
LISTING PRC COMPANIES ON THE HONG KONG STOCK EXCHANGE

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I. INTRODUCTION

1. General

With the rapid development and further opening up of the Chinese economy, listing on overseas stock exchanges became an important means for PRC companies to access international funds. Since the first listings of Chinese companies' shares on the Hong Kong Stock Exchange (Exchange) in the 1980s and 1990s, the Exchange has become the overseas listing venue of choice for PRC companies.

Historically, there have been two routes for PRC companies to list on the Exchange: directly by way of an H share listing or indirectly via a "red chip" listing.

H share companies are joint stock limited companies incorporated in the PRC which have received approval from the China Securities Regulatory Commission ("CSRC") to list in Hong Kong. They are different from so-called red chip companies which are incorporated outside the PRC (usually in Hong Kong, the Cayman Islands or Bermuda), are controlled by PRC entities or individuals and conduct most of their business in the PRC.

For the purposes of quoting statistics, the Exchange uses the term "red chip" to refer to companies incorporated outside the PRC which are controlled by PRC government entities. It uses the term Non-H Share Mainland Private Enterprises to refer to companies incorporated outside the PRC which are controlled by PRC individuals.

To give some indication of the significance of China as a source of IPOs for the Exchange, there were 1,924 listed companies on the Exchange at the end of July 2016. Among them, 980 (or 51%) were Mainland enterprises, including 233 H-share companies, 152 red-chip companies and 595 Mainland private enterprises. Together, Mainland enterprises accounted for 62.6% of the market capitalization and 69.9% of the equity turnover of listings on the Exchange at the end of July 2016.

The Exchange is the world's 8th largest stock exchange in terms of market capitalization, and the fourth largest in Asia after Japan, Shanghai and Shenzhen. In terms of IPO funds raised, however, Hong Kong ranked first among the world's exchanges in 2015, continuing a trend that has placed it in the world's top five for the past 14 years.

There were a total of 138 new listings in 2015, raising HKD 261.3 billion, an increase of 12% from 2014.

There were 63 new listings on the Exchange in the first seven months of 2016, down from 69 in the same period last year.

2. Benefits of Listing

There are many reasons for listing on the Exchange, but specifically in relation to Chinese companies, the following reasons should be borne in mind:

- access to international funds: Hong Kong is a regional and international financial centre, and a base for some of the world's most successful fund managers;
- active post-listing trading which facilitates subsequent fund-raising. This is attributable to an active interest in, and more in-depth understanding of, the China market due to geographical and cultural proximity, a high concentration of

analysts focused on China and the existence of a separate Hang Seng Chinese Enterprise Index;

- securing the interest and confidence of international investors who are familiar with the standards of regulation in Hong Kong;
- enhanced profile and reputation through participation in an international financial centre located in the financial hub of the Asia Pacific region; and
- positive pressure on the management of Chinese issuers to appreciate and follow international standards in terms of transparency and protection of minority shareholders.

3. Shanghai-Hong Kong Stock Connect

The Shanghai-Hong Kong Stock Connect pilot programme was launched in November 2014, allowing certain Mainland Chinese investors to invest directly in Hong Kong listed stocks for the first time. Under the Southbound Trading Link, Mainland investors can trade in the constituent stocks of the Hang Seng Composite LargeCap and MidCap Indexes, and all H-shares with corresponding A shares listed on the Shanghai Stock Exchange.

4. Main Board vs GEM Market

The Exchange has 2 boards – the Main Board and the Growth Enterprise Market or GEM. The Main Board caters for more established companies that are able to meet its profit or other financial requirements. GEM has lower entry criteria and acts as a stepping stone to Main Board listing: there is a streamlined process for GEM listed companies to transfer to the Main Board once they are able to meet the Main Board eligibility criteria.

The post-listing obligations of GEM companies are now broadly similar to those of Main Board listed companies. The principal difference in the ongoing obligations of Main Board and GEM companies is that quarterly reporting is a Listing Rule requirement for GEM companies, whilst for Main Board issuers it is still a Recommended Best Practice only (under the Corporate Governance Code).

