ⁵
Very substantial acquisition	Yes	Yes	Yes	Yes	Yes ²	Yes ⁴
Reverse takeover	Yes	Yes	Yes	Yes	Yes ^{2,6}	Yes ⁴

- Notes: 1. Shareholder approval is not required if the consideration shares are issued under a general mandate.
 2. Any shareholder and his associates must abstain from voting if such shareholder has a material interest in the transaction.
 3. An accountants' report on the business, company or companies being acquired is required.
 4. An accountants' report on any business, company or companies being acquired is required.
 5. The listed issuer may include an accountants' report.
 6. Approval of the Exchange is also necessary.

CHARLTONS
易周律師行

Notifiable Transactions (Cont'd)

Requirements for Announcements

Announcement

- ▶ As soon as possible after the terms of the notifiable transaction have been finalised, the issuer must:
 - inform the Exchange; and
 - publish an announcement on the Exchange's website and issuer's own website (Main Board Rule 14.34)

- ▶ Where a listed issuer has signed an agreement for a notifiable transaction and an announcement has not been published on a business day, the issuer must request a short suspension of dealings pending publication of the announcement.

- ▶ Where a listed issuer has signed an agreement for a notifiable transaction which is expected to be price sensitive, the issuer must immediately request a short suspension of dealings pending publication of an announcement. Once an issuer has finalised the major terms of a notifiable transaction which is expected to be price sensitive, it must ensure confidentiality of relevant information until the publication of an announcement (Main Board Rule 14.37).

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd)

Requirements for Announcements

Announcement

- ▶ Main Board Rule 14.58 requires all notifiable transaction announcements to include:
 - a prominent disclaimer of the liability of Hong Kong Exchanges and Clearing Limited and the Stock Exchange of Hong Kong Limited
 - a description of the principal business activities of the issuer and the counterparty
 - date of the transaction
 - confirmation that the counterparty and its ultimate beneficial owner are third parties independent of the listed issuer and its connected persons
 - aggregate consideration, how it will be satisfied and any arrangements for deferred payment
 - the basis for the determination of the consideration
 - value (book value and valuation, if any) of the transaction assets
 - where applicable, the net profits (before and after tax and extraordinary items) attributable to the transaction assets for the 2 preceding financial years
 - the reasons for entering into the transaction, the benefits expected to accrue to the issuer and a statement that the directors believe that the transaction terms are fair and reasonable and in the interests of shareholders as a whole
 - details of any guarantee and/or other security given or required

CHARLTONS
易周律師行

Notifiable Transactions (Cont'd)

Additional Requirements for Share Transaction Announcements

Announcements of Share Transactions must include the following additional information:

- ▶ The amount and details of the securities being issued and details of any restrictions on the subsequent sale of such securities
- ▶ Brief details of the assets being acquired, including the name of any company or business or the assets or properties and, if the assets include securities, the name and general description of the activities of the company in which the securities are held
- ▶ If the transaction involves an issue of securities by a subsidiary of the listed issuer, a declaration as to whether the subsidiary will continue to be a subsidiary after the transaction
- ▶ A statement that the announcement appears for information purposes only and does not constitute an invitation or offer to acquire, purchase or subscribe for the securities
- ▶ A statement that application has been or will be made to the HKEx for listing and permission to deal in the securities (Main Board Rule 14.59)

Notifiable Transactions (Cont'd) Announcements Requirements (Cont'd)

Additional Requirements for announcements of notifiable transactions (other than share transactions) are:

- ▶ the general nature of the transaction including, if securities are involved, details of any restrictions applying to subsequent sale of the securities;
- ▶ brief details of the assets being acquired or disposed of, including the name of the company/business or assets or properties and if the assets include securities, the name and general activities of the company in which the securities are held;
- ▶ in the case of a disposal:
 - details of the gain or loss expected and the basis of its calculation (the gain or loss should be calculated by reference to the carrying value); and
 - the intended application of the sale proceeds;
- ▶ for a major transaction to be approved by written shareholders' approval of a shareholder or a closely allied group of shareholders, the name of the shareholder(s), the number of shares held by each and the relationship between the shareholders;

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd) Announcements Requirements (Cont'd)

Additional Requirements for announcements of notifiable transactions (other than share transactions) are :

- ▶ where the transaction involves the disposal of an interest in a subsidiary, a declaration as to whether the subsidiary will continue to be a subsidiary after the transaction; and
- ▶ (except for disclosable transactions) the expected date of despatch of the circular to shareholders and, if this is more than 15 days after the announcement date, the reasons why this is so.

Notifiable Transactions (Cont'd) Shareholders' Approval Requirements

- ▶ Major Transactions, Very Substantial Disposals, Very Substantial Acquisitions and Reverse Takeovers must be made conditional on shareholders' approval.
- ▶ All voting at general meetings must be taken by poll (Main Board Rule 13.39(4)) and the results of the poll must be announced on the next business day following the meeting.
- ▶ The issuer must appoint its auditor, share registrar or external accountants to act as scrutineer for the vote taking.
- ▶ Any shareholder that has a material interest in the transaction must abstain from voting.
- ▶ Factors relevant to determining whether a shareholder has a "material interest" include:
 - whether the shareholder is a party to the transaction or a close associate of such a party; and
 - whether the transaction confers upon the shareholder or his close associate a benefit not available to other shareholders of the issuer (Main Board Rule 2.16)

Notifiable Transactions (Cont'd) Shareholders' Approval Requirements (Cont'd)

- ▶ On a reverse takeover where there is a change in control of the listed issuer, and any person/group of persons will cease to be a controlling shareholder (“**outgoing controlling shareholder**”) by virtue of a disposal of shares to a person/group of persons gaining control (“**incoming controlling shareholder**”), any of the incoming controlling shareholder’s associates or an independent third party, the outgoing controlling shareholder and his associates are prohibited from voting in favour of a resolution approving an injection of assets from the incoming controlling shareholder or his associates at the time of the change in control. The prohibition does not apply if the decrease in the outgoing controlling shareholder’s holding results solely from dilution through a new issue of shares to the incoming controlling shareholder.

Notifiable Transactions (Cont'd)

Written Shareholders' Approval and Requirement for Circular to Shareholders

Written Shareholders' Approval

Written shareholders' approval is allowed for Major Transactions only if:

- ▶ no shareholder would be required to abstain from voting;
- ▶ a “closely allied group of shareholders” holding more than 50% of the voting rights approves the transaction; and
- ▶ the reporting accountants' opinion in the accountants' report is unqualified

Circular to Shareholders

- ▶ Circulars for Major Transactions, VSDs and VSAs and listing documents for RTOs and must:
 - provide clear, concise and adequate explanation of subject matter;
 - contain all information necessary to allow shareholders to make an informed decision;

Notifiable Transactions (Cont'd)

Written Shareholders' Approval and Requirement for Circular to Shareholders

Circular to Shareholders (cont'd)

- Confirm that to the best of the directors' knowledge, information and belief (having made all reasonable enquiry) the counterparty and the ultimate beneficial owner of the counterparty are third parties independent of the issuer and its connected persons.
- A Circular for a Major Transaction to be approved by written shareholders' approval must be sent to shareholders within 15 business days after publication of the announcement (Main Board Rule 14.41(a))
- Circulars for Major Transactions to be approved at general meeting, VSAs and VSDs must be sent to shareholders at the same time as or before the issuer gives notice of the general meeting (Main Board Rules 14.41(b) and 14.51)

Notifiable Transactions (Cont'd)

Requirement for Circular to Shareholders

The issuer must send to shareholders any revised or supplementary circular and/or provide any material information that has come to the directors' attention after the issue of the circular (by way of announcement) not less than 10 business days before the date of the general meeting (Main Board Rules 14.42 and 14.52).

- ▶ Additional Requirements for Circulars for Major Transactions involving an acquisition of any business or company(ies)
 - an accountants' report on the business or company(ies) being acquired (although the HKEx may relax this requirement if the company will not become a subsidiary of the issuer);
 - a pro forma statement of the assets and liabilities of the listed issuer's group combined with those of the business or company(ies) being acquired on the same accounting basis (Main Board Rule 14.67(6)(a)); and
 - a discussion and analysis of the results of the business or company(ies) being acquired (Main Board Rule 14.67(7))

Notifiable Transactions (Cont'd)

Requirement for Circular to Shareholders (Cont'd)

- ▶ Additional Requirements for Circulars for Major Transactions involving an acquisition of any revenue generating assets (other than a business or company)
 - a profit and loss statement and valuation for the 3 preceding financial years (or less if the asset was held by the vendor for a shorter period) on the identifiable net income stream and valuation in relation to such assets, reviewed by the auditors or reporting accountants
 - a pro forma statement of the assets and liabilities of the listed issuer's group combined with the assets being acquired on the same accounting basis (Main Board Rule 14.67(6)(b))
 - a discussion and analysis of the results of the business or company(ies) being acquired (Main Board Rule 14.67(7))

- ▶ Additional Requirements for Circulars for VSAs and RTOs involving an acquisition of any business or company(ies)
 - an accountants' report on the business or company(ies) being acquired
 - a pro forma income statement, balance sheet and cash flow statement of the enlarged group on the same accounting basis (Main Board Rule 14.69(4)(a))
 - in relation to a VSA, a separate discussion and analysis of the performance of each of the group and any business or company acquired for the period referred to in Main Board Rule 4.06(1)(a)

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd)

Requirement for Circular to Shareholders (Cont'd)

- ▶ Additional Requirements for Circulars for VSAs and Reverse Takeovers involving an acquisition of any revenue generating assets (other than a business or company)
 - a profit and loss statement and valuation for the 3 preceding financial years (or less if, other than in the case of an RTO, the asset held by vendor for shorter period) on the identifiable net income stream and asset valuation, reviewed by the auditors or reporting accountants
 - a pro forma profit and loss statement and net assets statement on the enlarged group on the same accounting basis (Main Board Rule 14.69(4)(b))
 - in relation to a VSA, a separate discussion and analysis of the performance of each of the group and any business or company acquired for the period referred to in Main Board Rule 4.06(1)(a) (Main Board Rule 14.69(7))

Notifiable Transactions (Cont'd)

Additional Requirements for Very Substantial Disposal Circulars

- ▶ Additional Requirements for VSD Circulars on a disposal of a business or company(ies) are:
 - financial information on either (a) the business or company(ies) being disposed of; or (b) the issuer's group with the business or company(ies) being disposed of shown separately as a disposal group(s) or a discontinuing operation(s) for the relevant period described in Main Board Rule 4.06(1)(a);
 - the financial information must include at least the income statement, balance sheet, cash flow statement and statement of changes in equity and must be reviewed by the issuer's auditors or reporting accountants; and
 - a pro forma income statement, balance sheet and cash flow statement of the remaining group on the same accounting basis (Main Board Rule 14.68(2)(a)).