5. Applicable Hong Kong Laws and Non-statutory Codes

An issuer listing in Hong Kong will be subject to the Rules Governing the Listing of Securities on The Exchange of Hong Kong Limited (the "Listing Rules"), the Companies Ordinance, the Companies (Winding-Up and Miscellaneous Provisions) Ordinance, the Securities and Futures Ordinance; and the Code on Takeovers and Mergers and the Code on Share Buy-backs.

The Listing Rules are as applicable to Chinese issuers as they are to Hong Kong and overseas incorporated issuers. However, in view of the existence of two separate markets (domestic and foreign) for the securities of Chinese issuers, and the differences between the Chinese and Hong Kong legal systems, some additional requirements, modifications and exceptions are set out in Chapter 19A of the Main Board Listing Rules and in Chapter 25 of the GEM Listing Rules, specifically designed for Chinese incorporated issuers (i.e. H share issuers). H shares can be subscribed for and traded in other currencies in addition to Hong Kong dollars.

Red chip companies and non-H share Mainland private enterprises, on the other hand, as companies incorporated outside the PRC, are required to meet the additional requirements of Chapter 19 of the Main Board Rules (Chapter 24 of the GEM Rules) for overseas companies, assuming that they are not incorporated in Hong Kong.

Hong Kong Sponsor Due Diligence Guidelines

In 2013, Charltons led a group of 20 leading Hong Kong corporate law firms and 40 investment banks in the production of the Hong Kong Sponsor Due Diligence Guidelines. The Guidelines provide practical guidance on the due diligence that needs to be conducted on companies listing on the Hong Kong Stock Exchange in order to comply with requirements that came into effect on 1 October 2013.

The Guidelines contain 3 main sections:

- 1) Standards – these are statements of sponsors’ due diligence obligations under Hong Kong’s regulatory regime;
- 2) Guidance - guidance as to the market’s interpretation of the Standards; and
- 3) Recommended Steps - these set out practical steps which would generally be expected to meet the Standards in a typical case.

The Guidelines provide a comprehensive handbook for companies considering a Hong Kong listing and the professional parties involved – sponsors, lawyers, accountants etc. The guidelines incorporate all relevant regulatory standards and guidance from the Hong Kong regulators as well as industry guidance.

The English version of the Due Diligence Guidelines was published in September 2013 and is available free online at <http://duediligenceguidelines.com>. The Chinese version of the Guidelines is also available free online at <http://duediligenceguidelines.com/zh-hant/>.

6. PRC Regulatory Requirements for H Share Issuers

The China Securities Regulatory Commission (**CSRC**) is the regulatory authority responsible for authorizing all overseas listings by PRC incorporated companies.¹

The CSRC Guidelines

The CSRC’s “Guidelines for Supervising the Application Documents and Examination Procedures for the Overseas Stock Issuance and Listing of Joint Stock Companies” (the “**Guidelines**”) came into effect on 1 January 2013. These removed the financial requirements for PRC companies seeking to list overseas in the form of joint stock companies (i.e. H share companies). Previously, Chinese joint stock companies seeking an offshore listing were required to:

- (i) have RMB 400 million of net assets,
- (ii) raise US50 million of funds and
- (iii) have after-tax profit of more than RMB 60 million in the preceding year (the “4-5-6 Requirements”).

¹ Securities Law (Article 10) and the Special Provisions of the State Council on Issuing and Listing of Shares Abroad by Companies Limited by Shares (Article 5)

Under the Guidelines, the 4-5-6 Requirements were replaced by a requirement that Chinese joint stock companies seeking an overseas listing must satisfy the CSRC that they meet the listing requirements of the overseas stock exchange.

The 4-5-6 Requirements had previously meant that the H share companies listing in Hong Kong were mainly large state-owned enterprises, since small and medium sized private companies (“SMEs”) found it difficult to satisfy the rules. The Guidelines provided Chinese SMEs with an alternative to a domestic IPO.