- ▶ Additional Requirements for VSD Circulars on a disposal of revenue-generating assets (other than a business or company(ies) are:
 - a profit and loss statement and valuation for the 3 preceding financial years (or less where the asset was held by the issuer for a shorter period) on the identifiable net income stream and valuation in relation to such assets, which are reviewed by the auditors or reporting accountants; and
 - a pro forma profit and loss statement and net assets statement on the remaining group on the same accounting basis (Main Board Rule 14.68(2)(b))

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd)

Summary of historical financial information requirements applicable to acquisitions of any business, company, companies or revenue-generating asset with an identifiable income stream or asset valuation.

	Where the target is a business/ company	Where the target is a revenue- generating asset with an identifiable income stream or asset valuation
Major disposal	Not required	Not required
Major acquisition	Accountants' report on the <u>target</u>	Profit/ loss statement and (where available) valuation of the target
Very substantial disposal	Financial information of either the <u>target</u> or <u>the listed issuer group with the target shown separately</u>	Profit/ loss statement and (where available) valuation of the target
Very substantial acquisition or reverse takeover	Accountants' report on the <u>target</u>	Profit/ loss statement and (where available) valuation of the target

Notifiable Transactions (Cont'd)

Summary of pro forma financial information requirements applicable to acquisitions of any business, company, companies or revenue-generating asset with an identifiable income stream or asset valuation.

	Where the target is a business/ company	Where the target is a revenue- generating asset with an identifiable income stream or asset valuation
Major disposal	Not required	Not required
Major acquisition	Pro forma statement of assets and liabilities of the <u>enlarged</u> group	Pro forma statement of assets and liabilities of the <u>enlarged</u> group
Very substantial disposal	Pro forma income statement, balance sheet and cash flow statement of the <u>remaining</u> group	Pro forma profit and loss statement and net assets statement on the <u>remaining</u> group
Very substantial acquisition or reverse takeover	Pro forma income statement, balance sheet and cash flow statement of the <u>enlarged</u> group	Pro forma profit and loss statement and net assets statement on the <u>enlarged</u> group

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd)

Additional Requirements for Reverse Takeovers

- ▶ Issuer proposing an RTO will be treated as a new listing applicant (Main Board Rule 14.54)
- ▶ Enlarged group or assets to be acquired must be able to meet one of the financial tests in Main Board Rule 8.05 and all other basic listing requirements
- ▶ Listed issuer must issue a prospectus and pay an initial listing fee

Definition of Reverse Takeover

- ▶ “acquisition(s) by a listed issuer which, in the Exchange’s opinion, constitute(s) an attempt to achieve a listing of the assets to be acquired and a means to circumvent the requirements for a new listing” (the ‘**Definition**’) (preamble to Main Board Rule 14.06)
- ▶ Bright Line Tests apply to 2 specific forms of reverse takeover:
 - a) VSA of assets where there is a change of control of listed issuer; or
 - b) VSA of assets from the incoming controlling shareholder within 24 months of the change of control.
- ▶ Where the VSA is within Bright Line Tests it will be an RTO and issuer treated as new listing applicant.

CHARLTONS
易周律师行

Notifiable Transactions (Cont'd)

Additional Requirements for Reverse Takeovers

- ▶ A VSA which is outside the Bright Line Tests may still be treated as an RTO if it falls within the Definition (i.e. the Exchange considers that the acquisition(s) are an attempt to list the assets acquired and circumvent the new listing requirements).

Exchange Guidance Letter HKEx-GL78-14

- ▶ Where there is no change in control, the Exchange will treat a VSA which attempts to list the assets acquired and circumvent the new listing requirements as an RTO only if it is an **extreme case**
- ▶ In evaluating whether a backdoor listing is an extreme case, the following factors are taken into account:
 - the size of the acquisition relative to the size of the issuer;
 - the quality of the acquired business – whether it can meet the trading record requirements for new listings, or whether it is unsuitable for listing (the example given here by the Committee is an early stage exploration company);

Notifiable Transactions (Cont'd)

Additional Requirements for Reverse Takeovers

- the size and type of business that the issuer was engaged in prior to the acquisition (a key question here is whether it is merely a listed shell or not);
- any fundamental alteration to the issuer's principal business (e.g. the existing business would be discontinued or very immaterial to the enlarged group's operations post acquisition);
- any other events and transactions, whether they be historical, proposed or intended, which, when considered alongside the acquisition, constitute a sequence of arrangements designed to circumvent the RTO Rules (e.g. a disposal of the issuer's original business simultaneous with a very substantial acquisition); and
- any issue of Restricted Convertible Securities to the vendor which would provide it with *de facto* control of the issuer.

Notifiable Transactions (Cont'd)

Additional Requirements for Reverse Takeovers

▶ Non-extreme cases

Where a VSA seems to be a backdoor listing within the Definition, but is not an extreme case, the Exchange will generally require enhanced prospectus-style disclosure in the issuer's transaction circular and adopt a more stringent vetting approach.

▶ Extreme VSAs ("borderline cases")

Where a VSA is an extreme case, but the acquired business(es) can meet the track record requirements so circumvention of the new listing requirements is not a material concern, the VSA is not treated as an RTO subject to requirements for a new listing. Instead, Exchange requires enhanced prospectus-style disclosure in shareholders' circular and applies enhanced vetting procedure.

▶ Acquisition of new business

Acquisitions of new businesses or assets cases are more likely to be regarded as new listings as enhanced disclosure is of limited use where the business/assets acquired have little in the way of operating history or track record.

Notifiable Transactions (Cont'd)

- ▶ **Reverse Takeovers: Listing Committee Report 2008/09 - Reverse Takeovers and restriction on disposals after a change of control (Main Board Rules 14.92 and 14.93)**
 - The Listing Rules prohibit a listed issuer from disposing of its existing business within 24 months after a change in control unless assets acquired by the listed issuer after the change in control can meet the trading record requirement of Main Board Rule 8.05. If not, on a disposal by a listed issuer of its existing business within 24 months of a change in control, the issuer will be treated as a new listing applicant.
 - Aim of Main Board Rules 14.92 and 14.93 – prevent the circumvention of reverse takeover rules by a new controlling shareholder deferring the sale of existing business until after the asset injection, thereby avoiding classification as a VSA.
 - A waiver of Main Board Rule 14.92 can be sought for a legitimate sale of an existing business within 24 months of a change of control provided that:
 - the incoming controlling shareholder has not injected assets into the listed issuer; and
 - after factoring in the disposal(s) of the issuer's existing business, the asset injection(s) before and after the change in control would not have constituted a VSA.

- ▶ *See Listing Committee's Annual Reports of 2008 and 2009 and Listing Decision HKEx-LD7-2011.*

CHARLTONS
易周律師行

Notifiable Transactions (Cont'd)

Pre-Vetting Requirements for Notifiable Transaction Circulars

Circulars or listing documents in respect of notifiable transactions must be pre-vetted (that is, reviewed and approved by the Exchange) before publication, including listing documents and prospectuses (e.g. for reverse takeovers, that are treated as new listings). (Main Board Rule 13.52(1))

Connected Transactions

Introduction

The rules on connected transactions are set out in Chapter 14A of the Main Board Listing Rules.

Their objectives are:

- a) to ensure that a listed issuer takes into account the interests of shareholders as a whole when it or one of its subsidiaries enters into connected transactions; and
- b) to provide safeguards against the directors, chief executive and substantial shareholders (or their associates) taking advantage of their positions. This is achieved by the general requirement of independent shareholders' approval for connected transactions.

Connected Transactions (Cont'd)

Generally, a connected transaction is any transaction between a **listed issuer** or **any of its subsidiaries** and a **connected person**.

For classification purposes, the Exchange may aggregate a series of transactions that are completed over a 12-month period or are otherwise related (Main Board Rule 14A.81).

Factors which the Exchange takes into account in determining whether connected transactions should be aggregated are whether they:

- i. are entered into by the listed issuer with the same party or parties connected/associated with one another;
- ii. involve the acquisition or disposal of securities or an interest in one particular company or group of companies;
- iii. involve the acquisition or disposal of parts of one asset; or
- iv. together lead to substantial involvement by the listed issuer in a business activity not previously part of its principal business activities (Main Board Rule 14A.82).

The Exchange may consider aggregating continuing connected transactions with a single connected person (Main Board Rule 14A.83).

CHARLTONS
易周律師行

Connected Transactions (Cont'd)

▶ Definitions

Transaction

The term “transaction”, **whether or not** it is of a revenue nature in the ordinary and usual course of business, includes:

- a) the acquisition or disposal of assets (including deemed disposals under Main Board Rule 14.29)
- b) any transaction involving an option to acquire or dispose of assets or to subscribe for securities;
- c) entering into or terminating finance/ operating leases;
- d) granting an indemnity or a guarantee or providing financial assistance;
- e) entering into a joint venture in any form;
- f) issuing new securities of the issuer or its subsidiaries;
- g) provision or receipt of services;
- h) sharing of services;
- i) providing or acquiring raw materials, intermediate products and finished goods; and
- j) a qualified property acquisition.

(Main Board Rule 14A.24)

CHARLTONS
易周律师行

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

Connected Person

- a) a **director, chief executive or substantial shareholder** (holding 10% or more of the voting rights) of the **listed issuer** or any of its **subsidiaries**, or an **associate** of any such persons;

Persons connected with the listed issuer's "insignificant subsidiaries" are **not** connected persons. An "insignificant subsidiary" is a subsidiary of the issuer whose total assets, profits and revenues are less than:

- i. 10% under the percentage ratios for each of the three preceding financial years; or
- ii. 5% under the percentage ratios for the latest financial year (Main Board Rule 14A.66).

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

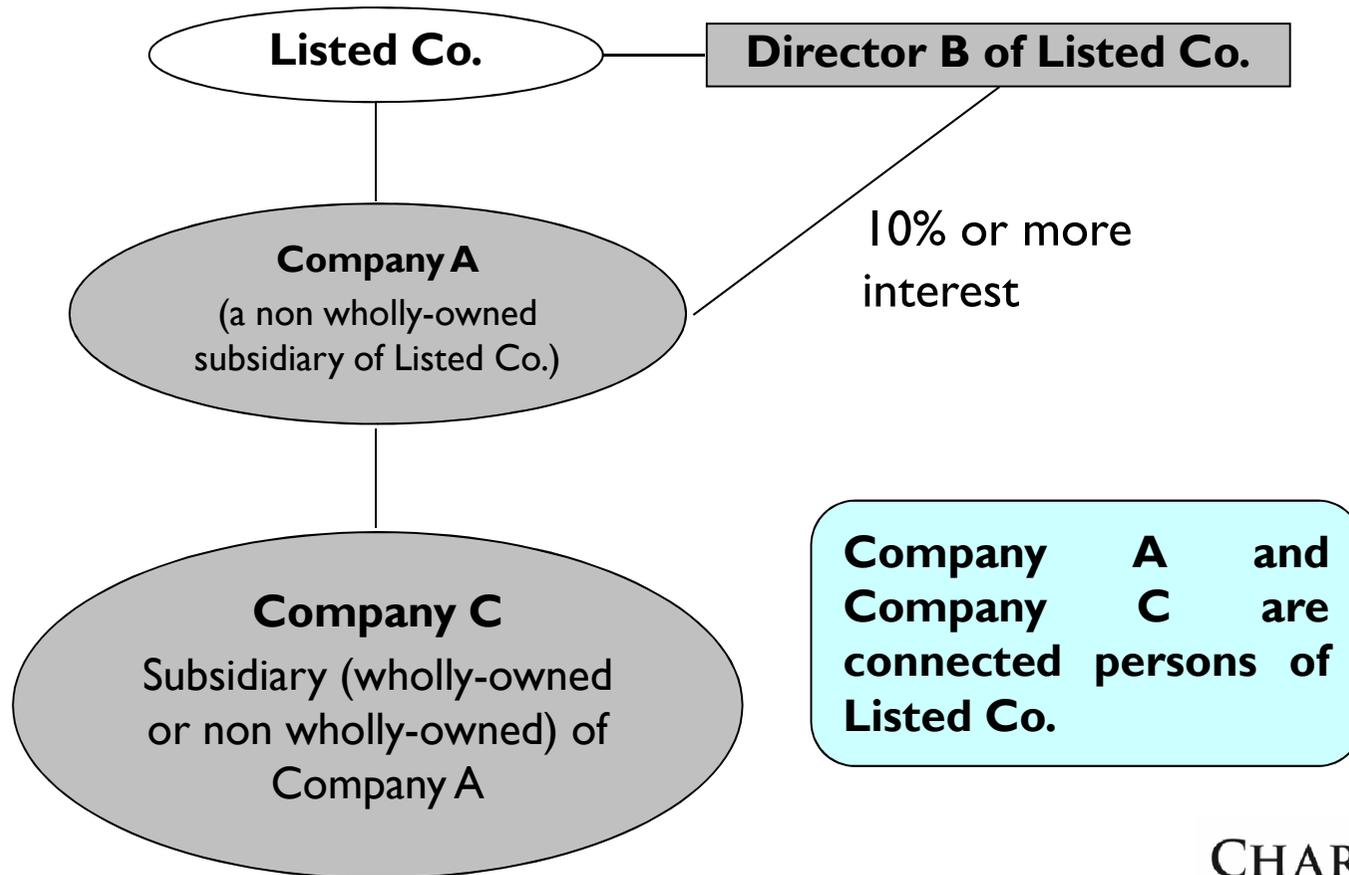
Connected Person (Cont'd)

- b) a **person who was a director** of the listed issuer or any of its subsidiaries in the past 12 months, or an **associate** of such a person; or
- c) a **connected subsidiary** – i.e. a **non-wholly owned subsidiary** of the listed issuer where any connected person(s) at the **issuer level** are entitled to exercise, or control the exercise of, **10% or more of the voting power** at general meetings of the non-wholly owned subsidiary or a **subsidiary of such a non-wholly owned subsidiary**.

*Note: A **wholly-owned subsidiary** of a listed issuer is **not** a connected person.*

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)



CHARLTONS
易周律师行

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

Associates of an individual

- a) his spouse, his (or his spouse's) child or step-child (natural or adopted) under the age of 18 (each an “**immediate family member**”);
- b) the trustees, acting in their capacity as trustee of any trust of which the **individual** or his **immediate family member** is a beneficiary or, in the case of a discretionary trust, is (to his knowledge) a discretionary object (the “**trustees**”);

However, the trustees of an employee share scheme or occupational pension scheme are not “associates” of a connected person if;

- i. the scheme is established for a wide scope of participants; and
- ii. the connected persons' interests in the scheme are together less than 30% (Main Board Rule 14A.18(1))

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

Associate of an individual (Cont'd)

- c) a company in which in which the **individual**, his **immediate family members** and/or the **trustees** (individually or together) control **30%** or more of the voting power or control the board's composition, and **any subsidiary** of such company;

An entity is excluded from the definition of associate if the interests of the connected person and his associates in the entity (other than those held through the issuer) are together less than 10%

- d) a person cohabiting with him as a spouse, or his child, step-child, parent, step-parent, sibling or step-sibling (each a "**family member**");
- e) a company in which the **family members** (individually or together), or the **family members** together with the **individual**, his **immediate family members** and/or the **trustees** control **50%** or more of the voting power or control the board's composition, and any of its **subsidiaries**;

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

Associate of an individual (Cont'd)

- f) a parent-in-law, brother-in-law, sister-in-law, son-in-law, daughter-in-law, grandparent, grandchild, uncle, aunt, nephew, niece or cousin of the connected person (each a “**relative**”) whose association with the **connected person** is such that, in the opinion of the Exchange, the proposed transaction should be subject to the connected transaction requirements ; or
- g) a company in which the **relatives** (individually or together) or the relatives together with the connected person, the trustees, his immediate family members and/or family members control **50%** or more of the voting power or control the board’s composition, and any of its **subsidiaries**, whose association with the **connected person** is such that, in the opinion of the Exchange, the proposed transaction should be subject to the connected transaction requirements.

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

Associates of a company

- a) its **subsidiary, holding company, or fellow subsidiary** of such a holding company (together “**group companies**”);
- b) the **trustees** of any trust of which the company is a beneficiary or, to its knowledge, discretionary object (the “**trustees**”);
- c) a **company** in which the company, the group companies and/or the trustees (individually or together), can:
 - i. exercise or control the exercise of **30% or more of the voting power** at general meetings; or
 - ii. control the composition of a majority of the board of directors; and
- d) a **subsidiary** of a company in (c).

Connected Transactions (Cont'd)

▶ Definitions (Cont'd)

Deemed Connected Persons

The Exchange has the power to deem a person or entity as an issuer's connected person where the person or entity:

- a) has entered, or proposes to enter, into:
 - i. a transaction with the group; and
 - ii. an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with respect to the transaction with a director, chief executive or substantial shareholder of the issuer or any of its subsidiaries or person who was a director within the previous 12 months; and
- b) should, in the Exchange's opinion, be considered as a connected person.

Connected Transaction Where There Is No Transaction With A Connected Person

The following transactions between a group and non-connected persons are also connected transactions.

Acquisition of interest in a company in which a Controller has an interest

- a) a group's acquisition of an interest in a company ("**target company**") where a substantial shareholder of that company is, or is proposed to be a **controller** (i.e. a director, chief executive or controlling shareholder of the listed issuer or any of its subsidiaries) or an associate of a controller.

Acquiring the target company's assets is also a connected transaction if the assets account for 90% or more of the target company's total or net assets.

However, the following transactions with third parties where a controller is, or will be, a shareholder of the target company are **not** connected transactions:

- any disposal of interests in the target company to a third party where a controller at the issuer level is a substantial shareholder of the target company;
- any acquisition or disposal of interests in the target company from or to a third party where a controller at the subsidiary level is a substantial shareholder of the target company; and
- transactions involving the issuer (or its controller) acquiring interests in a target company in specific circumstances where the controller has or will have an interest of less than 10% in the target company

Connected Transaction (Cont'd)

▶ Financial assistance

Financial assistance includes granting credit, lending money, providing security for, or guaranteeing a loan (Main Board Rules 14A.06(17) and 14A.24(4)).

Financial assistance provided by a listed issuer or its subsidiaries

- a) to a connected person; or
- b) to a Commonly Held Entity.