The Guidelines also simplified the application process for PRC companies seeking to list overseas. Before they came into force, potential overseas issuers were required to submit to the CSRC all relevant corporate documents for approval 3 months before the submission of the listing application to the overseas exchange (e.g. the submission of A1 form to the Hong Kong Exchange). Under the Guidelines, this requirement was removed.

The Guidelines aimed to ease fundraising pressure on stock markets in the PRC and promote the development of small and medium companies in the PRC.

7. Conversion of B shares to H shares

In December 2012, China International Marine Containers Group became the first PRC B share company to convert its B-share listing into an H-share listing on the Exchange by way of introduction following approval by the CSRC and the Exchange.

Listing by way of introduction

Listing by introduction is a means of listing shares already in issue on another stock exchange where no marketing arrangements are required because the shares are already widely held. As only existing shares are listed by introduction, no additional funds are raised.

Listing Rule 7.15 states that an introduction will only be permitted in exceptional circumstances if there has been a marketing of the securities in Hong Kong within the six months prior to the proposed introduction where such marketing was made conditional on listing being granted for those securities. Furthermore, there may be other factors, such as a pre-existing intention to dispose of securities, a likelihood of significant public demand for the securities or an intended change of the issuer’s circumstances, which would render an introduction unacceptable to the Exchange. An introduction will not be permitted if a change in the nature of the business is contemplated.

There are problems which may hinder B shares conversion to H shares due to regulatory differences such as differences in accounting systems and financial reporting and requirements of independent non-executive directors (“INEDs”).

Exchange Guidance Letter GL53-13 provides guidance to issuers seeking to list by way of introduction on arrangements to facilitate liquidity of issuers’ securities to meet demand on the Hong Kong market during the initial period after listing.

Listing decision HKEx-LD52-2013 provides a detailed explanation for the Exchange’s decision to allow an un-named company listed on a PRC stock exchange to convert its entire B shares into H shares to be listed on the Exchange by way of introduction.

8. Regulation of Red Chip Listings

Circular 10 – the M&A Rules

In the past, the reorganisation and PRC regulatory approval process for red-chip listings was more straightforward than that for H-share listings. However, that changed with the issue of the Provisions on the Takeover of Domestic Enterprises by Foreign Investors (the “M&A Rules” or “Circular 10”), which came into effect in September 2006.

Issued by the Ministry of Commerce (“MOFCOM”), with six other governmental departments, the M&A Rules represented a significant step in the development of China’s regulation of foreign acquisitions of Chinese companies. The requirements imposed had significant consequences both for round-trip investments and red-chip listings. Since the M&A Rules came into force, there have been virtually no approvals for restructurings of Chinese companies into offshore holding companies.

In a red-chip listing of a PRC domestic company, the PRC shareholders would set up an offshore holding company typically in the Cayman Islands or Bermuda. The offshore company would then purchase the PRC company which would become its wholly owned subsidiary.

The use of an offshore SPV to achieve an offshore listing of a Chinese company is effectively prevented by the M&A Rules, since MOFCOM approval at the central government level is required for:

- the establishment of an offshore SPV for the purpose of achieving an overseas listing where the offshore company is directly or indirectly controlled by a Chinese company or Chinese individuals; and
- the acquisition by the offshore SPV of the affiliated Chinese company.

The M&A Rules additionally require CSRC approval for the listing of an SPV holding China assets on an overseas stock exchange.

The M&A Rules impose an obligation on the parties to an acquisition to declare whether they are affiliated. If two parties to a transaction are under common control, the identities of the ultimate controlling parties must be disclosed to the approving authorities, together with an explanation of the purpose of the M&A transaction and a statement as to whether the appraised value represents fair market value. The use of trusts or other arrangements to avoid this requirement is expressly prohibited (Article 15).

A further hurdle to a red chip listing is that the M&A Rules provide that the listing price of the SPV’s shares on the overseas exchange may not be less than the valuation of the onshore equity interest as determined by a PRC asset valuation company.

There is also a requirement that the proceeds of the offshore listing, as well as dividends and the proceeds of changes in the capital of Chinese shareholders must be repatriated to China within 180 days / 6 months.