Financial assistance provided to a listed issuer or its subsidiaries

- a) by a connected person; or
- b) by a Commonly Held Entity.

Main Board Rules 14A.26 and 14A.27

Connected Transaction (Cont'd)

▶ **Financial assistance**

Financial assistance for the benefit of connected interests

An indemnity or guarantee granted, or financial assistance provided, by the listed issuer or its subsidiaries to and/or for the benefit of a connected person or a Commonly Held Entity

Granting security to connected interests

Security granted over the assets of a listed issuer or its subsidiaries in respect of any financial assistance made to the listed issuer or its subsidiaries by a connected person or Commonly Held Entity

Main Board Rules 14A.25 and 14A.26

Connected Transaction (Cont'd)

Commonly Held Entity

A company whose shareholders include:

- a) a member of the listed issuer's group; and
- b) a connected person(s) at the issuer level who (individually or together) can exercise or control the exercise of 10% or more of the voting power at the company's general meeting (Main Board Rule 14A.27).

Connected Transaction (Cont'd)

▶ Options involving connected persons

The grant, acquisition, transfer, exercise or non-exercise of an option involving a listed issuer or its subsidiaries and a connected person is a connected transaction and is classified by reference to the percentage ratios (except the profits ratio) (Main Board Rule 14A.24(2)(a))

The termination of an option is treated in the same way as the transfer or non-exercise of an option, such that the termination should be classified as if the option is exercised, unless the issuer has no discretion over the termination (Main Board Rule 14A.79(4)).

If the group grants an option to a connected person and exercise of the option is **not** at the group's discretion:

- on grant of the option, the transaction is classified as if the option had been exercised – for the purposes of calculating the percentage ratios, consideration includes both the premium and exercise price
- the issuer must announce any exercise or transfer of the option and/or (if the option is not exercised in full) the notification from the option holder that the option will not be exercised or the expiry of the option, whichever is earlier. (Main Board Rule 14A.61 and 14A.79)

Connected Transaction (Cont'd)

▶ Options involving connected persons (Cont'd)

If the group acquires or accepts an option from a connected person, where the option is exercisable at the group's discretion :

- on acquisition by (or grant of the option to) the group, only the premium is taken for the purpose of calculating the percentage ratios. Where the premium represents 10% or more of the sum of the premium and the exercise price, the value of the underlying assets + the revenue attributable to such assets + the premium + the exercise price are used for the purpose of calculating the percentage ratios.
- on exercise of the option by the group, the exercise price + value of the underlying assets + the revenue attributable to such assets are used for the purpose of the percentage ratios.
- non-exercise or termination of the option or transfer of the option to a 3rd party are treated as if the option was exercised. The exercise price + value of the underlying assets + the revenue attributable to such assets + (if applicable) the premium for transferring the option are used for the purpose of calculating the percentage ratios.

(Main Board Rule 14A.70)

CHARLTONS
易周律師行

Connected Transaction (Cont'd)

▶ Options involving connected persons (Cont'd)

The Listing Rules provide an alternative test for classifying transfer, non-exercise or termination of options based on the asset and consideration ratios using the higher of:

- a) i. for a put option held by the listed issuer's group, the exercise price less the value of the assets subject to the option; or
- ii. for a call option held by the listed issuer's group, the value of the assets subject to the option less the exercise price; and
- b) the consideration or amount payable or receivable by the issuer group.

An issuer may adopt the alternative classification test if the value of the option assets is readily ascertainable and the issuer is able to provide:

- a valuation of the option assets prepared by an independent expert using generally acceptable methodologies; and
- a confirmation from the INEDs and an independent financial adviser that the transfer, termination or non-exercise of the option is fair and reasonable and in the interests of the listed issuer and its shareholders as a whole.

If an issuer adopts the alternative method, it must announce the transfer, termination or non-exercise of the option with the views of the INEDs and independent financial adviser.

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ **Joint venture arrangements involving connected persons**

Entering into any agreement or arrangement involving the formation of a joint venture entity in any form, such as a partnership or a company, or any other form of joint arrangement by a listed issuer and a connected person constitutes a connected transaction (Main Board Rule 14A.24(5)).

▶ **Continuing Connected Transactions**

Continuing connected transactions are connected transactions that:

- i. involve the provision of goods, services or financial assistance;
- ii. are carried out on a continuing or recurring basis; and
- iii. are expected to extend over a period of time.

They are usually transactions in a group's ordinary and usual course of business.

Continuing connected transactions are governed by Main Board Rules 14A.50 to 14A.60.

Connected Transaction (Cont'd)

▶ Classification of Connected and Continuing Connected Transactions

Connected and continuing connected transactions fall into 3 categories:

- 1) Non-exempt transactions
- 2) Transactions exempt from the reporting, announcement and independent shareholders' approval requirements (“**wholly exempt**” transactions)
- 3) Transactions exempt from the circular, independent financial advice and independent shareholders' approval requirement only (but subject to the reporting and announcement requirements) (“**partially exempt**” transactions)

Connected Transaction (Cont'd)

▶ Connected Transaction Requirements

Written agreement requirement

The listed issuer must enter into a written agreement with all relevant parties in respect of the connected transaction.

Reporting requirements

The listed issuer's next published annual report and accounts must include the details of the connected transaction specified in Main Board Rule 14A.71:

- the transaction date;
- the transaction parties and a description of their connected relationship;
- a brief description of the transaction and its purpose;
- the total consideration and terms; and
- the nature and extent of the connected person's interest.

Connected Transaction (Cont'd)

▶ Connected Transaction Requirements (Cont'd)

Notification and Announcement requirement

The listed issuer must **notify the Exchange** as soon as possible after the terms of the connected transaction have been agreed upon and **publish an announcement** as soon as possible (Main Board Rule 14A.35).

Independent shareholders' approval requirement

Connected transactions and continuing connected transactions must be approved by the issuer's independent shareholders. Voting on the resolution approving the connected transaction must be **by way of poll**.

Any shareholder who has a material interest in the transaction(s) must **abstain from voting** (Main Board Rule 14A.36).

Connected Transaction (Cont'd)

▶ Connected Transaction Requirements (Cont'd)

Independent board committee and financial adviser requirements (Cont'd)

An **independent board committee** (consisting only of INEDs) must be established to advise shareholders as to:

- whether the terms of the connected transaction are **fair and reasonable**;
- whether the transaction is **in the interests of the listed issuer and the shareholders** as a whole;
- whether the connected transaction is on normal commercial terms and in the issuer's ordinary and usual course of business; and
- how to vote, taking into consideration the views of the independent financial adviser (Main Board Rule 13.39(6)(a)).

An **independent financial adviser** must be appointed to advise the independent board committee and independent shareholders on the matters set out above (Main Board Rule 13.39(6)(b)).

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ **Connected Transaction Requirements (Cont'd)**

Written Independent Shareholders' Approval

Written independent shareholders' approval is acceptable (in lieu of a general meeting) if:

- i. no shareholder would be required to abstain from voting if a general meeting were held; and
- ii. the written independent shareholders' approval is obtained from a shareholder or closely allied group of shareholders who (together) hold >50% of the voting rights in the general meeting to approve the connected transaction. (Main Board Rule 14A.37 and 14A.38)

Shareholders' Circular Requirement

The listed issuer must send a circular to shareholders:

- at the same time as it gives notice of the general meeting to approve the transaction; or
- if the transaction is to be approved by way of written shareholders' approval from a shareholder or closely allied group of shareholders, within 15 business days of publication of the announcement (Main Board Rule 14A.46 and 14A.48).

The shareholders' circular must comply with the contents requirements of Main Board Rules 14A.69 and 14A.70 and must include the letter from the independent board committee and the independent financial adviser's opinion.

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ Continuing Connected Transaction Requirements (Cont'd)

Additional requirements for continuing connected transactions

The written agreement governing the transaction must be on **normal commercial terms** and be for a **fixed period**, usually not exceeding 3 years.

The reporting requirements must be followed for **each subsequent financial year** during which the listed issuer undertakes the continuing connected transaction.

Annual cap requirement for continuing connected transactions

The listed issuer must set a **maximum aggregate annual cap** expressed in **monetary terms**, the basis of which must be disclosed.

The annual cap must be determined by reference to **previous transactions and figures** or be based on **reasonable assumptions** if no previous transaction exists.

If the annual cap is exceeded, or if the relevant agreement is renewed or its terms are changed materially, the listed issuer must re-comply with the reporting, announcement and independent shareholders' approval requirements.

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ Continuing Connected Transaction Requirements (Cont'd)

Annual review requirements for continuing connected transactions

Each year, the listed issuer's INEDs must review the continuing connected transactions and confirm in the annual report and accounts that the transactions have been entered into:

- a) in the **ordinary and usual course of business** of the group;
- b) either on **normal commercial terms** or terms **no less favourable** to the listed issuer than those available to/from independent third parties; and
- c) in accordance with the governing agreement on terms that are fair, reasonable and in the interests of the shareholders as a whole.

Connected Transaction (Cont'd)

▶ Continuing Connected Transaction Requirements (Cont'd)

Annual review requirements for continuing connected transactions (Cont'd)

Each year, the auditors must provide a letter to the board of directors confirming whether anything has come to their attention that causes them to believe that the non-exempt continuing connected transactions:

- a) have not been approved by the issuer's board of directors;
- b) were not, in all material respects, in accordance with the group's pricing policies if the transactions involve the provision of goods or services by the group;
- c) were not entered into, in all material respects, in accordance with the relevant agreement governing the transactions; and
- d) have exceeded the annual cap.