Circular 10 did not however put a stop to offshore financings and listings of Chinese companies. The number of both has remained high, although many such deals involved companies that were restructured prior to Circular 10’s effective date. Other Chinese businesses have been listed using different re-organisation structures to take

them outside the ambit of Circular 10. Chief among these has been the variable interest entity (“VIE”) structure.

In 2012, China Zhongsheng Resources Holdings Limited (2623.hk), originally a PRC company, transformed itself into a Sino-foreign enterprise and then a wholly foreign-owned enterprise and successfully listed in Hong Kong. The company only commenced the red-chip restructuring in 2010 after the implementation date of Circular 10. At various stages of the restructuring, approvals of the provincial bureau of commerce were granted. The company’s successful listing is seen as a circumvention of the regulations prohibiting red-chip listing. It remains to be seen whether the listing resulted from a change in MOFCOM’s policy towards red-chip listing, or merely an exception based on the company’s particular facts and circumstances.

9. VIE structures

Alternative structures have been used to address the challenges to round trip investments posed by Circular 10 and Circular 75. Many of these have involved variations on the VIE structure.

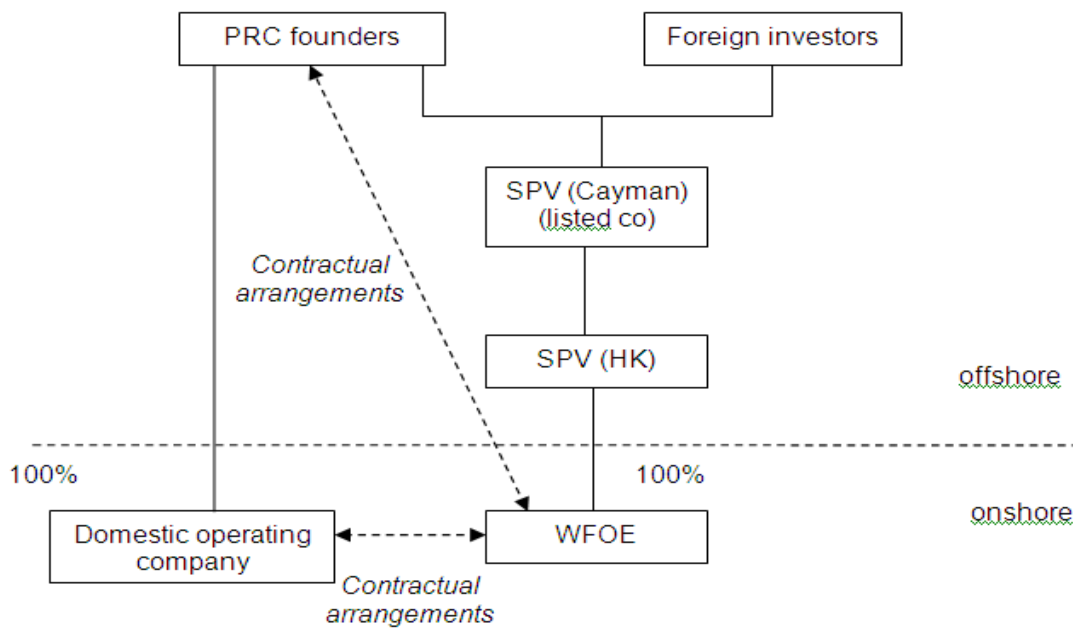
VIE structures are used to obtain an overseas listing of PRC businesses which operate in industries subject to restrictions on foreign investment under PRC law (“**restricted businesses**”) (e.g. internet content provision, media, telecom). Under a VIE structure, all relevant licences and permits for operating the restricted business are held by PRC operating companies (**OPCOs**) which are wholly owned by PRC shareholders, and the foreign investors control and obtain economic benefits from the OPCO through a series of agreements referred to as “contractual arrangements” or structured contracts.

In a typical VIE structure, the PRC shareholder(s) establish an offshore SPV (usually incorporated in Bermuda or the Cayman Islands) which will normally become the listed company. The offshore SPV will establish a subsidiary in the PRC which will be a wholly foreign-owned enterprise (“**WFOE**”). The WFOE will enter into contractual arrangements with the OPCOs and their PRC shareholders which give it control over the OPCOs and enable the listed company to consolidate their financial results in the group’s financial statements.

The VIE structure was first adopted by Sina in its 2000 listing on Nasdaq, followed by a number of leading internet or media companies listed overseas, including Sohu, Netease, Baidu, Focus Media, Youku and Dangdang (all listed on Nasdaq or NYSE) and Tencent and Alibaba (both listed on the Exchange, although Alibaba subsequently delisted).

Over the years, the VIE structure was never officially or publicly blessed by the PRC authorities, although it was generally regarded as a structure established to intentionally circumvent the restrictions on foreign investment. In the past, however, it was at least acquiesced by the Chinese regulatory authorities.

A typical VIE structure is illustrated in the following diagram:



Typical contents of contractual arrangements between domestic company and the WFOE

Control over the OPCO is exercised through a series of contractual arrangements between (1) the PRC shareholder(s) and the WFOE; and (2) the OPCOs and the WFOE.

These contractual arrangements will normally include:

- (a) Exclusive service agreement;
- (b) Call option agreement;
- (c) Equity pledge agreement;
- (d) Loan Agreement; and
- (e) Voting right agreement or power of attorney.

Exclusive Service Agreement

The exclusive service agreement is entered into between the WFOE and the OPCO pursuant to which the WFOE provides exclusive consulting, management or technology support services to the OPCOs for a fee for the purpose of shifting the profits of the OPCOs to the WFOE.

Call Option Agreement

The call option agreement is entered into between the WFOE and the PRC shareholder pursuant to which the WFOE is granted the option to acquire or designate a third party to acquire, all or a portion of the equity interest in the OPCO at the lowest permitted price under the applicable PRC laws and regulations.

Equity Pledge Agreement

The equity pledge agreement is entered into between the WFOE and the PRC shareholder, pursuant to which the PRC shareholder pledges all its equity interests in the OPCOs in favour of the WFOE to secure the due performance by the OPCOs of their obligations under the contractual arrangements. The equity pledge agreement is

required to be registered with the local Administration of Industry and Commerce to perfect the security interest.

Loan Agreement

The loan agreement is entered into between the WFOE and the PRC shareholder, pursuant to which the WFOE grants a loan to the PRC shareholder for the purpose of capitalising the OPCOs.

Voting Rights Agreement or Power of Attorney

The voting rights agreement or power of attorney is entered into between the WFOE and the PRC shareholder pursuant to which the PRC shareholder irrevocably grants the WFOE all its shareholder rights, including voting rights.

Risks involved

However, just because VIE structures have been widely used does not mean they are legally risk-free. The continued existence of VIE structures very much depends on the “policy-winds” among government officials.

The risks associated with use of the VIE structure essentially fall into two categories: (i) the regulatory risk that the structure might be declared to be invalid by the PRC authorities; and (ii) the risk that the contractual arrangements on which it relies will be unenforceable or insufficient to retain control over the OPCO. With regard to both these issues, comfort needs to be sought from the PRC legal advisers.

The principal regulatory risk probably arises where the OPCO operates in a sector which is subject to restrictions on foreign investment. Although the foreign investor does not directly own equity in the OPCO, there is the possibility that the Chinese regulatory authorities could regard it as *de facto* foreign investment. Failure to obtain the required foreign investment approvals could lead to the Chinese authorities requiring the structure to be unwound. Another risk is that VIE structures could be declared to be subject to the requirement for MOFCOM approval under the M&A Rules.

Use of the VIE structure to facilitate foreign investment in areas subject to restrictions on such investment has however been common for a number of years and many of China’s best known companies have used the structure to obtain foreign venture capital financing and list offshore.