Connected Transaction (Cont'd)

▶ Exemptions from Connected Transaction Requirements

Wholly exempt connected transactions

Connected transactions exempt from the reporting, announcement and independent shareholders' approval requirements include, but are not limited to:

- intra-group transactions
- *de minimis* transactions
- certain issues of new securities
- purchase of own securities
- directors' service contracts
- provision of director's indemnity or purchase of director's insurance
- sharing of administrative services
- buying or selling of consumer goods or services
- transactions with associates of a passive investor
- transactions with a connected person at the subsidiary level

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

Intra-group transactions

Transactions between a listed issuer and a non-wholly owned subsidiary (or between its non-wholly owned subsidiaries) are exempt where:

- a) none of the subsidiaries concerned is itself a connected person; and
- b) no connected persons at the issuer level exercise or control the exercise of 10% or more of the voting power at any general meeting of any of the subsidiaries concerned (Main Board Rule 14A.18).

Transactions are also exempt if they are between the issuer's non-wholly owned subsidiary of which a connected person of the issuer (at the issuer level) controls 10% or more of the voting power at any general meeting and any of its subsidiaries which are connected persons only by virtue of being the subsidiaries of such non-wholly owned subsidiary or where the transaction is between any of these subsidiaries (Main Board Rule 14A.17).

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

De minimis transactions

Transactions on normal commercial terms are wholly exempt where each or all of the percentage ratios except the profits ratio is/are:

- i. less than 0.1%;
- ii. less than 1% and the transaction is a connected transaction only because the connected person is connected by virtue of its relationship(s) with one or more of the listed issuer's subsidiaries; or
- iii. less than 5% and the total consideration is less than HK\$3 million.

This exemption does not apply to the issue of new securities by an issuer to a connected person.

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

Certain issues of new securities

Issues of new securities to a connected person are wholly exempt where:

- a) The connected person receives a pro rata entitlement to securities as a shareholder;
- b) Securities are issued under a Chapter 17 share option scheme or under a share option scheme in existence before the issuer was listed for which approval for listing was granted at the time of listing;
- c) The connected person subscribes for securities in, or acts as underwriter or sub-underwriter for, a rights issue or open offer by the listed issuer, provided that Main Board Rules 7.21 and 7.26A have been complied with; or
- d) Securities are issued under a “top-up placing and subscription” to a connected person within 14 days after such connected person has executed an agreement to reduce its holding in that class of securities by placing securities to a third person who is not its associate. The securities must be issued at a price not less than the placing price. The number of securities issued to a connected person must not exceed the number of securities placed by it (Main Board Rule 14A.92).

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

Purchase of own securities

Share repurchases from a connected person on a recognised stock exchange (unless the connected person knowingly sells shares to the listed issuer) or under a general offer

Directors' service contracts

A director entering into a service contract with the listed issuer or its subsidiary

Sharing of administrative services

Sharing of administrative services between a listed issuer and a connected person on a cost basis, provided that the costs are identifiable and allocated on a fair and equitable basis.

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

Buying or selling consumer goods or services

A **group** buying consumer goods or services as a customer from, or selling consumer goods or services to, a **connected person** on **normal commercial terms** in the **ordinary and usual course of business** is wholly exempt if :

- a) goods or services are of a type ordinarily supplied for private use or consumption;
- b) goods or services are for buyer's own consumption/use and not processed into buyer's products or for resale or used by the buyer for its businesses or contemplated businesses;
- c) they are used/consumed by the buyer in the same state as when they were bought;
- d) the transaction is on no more favourable terms to the connected person, or no less favourable terms to the group, than those available to or from independent third parties.

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

Transactions with associates of a passive investor

A transaction is wholly exempt if it is of a revenue nature in the ordinary and usual course of the listed group's business and on normal commercial terms or better, and involves an associate (the "**Relevant Associate**") of a substantial shareholder of the listed issuer ("**passive investor**") that:

- a) is a sovereign fund, or unit trust or mutual fund authorized by the SFC/appropriate overseas authority;
- b) has a wide spread of investments other than securities of the issuer and the Relevant Associate;
- c) is connected to the issuer only because it is a substantial shareholder;
- d) is not a controlling shareholder of the listed issuer;
- e) does not have any representative on the board of directors of the listed issuer, and is not involved in the management of the listed issuer (including any influence over the listed issuer's management through negative control on material matters); and
- f) is independent of the directors, chief executive, controlling shareholder(s) and any other substantial shareholder(s) of the listed issuer.

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ Wholly Exempt Connected Transactions (cont'd)

Provision of director's indemnity or purchase of director's insurance

The provision of an indemnity to, or the purchase of insurance for, a director of the issuer or its subsidiaries is exempt from the connected transaction rules if:

- the indemnity/insurance is for liabilities that may be incurred in the course of the director performing his duties; and
- the indemnity/insurance is in a form allowed under the laws of Hong Kong, and, where the company providing or purchasing the insurance is incorporated outside Hong Kong, the laws of the company's place of incorporation (Main Board Rules 14A.91 and 14A.96).

Connected Transaction (Cont'd)

▶ Partially Exempt Connected Transactions

De minimis transactions

Connected transactions (other than an issue of new securities by the listed issuer) are exempt from the circular, independent financial advice and independent shareholders' approval requirements (but subject to the reporting and announcement requirements) if:

- i. it is conducted on normal commercial terms or better; and
- ii. each or all of the percentage ratios except the profits ratio is/are:
 - a) less than 5%; or
 - b) less than 25% and the total consideration is less than HK\$10 million.

(Main Board Rule 14A.76(2))

Connected Transaction (Cont'd)

▶ **Partially Exempt Connected Transactions**

Exemption for connected persons at the subsidiary level

Transactions with persons connected **only at the subsidiary level** are exempt from the circular, independent financial advice and shareholders' approval requirement if:

- the transactions are on normal commercial terms or better;
- the transactions are approved by the issuer's board of directors; and
- the issuer's INEDs confirm that the terms of the transactions are fair and reasonable, and they are on normal commercial terms and in the interests of the issuer and its shareholders as a whole (Main Board Rule 14A.101).

Connected Transaction (Cont'd)

▶ Exemptions for Continuing Connected Transactions

Wholly exempt continuing connected transactions

The following exemptions also apply to continuing connected transactions:

- ▶ sharing of administrative services
- ▶ buying or selling consumer goods or services
- ▶ transactions with associates of a passive investor
- ▶ *de minimis* transactions (with the percentage ratios calculated on an annual basis).

Partially exempt continuing connected transactions

Continuing connected transactions on normal commercial terms or better are exempt from the independent shareholders' approval requirement (but subject to the reporting and announcement requirements) where each or all of the percentage ratios except the profits ratio is/are on an annual basis:

- a) less than 5%; or
- b) less than 25% and the annual consideration is less than HK\$10 million.

(Main Board Rule 14A.76(2))

CHARLTONS
易周律师行

Connected Transaction (Cont'd)

▶ Exemptions for Financial Assistance

Wholly exempt financial assistance provided **by** a listed issuer which is **not** a bank

Financial assistance provided by a listed issuer or its subsidiary for the benefit of a connected person in which it is a shareholder or a Commonly Held Entity is fully exempt if it is:

- a) provided on **normal commercial terms** (or better to the group); and
- b) the assistance provided is proportional to the equity interest directly held by the issuer or its subsidiary in the connected person or Commonly Held Entity and any guarantee is given on a several basis (Main Board Rule 14A.89).

Connected Transaction (Cont'd)

▶ Exemptions for Financial Assistance (cont'd)

Wholly exempt financial assistance provided to a listed issuer

Financial assistance provided **to a listed issuer** by a connected person or Commonly Held Entity is wholly exempt if it is provided on normal commercial terms or better to the listed issuer and no security is granted over the listed issuer's assets (Main Board Rule 14A.90).

Connected Transaction (Cont'd)

▶ Exchange's Discretion

In any situation, the Exchange reserves the right to specify that an exemption will not apply to a particular transaction.

The Exchange may also require that any connected transaction be subject to the independent shareholders' approval requirements.

(Main Board Rule 14A.75)

Corporate Governance Requirements (Cont'd)

a) Requirement for Independent Non-Executive Directors (INEDs)

- ▶ A listed issuer must have at least 3 INEDs, at least one of whom must have appropriate professional qualifications or accounting or related financial management expertise (Main Board Rule 3.10). In addition, at least one-third of an issuer's board should be INEDs (Main Board Rule 3.10A).
- ▶ An issuer which fails to comply with any of these requirements must immediately inform the Exchange and publish an announcement and must ensure compliance within 3 months.
- ▶ Independence tests are set out in Main Board Rule 3.13.

Corporate Governance Requirements (Cont'd)

b) Audit Committee

Every listed issuer is required to establish an audit committee comprising non-executive directors only. It must comprise a minimum of 3 members, at least one of whom must be an INED with appropriate professional qualifications or accounting or related financial management expertise.

The majority of audit committee members must be INEDs and it must be chaired by an INED (Main Board Rule 3.21). The duties of the audit committee are set out in Code Provisions under the Corporate Governance Code. Audit committee's terms of reference should be available on the websites of the HKEx and the listed issuer (Code Provision C.3.4).

c) Directors' Service Contracts

Shareholders' prior consent is required before the grant of a service contract to a director of the listed issuer or any of its subsidiaries, if the contract:

- i. may last for 3 years or more; or
- ii. requires the listed issuer to give more than one year's notice or pay the equivalent of more than one year's remuneration on termination (Main Board Rule 13.68)

d) Directors' Remuneration

Fees and any other reimbursement or emolument payable to a director or a past director must be disclosed in full in the annual reports and accounts of an issuer on an individual and named basis.

CHARLTONS
易周律師行

Corporate Governance Requirements (Cont'd)

e) Remuneration Committee

Main Board Rules 3.25-3.27 require:

- i. issuers to establish a remuneration committee with a majority of INED members;
- ii. an INED as chairman of remuneration committee;
- iii. written terms of reference for the remuneration committee; and
- iv. an issuer that fails to comply with these Rules to immediately announce its reasons for not doing so and any other relevant details. The issuer will have a three-month period to rectify its non-compliance.