There have been attempts by individual PRC regulators to restrict or curtail the use of the structure in specific industries or to circumscribe its use in the past. For example, in relation to value added telecommunications businesses, a circular issued by the PRC Ministry of Information Industry in 2006, requires certain key assets, including trademarks and domain names, to be held by the company with the value added telecommunications service provider licence or its shareholders. As a result, in a VIE structure, the OPCO needs to hold key assets and cannot lease or license them from the WFOE. Although this increases the potential loss suffered by the WFOE if it loses control of the OPCO, the circular can also be regarded as acknowledging the use of the VIE structure in the value added telecommunications industry.

Another example is the notice of general administration of press and publication issued in 2009 - targeting the online gaming business. Under the notice, foreign investors are not allowed to control or participate in a domestic online gaming business by setting up

a joint venture company, through contractual arrangements, or providing technical support.

In September 2011, the measures on the security review system of mergers and acquisitions of Chinese enterprise by foreign investors were issued. These require MOFCOM approval for foreign investment in industries deemed sensitive to China's national security interests. The measures specifically prohibit foreign investors from adopting indirect or contractual arrangements so as to avoid the national security review requirements. This is considered to take aim specifically at VIE structures.

A potential risk is that a VIE structure will be declared invalid on public policy grounds. Buddha Steel, a small steel maker, applied for listing in the United States through a VIE structure. In March 2011, it was advised by the local government authorities of Hebei Province that the VIE contractual arrangements contravened existing Chinese management policies relating to foreign invested enterprises and as a result, were against public policy. Buddha Steel terminated the VIE contracts and withdrew its listing application.

Buddha Steel has not however been viewed as an indication of Chinese authorities' disapproval of the VIE structure. Rather, it has been seen as the regulatory authorities tightening control on foreign investment in certain core and important industries, including the steel production industry.

China's Draft Foreign Investment Law

Since the PRC Ministry of Commerce published a consultation draft of a new Foreign Investment Law (the "FIL") in January 2015, there have been increased concern over the legality and validity of the structured contracts used in VIE arrangements. The key changes in relation to VIEs proposed by the Draft FIL are that:

- the legal validity of VIE structures will be recognised;
- a VIE structure controlled by a foreign investor will have to comply with restrictions on investment in "restricted" and "prohibited" industries.

Control is defined in Article 18 of the draft FIL as:

- (a) holding (directly or indirectly) more than 50% of the shares, voting rights or similar equity interests;
- (b) having the right or ability to appoint or nominate at least half of the board of directors (or of a similar governance body);
- (c) having the ability to exercise a major influence on shareholders' or directors' decisions; or
- (d) having the ability to have a decisive influence over an entity's operations, finances, human resources or technology through contract, trust or other arrangements (contractual control).

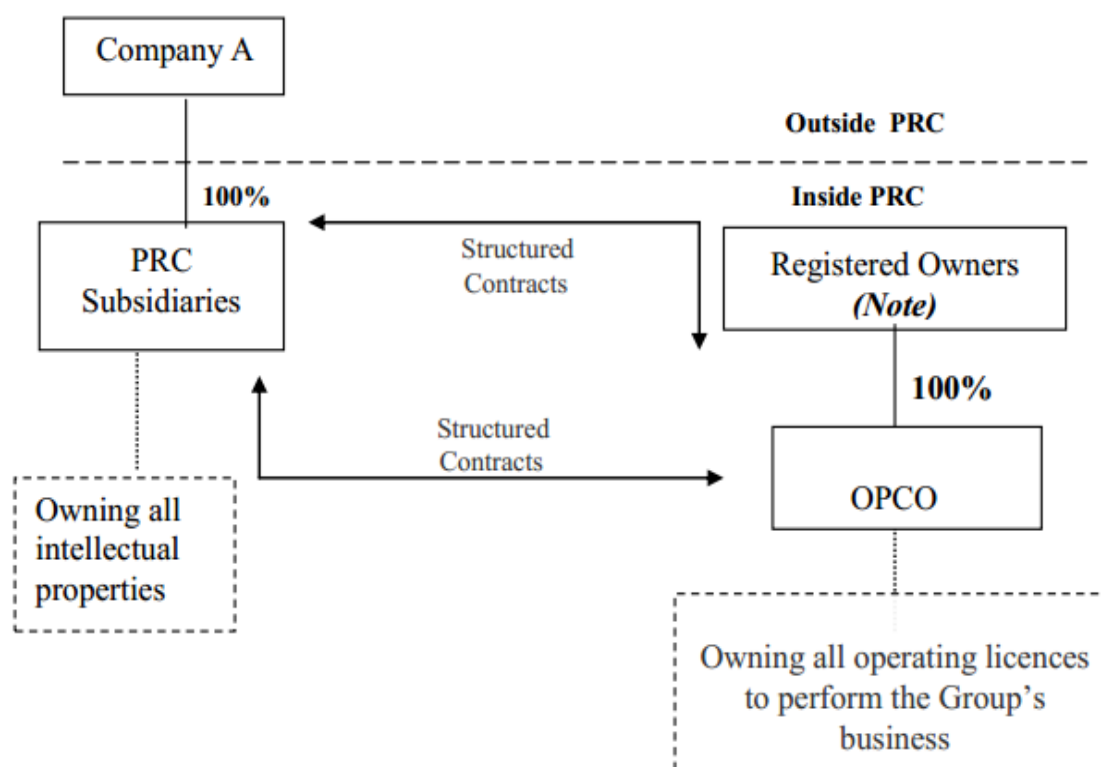
The Exchange thus now requires PRC companies that use VIE structures to list on the Exchange to demonstrate that they are (and will continue to be) “controlled” by PRC nationals.