The Corporate Governance Code allows two different types of remuneration committee. Under the first, the board delegates to the remuneration committee authority to determine the remuneration of executive directors and senior management. Under the second, the board retains that authority, with the remuneration committee taking an advisory role.

The minimum terms of reference for a remuneration committee are set out at Code Provision B.1.2.

Terms of reference of the remuneration committee should be available on the websites of the HKEx and the listed issuer (Code Provision B.1.3).

CHARLTONS
易周律師行

Corporate Governance Requirements (Cont'd)

f) Nomination Committee

- ▶ A listed issuer should establish a nomination committee with a majority of INEDs, chaired by an INED or the board chairman (Code Provision A.5.1).
- ▶ Written terms of reference should include:
 - reviewing the board's structure, size and composition (including the skills, knowledge and experience) at least annually;
 - identifying and recommending potential board members; and
 - assessing the independence of INEDs.
- ▶ Nomination committee's written terms of reference should be available on the websites of the HKEx and the listed issuer (Code Provision A.5.3).

Corporate Governance Requirements (Cont'd)

g) Compliance Adviser

An issuer must appoint a compliance adviser (licensed by the SFC to conduct sponsor work) from the date of listing until the publication date of its financial results for the first full financial year commencing after listing.

An issuer is required to consult and, if necessary, seek advice from its Compliance Adviser in the following situations:

- i. before publication of any regulatory announcement, circular or financial report;
- ii. where a transaction which might be a notifiable or connected transaction is contemplated (including share issues and repurchases);
- iii. where the listed issuer proposes to use the IPO proceeds in a manner different to that set out in the listing document;
- iv. where the business activities, developments or results of the issuer deviate from any forecast, estimate or other information in the listing document; and
- v. where the Exchange makes an inquiry of the issuer under Main Board Rule 13.10.

(Main Board Rule 3A.23)

CHARLTONS
易周律师行

Corporate Governance Requirements (Cont'd)

h) Authorised Representatives

- ▶ Listed issuer must appoint 2 authorised representatives to act as principal channel of communication with Exchange
- ▶ Must be 2 directors or a director and the company secretary
- ▶ Must appoint suitable alternates whenever they are outside Hong Kong and provide Exchange with alternates' contact details
- ▶ Exchange must be given prior notification of an authorised representative's proposed termination of his role and the reasons for it

i) Company Secretary

- ▶ Listed issuer must appoint as its company secretary an individual who, by virtue of his academic or professional qualifications or relevant experience, is, in the Exchange's opinion, capable of discharging functions of company secretary (Main Board Rule 3.28).
- ▶ Acceptable academic or professional qualifications: members of the HK Institute of Chartered Secretaries; solicitors or barristers (under the HK Legal Practitioners Ordinance); and certified public accountants (under the HK Professional Accountants Ordinance).

Corporate Governance Requirements (Cont'd)

i) Company Secretary (Cont'd)

- ▶ In assessing “relevant experience”, Exchange considers length of employment with issuer and other issuers, familiarity with Listing Rules and other relevant laws (including SFO, CO and Takeovers Code), training completed/to be completed and professional qualifications in other jurisdictions.

j) Board Diversity

Board Composition - Code Principle A.3 requires that a board should have a balance of skills, experience and diversity of perspective appropriate to the requirements of the issuer’s business.

Nomination Committee – Code Provision A.5.6 provides that the nomination committee (or the board) should have a policy concerning board diversity and that policy (or a summary) should be included in the issuer’s corporate governance report.

Board diversity will differ according to the circumstances of each issuer. Diversity of board members can be achieved through consideration of a number of factors, including but not limited to gender, age, cultural and educational background, or professional experience. Each issuer should take into account its own business model and specific needs, and disclose the rationale for the factors it uses for this purpose.

CHARLTONS
易周律师行

Corporate Governance Requirements (Cont'd)

k) Website Publication of Certain Documents

The Main Board Rules require certain documents to be published on the websites of the listed issuer and the Exchange. These include:

- ▶ an up to date consolidated version of its constitutional documents must be published on the websites of both the issuer and the Exchange's website (Main Board Rule 13.90); and
- ▶ the procedures for shareholders to propose a person for election as a director must be published on the issuer's website (Main Board Rule 13.51D).

The Corporate Governance Code requires publication on the websites of the issuer and the Exchange of:

- ▶ an up-to-date list of directors identifying their role and function and whether they are INEDs (Code Provision A.3.2); and
- ▶ the terms of reference of the issuer's nomination, remuneration and audit committees explaining their roles and the authority delegated to them by the board (Code Provisions A.5.3, B.1.3 and C.3.4)

Documents published on the issuer's and Exchange websites should be in English and Chinese.

Corporate Governance Requirements (Cont'd)

I) Environmental, Social and Governance (ESG) Reporting

- ▶ Appendix 27 to the Main Board Rules sets out a guide for **ESG reporting**, which is a required practice under Main Board Rule 13.91 and is the **overall responsibility of the board**.
- ▶ Listed issuers must state whether or not they have complied with the “comply or explain” provisions of the ESG Guide. If there is any deviation from any of those provisions, reasons for such deviation must be provided in the ESG report.
- ▶ The ESG Guide sets out 2 key subject areas for reporting: **Environmental** and **Social**. There are several aspects under each area, each with general disclosure requirements and Key Performance Indicators (“**KPIs**”) to measure ESG performance.
- ▶ The ESG Guide is not comprehensive; issuers are encouraged to identify and disclose additional ESG issues and KPIs relevant to their businesses. They may adopt international ESG reporting guidance for their relevant industry or sector if it includes disclosure provisions comparable to the “comply or explain” provisions of the ESG Guide.
- ▶ An ESG report must be included in an issuer’s annual report or in a separate ESG report published in print or on the issuer’s website. The ESG report and annual report must cover the same reporting period.

CHARLTONS
易周律师行

The Code on Corporate Governance Practices

- ▶ The Corporate Governance Code (the “**Code**”) is set out in Appendix 14 of the Listing Rules.
- ▶ Two tiers of recommended practices.
- ▶ The first tier contains the “Code Provisions” which are the minimum standards with which listed companies are expected to comply.
- ▶ Companies must state in their half-year and annual reports whether they have complied with the Code Provisions. If they have chosen to deviate from the Code Provisions, considered reasons for each deviation must be stated.
- ▶ The second tier of recommended practices consists of recommended best practices which listed companies are encouraged to adopt. Listed companies are encouraged, but are **not** required, to include a statement as to compliance with the recommended best practices and considered reasons for any deviations from them in their Corporate Governance Reports.
- ▶ The Code covers 5 principal areas: Directors; Remuneration of Directors and Senior Management; Accountability and Audit; Delegation by the Board and Communication with Shareholders.

The Code on Corporate Governance Practices

Examples of Code Provisions relating to Directors:

- ▶ Full board meetings should be held at least 4 times a year at approximately quarterly intervals;
- ▶ Different people should perform the roles of chairman and chief executive;
- ▶ All directors should be subject to retirement by rotation once every 3 years;
- ▶ The directors should conduct an annual review of the internal controls of the issuer and its subsidiaries;
- ▶ Directors should provide records of training they received to the issuer;
- ▶ Issuers should arrange appropriate insurance cover for directors; and
- ▶ In the circular nominating an INED for election, issuers should include the reasons why the board considers an INED to be independent. Shareholders should vote on a separate resolution to retain an INED who has served on the board for more than nine years.

The Corporate Governance Report

- ▶ Listed issuers are required to include a Corporate Governance Report prepared by the board in their annual reports and any summary financial report.
- ▶ The Corporate Governance Report must include certain mandatory disclosures which are set out at paragraphs G to Q of Appendix 14 to the Listing Rules. Failure to include any of the mandatory disclosures is regarded as a breach of the Listing Rules.
- ▶ Paragraphs R to T of Appendix 14 set out recommended disclosures for Corporate Governance Reports.

The Model Code for Securities Transactions by Directors of Listed Issuers (“Model Code”)

Listed companies are required to adopt rules governing dealings by directors in their listed securities on terms no less stringent than the terms set out in the Model Code in Appendix 10 of the Listing Rules.

Absolute Prohibition

The Model Code prohibits a director of a listed issuer from dealing in its securities:

- a) at any time when he is in possession of inside information in relation to those securities, or where clearance to deal has not been given;
- b) on the publication date of the company’s financial results;
- c) during the 60 days preceding the publication of the annual results or, if shorter, the period from the end of the relevant financial year up to the publication date of the results; and
- d) during the 30 days preceding the publication date of the quarterly or half-year results or, if shorter, the period from the end of the relevant quarter or half-year up to the publication date of the results.

A listed issuer must give advance notice to the Exchange of the commencement date of each blackout period under (c) and (d) above.

CHARLTONS
易周律师行

The Model Code for Securities Transactions by Directors of Listed Issuers (“Model Code”) (Cont’d)

A director of a listed issuer is also prohibited from dealing in the securities of a listed issuer if he is in possession of inside information in relation to those securities by virtue of his position as a director of another listed issuer.

The restrictions on dealings in the Model Code apply equally to dealings by directors’ spouses and children under the age of 18 and to any dealings in which they are deemed to be interested for the purposes of Part XV of the SFO.

Duty of Notification

The Model Code requires listed companies to establish a procedure requiring directors to provide written notification to the chairman or a director designated by the board and receive a dated written acknowledgement before dealing in any securities of the listed issuer.

A response to a request for clearance to deal must be given to the relevant director within 5 business days of the request being made and the clearance must not be valid for more than 5 business days of clearance being received.

The company must maintain a written record of notifications given by directors, acknowledgements of such notifications and written responses given.

CHARLTONS
易周律師行

Disclosure of Interests under Part XV SFO

The directors and chief executive of a listed issuer are required to disclose:

- ▶ their interests and short positions in any shares of the listed issuer or its associated corporations;
- ▶ their interests in any debentures of the listed issuer or its associated corporations; and
- ▶ any change in or cessation of any such interest.

An “**associated corporation**” is defined to include the holding companies and subsidiaries of the listed issuer, subsidiaries of any holding company and any company in which the listed issuer holds more than 20% of any class of its issued shares.

In calculating the number of shares in which a director is interested, he/she must include any interests held by a spouse, children under the age of 18, a company controlled by the director and a trust.

Disclosure of Interests under Part XV SFO (Cont'd)

Directors must also disclose their interests in the underlying shares of equity derivatives.

The term “equity derivative” is defined to include any contract which gives a person rights, options or interests in respect of the underlying shares.

Directors must therefore disclose their interests under any options or warrants giving them rights to acquire shares in the company.

“Short positions”

A person has a **short position** in shares if he:

- ▶ borrows shares under a securities borrowing and lending agreement; or
- ▶ holds or issues a financial instrument under which he has a right to require another person to take the underlying shares or is under an obligation to deliver the underlying shares

Note: Long and short positions must be disclosed separately and cannot be netted off.

Disclosure of Interests under Part XV SFO (Cont'd)

- ▶ On the listing of a company, directors and the chief executive have **10 business days** in which to disclose their interests to the Exchange and the issuer.
- ▶ On listing, notice should be given of:
 - i. an interest in the shares of the listed issuer or an associated corporation;
 - ii. a short position in the shares of the listed issuer or an associated corporation; and
 - iii. an interest in debentures of the listed issuer or an associated corporation.
- ▶ A new director of a listed issuer must give notice of the above interests within **10 business days** of being appointed as a director
- ▶ Directors and the chief executive must make subsequent filings with the Exchange and the issuer of “**relevant events**” including (in relation to shares):
 - i. when he becomes interested in the shares of the listed issuer or an associated corporation (e.g. on the grant to the director of share options);
 - ii. when he ceases to be interested in such shares;
 - iii. when he enters into a contract to sell any such shares;
 - iv. when he assigns any right granted to him by the listed issuer to subscribe for such shares.

CHARLTONS
易周律师行

Disclosure of Interests under Part XV SFO (Cont'd)

- v. when an associated corporation grants a director a right to subscribe for shares in the associated corporation or the director exercises or assigns such rights;
 - vi. when the nature of his interest changes (e.g. on the exercise of an option);
 - vii. when he comes to have, or ceases to have, a short position in the shares of the listed issuer or an associated corporation;
 - viii. if he has an interest, or a short position, in the shares of the listed issuer or an associated corporation, at the time when he becomes a director or chief executive of the listed issuer; and
 - ix. if he has an interest, or a short position, in the shares of an associated corporation, at the time when it becomes an associated corporation.
- ▶ Notice of the relevant events at (i) to (vii) above must be filed with the Exchange and the issuer within 3 business days after the event.
 - ▶ Notice of the relevant events at (viii) and (ix) must be filed within 10 business days after the event.

Disclosure of Interests under Part XV SFO (Cont'd)

- ▶ Failure to make proper and timely disclosure as required by Part XV is a criminal offence which carries a maximum penalty of a fine of HK\$100,000 and imprisonment for up to two years.
- ▶ The listed issuer must keep registers of:
 - the interests and short positions of its substantial shareholders (i.e. holders of 5% or more of any class of voting shares);
 - the interests and short positions of its directors and chief executive in the shares of the listed issuer and its associated corporations;
 - the interests of its directors and chief executive in the debentures of the listed issuer and its associated corporations.
- ▶ Registers must be kept at the registered office or where the shareholders' register is kept.
- ▶ On receipt of a notice in the prescribed form, information must be entered in the register within 3 business days.
- ▶ The interests and short positions of a listed issuer's directors and chief executive in the shares, underlying shares and debentures of the company and its associated corporations must also be disclosed in the company's annual accounts and half-year reports.
- ▶ See also the [SFC's Outline of Part XV of the SFO](#).

CHARLTONS
易周律师行

Insider Dealing

The SFO sets out 6 types of market misconduct which are prohibited in relation to shares listed on the Exchange.

Insider dealing takes place when:

- i. a person who is (a) connected with a listed issuer and having information which he knows is inside information; or (b) contemplating (or has contemplated) making a takeover offer for a listed issuer and who knows that the information that the offer is contemplated (or is no longer contemplated) is inside information in relation to the listed issuer:
 - a. deals, or counsels or procures another to deal, in the company's listed securities or their derivatives or in those of a related corporation (otherwise than for the purpose of the takeover in the case of (b) above); or
 - b. discloses the information knowing or having reasonable cause to believe that the recipient will use the information to deal, or to counsel or procure another person to deal, in the company's listed securities or their derivatives or in those of a related corporation;

Insider Dealing (Cont'd)

- ii. person who has received inside information from a connected person or a person who is contemplating or has contemplated making a takeover offer for a listed issuer either deals, or counsels or procures another person to deal, in the company's listed securities or their derivatives or those of a related corporation; or
- iii. person who has information which he knows is inside information in relation to a listed issuer in any of the circumstances referred in paragraphs (i) and (ii) above:
 - a. counsels or procures another person to deal, knowing or having reasonable cause to believe that the person will deal in the company's listed securities or their derivatives or in those of a related corporation outside Hong Kong on an overseas stock market; or
 - b. discloses the information knowing or having reasonable cause to believe that the recipient will use the information to deal, or to counsel or procure another person to deal, in the company's listed securities or their derivatives or in those of a related corporation outside Hong Kong on an overseas stock market.

Insider Dealing (Cont'd)

Key definitions

The term “securities” is defined widely and includes shares, stocks, debentures, loan stocks, bonds and notes as well as any rights, options or interests in respect of any of the foregoing.

“Persons connected with a corporation” or “connected persons” include the directors (including non-executive directors and shadow directors), employees and substantial shareholders (meaning those holding 5% or more of the issued voting share capital) of the listed issuer and its related corporations. The term also includes persons who have a professional or business relationship with the listed issuer or its related corporation which give them access to inside information.

Insider Dealing (Cont'd)

“Related corporations” of a listed issuer include its subsidiaries and holding companies and other subsidiaries of any holding company of the listed issuer. In addition, where two or more companies are controlled by the same individual, each of those companies and their subsidiaries are regarded as “related corporations” of each other. “Control” means controlling (i) the composition of the company’s board; (ii) more than half of the voting power at general meetings; or (iii) more than half of the company’s issued shares.

“Inside information” in relation to a company means specific information about the company, a shareholder or officer of the company, the listed securities of the company or their derivatives, which is not generally known to the persons who are accustomed or likely to deal in the listed securities of the company but which would, if it were generally known to them, be likely to materially affect the price of the listed securities.

Insider Dealing (Cont'd)

The directors of a listed issuer will be “insiders” for the purposes of these provisions. In practical terms, this means that a director should immediately refrain from dealing or procuring another to deal in the listed securities of his own company once he is aware of, or privy to any negotiations, agreements or information which are or may be price-sensitive until a formal announcement of such information has been made.

Market Misconduct

OTHER TYPES OF MARKET MISCONDUCT

- ▶ False Trading
- ▶ Price rigging
- ▶ Stock Market Manipulation
- ▶ Disclosure of information about prohibited transactions
- ▶ Disclosure of false or misleading information inducing transactions

For further information, please see Charltons' note on Market Misconduct under the SFO.

Market Misconduct (Cont'd)

Dual civil and criminal regimes

The 6 forms of market misconduct may either be prosecuted as a criminal offence under Part XIV of the SFO or made the subject of civil proceedings before the Market Misconduct Tribunal.

Criminal penalties

The maximum criminal penalty for an offence of market misconduct is imprisonment for up to 10 years and/or a fine of up to HK\$10 million.

Market Misconduct (Cont'd)

Market Misconduct Tribunal Proceedings

The Market Misconduct Tribunal may make a number of orders in respect of a person identified as having engaged in market misconduct including a:

- ▶ *Disqualification Order*: an order that the person shall not be involved in the management of any listed corporation or any other specified corporation for a maximum period of 5 years;
- ▶ *Disgorgement Order*: an order that the person pay to the Government an amount up to the amount of any profit gained or loss avoided by the person as a result of the market misconduct.

Market Misconduct (Cont'd)

Civil Liability

A person who has suffered financial loss as a result of market misconduct can bring a civil action against any person who has committed market misconduct if it is fair, just and reasonable in the circumstances.

Liability of officers of a listed issuer

The officers of a listed issuer are required to take reasonable measures to ensure that proper safeguards exist to prevent the company from acting in a way that results in the company perpetrating any conduct which constitutes market misconduct.

If a company commits an act of market misconduct and that occurred with the “consent or connivance” of one of its officers, the officer may be liable to pay damages to any person who suffers financial loss as a result of the market misconduct.

Obligations under the Codes on Takeovers and Mergers and Share Buy-backs

The Code on Takeovers and Mergers (the “**Takeovers Code**”) and the Code on Share Buy-backs apply to takeovers, mergers and share buy-backs affecting public companies in Hong Kong and companies with a primary listing of their shares in Hong Kong.

The primary purpose of the Codes is to ensure that all shareholders affected by takeovers, mergers and share buy-backs of relevant companies are treated fairly. In order to achieve fair treatment, the Codes require equality of treatment of shareholders and disclosure of timely and adequate information to shareholders. The Takeovers Code in particular has the objective of protecting minority shareholders when control of their company changes.

The Takeovers Code is concerned with:

- i. offers for, and takeovers and mergers of, all relevant companies; and
- ii. partial offers, offers by a parent company for shares in its subsidiary and certain other transactions where control (as defined) of a company is to be obtained or consolidated.

The Takeovers Code (Cont'd)

Mandatory Offer Requirements: Rule 26

Except where a waiver has been granted, Rule 26 of the Takeovers Code requires a mandatory offer to be made to all the shareholders of the company in the following circumstances:

- i. when any person (or two or more persons acting in concert) acquires, whether by a series of transactions over a period of time or not, 30% or more of the voting shares of a company; or
- ii. when any person (or two or more persons acting in concert) who holds between 30% and 50% of the voting shares of a company, acquires additional voting shares that increase his or their holding of voting shares by more than 2% from the lowest percentage holding by that person (or the concert group) in the previous 12 month period.

The Takeovers Code (Cont'd)

Mandatory Offer Requirement: Rule 26 (Cont'd)

“Persons acting in concert”

A person will be taken to be acting in concert with an offeror if, pursuant to an agreement or understanding, he is actively co-operating through the acquisition of voting rights, to obtain or consolidate control of the offeree. In the absence of proof to the contrary, certain categories of persons are presumed to be acting in concert with others in the same category.

Offers under Rule 26 must be made in cash (or have a cash alternative) at not less than the highest price paid by the offeror (or any person acting in concert with it) for shares of the offeree in the previous 6 months.

The Takeovers Code (Cont'd)

Requirements of the Takeovers Code

- ▶ any offer of takeover of a listed issuer should be put in the first instance to the board of the listed issuer or its advisers before the offer is announced to the public. The identity of the offeror must also be disclosed. The board of the listed issuer must establish an independent committee of the board to make a recommendation (i) as to whether or not the offer is fair and reasonable and (ii) as to acceptance and voting. The board must also retain an independent financial adviser to advise the independent board committee as to those matters.

The Code on Share Buy-backs

THE CODE ON SHARE BUY-BACKS

The Code on Share Buy-backs applies to share buy-backs of all relevant companies (i.e. Hong Kong public companies and companies with a primary listing of their shares in Hong Kong).

The Share Buy-backs Code distinguishes between 4 types of share buy-backs:

- 1) **On-Market** – this is the most usual method and is normally carried out pursuant to the 10% general mandate normally granted at the AGM.
- 2) **Off-Market** – Off-market share buy-backs must be approved by the Executive Director of the Corporate Finance Division of the SFC under Rule 2 of the Share Buy-backs Code. Approval is normally conditional on the approval of at least 75% of the votes cast by “disinterested shareholders”.
- 3) **Exempt** – includes an employee share buy-back; a share buy-back made in accordance with the terms attached to the shares; and a share buy-back that is required by the law of the jurisdiction in which the offeror is incorporated or established.
- 4) **By General Offer** – this usually takes the form of a tender offer of a certain percentage of all shareholders’ holdings. A share buy-back by General Offer requires approval by at least 50% of shareholders in general meeting. A shareholder with a material interest in the share buy-back will not be allowed to vote. If the buy-back will result in privatisation or de-listing of the issuer, the approval of 75% of shareholders is required.

CHARLTONS
易周律师行

The Code on Share Buy-backs (Cont'd)

On-market buy-backs

Main Board Rules 10.5 and 10.6 set out the relevant requirements in relation to on-market buy-backs. An issuer whose primary listing is on the Exchange may only purchase shares on the Exchange in the following circumstances:

- ▶ the shares proposed to be repurchased are fully-paid up;
- ▶ an Explanatory Statement complying with the detailed contents requirements of Main Board Rule 10.06(1)(b) is issued to the shareholders; and
- ▶ its shareholders have given specific approval or a general mandate to make the buy-back(s) by way of an ordinary resolution passed at a general meeting of the issuer duly convened.

The Code on Share Buy-backs (Cont'd)

The Explanatory Statement must contain all information reasonably necessary to enable the shareholders to make an informed decision on whether to vote for or against the ordinary resolution to approve the share buy-back. Such information includes, in summary, the following :

- ▶ total number and description of the shares to be repurchased, and reasons for the buy-back;
- ▶ the proposed source of funds for making the proposed buy-back;
- ▶ any directors or any close associates of the directors who have an intention to sell shares to the issuer, or an appropriate negative statement;
- ▶ consequences arising under the Takeovers Code of which the directors are aware, if any;
- ▶ details of any purchases by the issuer of shares made in the previous 6 months (whether on the Exchange or not);
- ▶ whether or not any core connected persons of the issuer have notified the issuer that they have an intention to sell their shares to the issuer; and
- ▶ the highest and lowest prices at which the relevant shares have traded on the Exchange during each of the previous 12 months.

The Code on Share Buy-backs (Cont'd)

Dealing restrictions for on-market buy-back

On-market buy-backs are subject to the following dealing restrictions:

- ▶ no shares may be repurchased if the purchase price is higher by 5% or more than the average closing market price for the 5 preceding trading days;
- ▶ shares cannot be repurchased for non-cash consideration;
- ▶ the issuer must not knowingly purchase its shares from a core connected person;
- ▶ the issuer must not repurchase its shares at any time after inside information has come to its knowledge until the information is made public. In particular, buy-backs are not allowed during the period of one month immediately preceding the earlier of:
 - i. the date of the board meeting to approve the annual or interim financial results; and
 - ii. the deadline for publishing any such results under the Listing Rules,and ending on the date of the results announcement; and
- ▶ no shares may be repurchased if that purchase will result in the number of listed shares held by the public falling below the prescribed minimum percentage.

CHARLTONS
易周律师行

The Code on Share Buy-backs (Cont'd)

Off-market buy-backs

Off-market buy-backs must be approved by the SFC before a repurchasing company acquires any shares. Such approval will normally be conditional upon:

- ▶ approval given by at least 75% of votes cast on a poll by disinterested shareholders in attendance in person or by proxy at a general meeting of the issuer;
- ▶ notice of the shareholders' meeting being accompanied by a circular containing:
 - i. details of the proposed offeree(s);
 - ii. terms and conditions of the agreement between the issuer and the proposed offeree(s); and
 - iii. advice of an independent financial adviser and the recommendation of an independent committee of the board in relation to the off-market share buy-back
- ▶ certified copy of the shareholders' resolution approving the share buy-back filed with the SFC within three days of the general meeting; and
- ▶ a copy of the agreement(s) for the off-market share buy-back being available for inspection by the shareholders

CHARLTONS
易周律师行

The Code on Share Buy-backs (Cont'd)

Buy-back by general offer

A share buy-back by general offer must be approved by a majority of the votes cast by independent shareholders in attendance in person or by proxy at general meeting.

If the share buy-back will result in the delisting and privatisation of the issuer :

- ▶ the directors of the offeror and any persons acting in concert will not be considered to be independent and therefore may not vote at the general meeting; and
- ▶ the share buy-back must be approved by at least 75% of votes attaching to the shares owned by independent shareholders cast in person or by proxy and the number of votes cast against the resolution must not be more than 10% of the votes attaching to the shares owned by independent shareholders.

The Code on Share Buy-backs (Cont'd)

Reporting requirements for repurchases

The issuer must:

- ▶ file a return with the Exchange on the next business day following a share repurchase (on or off Exchange) showing the number of shares repurchased, the purchase price paid per share (or the lowest and highest prices paid); and
- ▶ include in its annual report and accounts a monthly breakdown of purchases of shares made during the financial year under review showing the number of shares purchased each month, the purchase price paid per share (or the lowest and highest prices paid) and the aggregate price paid.

Status of purchased shares

- ▶ The listing of the repurchased shares will be automatically cancelled upon purchase and the issuer must apply for listing of any further issues of that type of shares.
- ▶ The issuer must ensure that the documents of title of the repurchased shares are cancelled and destroyed as soon as reasonably practicable.

The Code on Share Buy-backs (Cont'd)

Restriction on new issue of shares following share repurchase

- ▶ Issuers with a primary listing on the Exchange cannot issue new shares (or announce a proposed new issue) in the 30 days after a share repurchase (on or off Exchange), without prior Exchange approval.

Takeovers Implications of Share Repurchases

- ▶ Under Rule 32.1 of the Takeovers Code, a share buy-back is considered to be an acquisition by shareholders whose shares are not repurchased. This is because their percentage holding of shares increases even though the actual number of shares held does not.
- ▶ A shareholder who acquires/consolidates control as a result of a company's share buy-back will not normally incur an obligation to make a mandatory general offer unless the shareholder is a director or acting in concert with a director (Note 2 to Rule 32 Takeovers Code).

Disclaimer

Disclaimer

This presentation contains a summary only of certain Listing Rule and other regulatory requirements. It is intended for information and educational purposes only and should not be treated as a substitute for legal advice.

CHARLTONS
易周律师行

Contact us

Hong Kong Office

12th Floor
Dominion Centre
43 – 59 Queen's Road East
Hong Kong

Telephone: (852) 2905 7888
Fax: (852) 2854 9596
Email: enquiries@charltonslaw.com
Website: <http://www.charltonslaw.com>



CHARLTONS
易周律師行

Other Locations

China

Beijing Representative Office

3-1703, Vantone Centre
A6# Chaowai Avenue
Chaoyang District
Beijing
People's Republic of China
100020

Telephone: (86) 10 5907 3299
Facsimile: (86) 10 5907 3299
enquiries.beijing@charltonslaw.com

Myanmar

Yangon Office of Charltons Legal Consulting Ltd

161, 50th Street
Yangon
Myanmar
enquiries.myanmar@charltonslaw.com

Shanghai Representative Office

Room 2006, 20th Floor
Fortune Times
1438 North Shanxi Road
Shanghai
People's Republic of China
200060

Telephone: (86) 21 6277 9899
Facsimile: (86) 21 6277 7899
enquiries.shanghai@charltonslaw.com

In association with:



Networked with:



CHARLTONS
易周律師行