When the draft FIL was published for consultation, it was thought that it would be implemented in the relatively near future. However, consultation conclusions have not been published since the draft FIL was published in January 2015. Many PRC lawyers now believe that it is unlikely that the new FIL will be implemented in the near future in its present form. Moreover, it’s generally expected that if it is finally implemented, there will be some form of grandfathering provision to either exempt currently listed VIE structures or allow a grace period for them to amend their structure to comply with the new requirements. Nevertheless, the Exchange’s current policy requires Chinese VIE structures to be controlled by PRC nationals on the date of listing.

Given the provisions of the draft FIL, the Exchange requires the controlling shareholders of a listed issuer using a VIE structure to give undertakings to the listed issuer that they will:

- hold or control at least 50% of the voting rights in the listed issuer’s share capital;
- maintain his/her PRC nationality; and
- procure that any arrangement in support of maintaining the holding or control of at least 50% of the listed issuer’s share capital would only be terminated when the listed issuer’s shares cease to be listed on the Exchange.

10. Exchange’s Approach to Listing VIE Structures: Listing Decision 43-3



The Registered Owners were controlling shareholders of Company A

The Exchange's approach to the listing of applicants using VIE structures is set out in its Listing Decision 43-3 which was first issued in 2005. It has been updated a number of times. The Exchange generally allows listing applicants using a VIE structure (also known as "Contractual Arrangements" or "Structured Contracts") to list provided that it is satisfied as to the reasons for adopting the structure and the listing applicant meets the requirements set out in that Listing Decision. VIE structures are normally only accepted for listing where they are used for restricted businesses. Where a VIE structure is used for an unrestricted business, the Listing Division will normally refer the case to the Listing Committee.

Under the disclosure-based approach, the Exchange will not consider an applicant using a VIE structure to be unsuitable for listing if it has complied with all relevant PRC laws and regulations. The listing decision requires appropriate regulatory assurance to be obtained from the relevant regulatory authorities. In the absence of such regulatory assurance, the applicant's PRC legal counsel must include a statement in its legal opinion to the effect that all possible actions or steps taken to enable it to reach its legal conclusions have been taken.

The PRC legal opinion must also confirm that the structured contracts would not be deemed as "concealing illegal intentions with a lawful form" and thus void under PRC contract law.² This requirement was added in November 2013 following a ruling by China's Supreme Court in October 2012 that arrangements which sought to give control to Chinachem Financial Services, a Hong Kong company, over a shareholding stake in China Minsheng Banking Corporation, were invalid. The court found that the arrangements had been entered into with the intention of circumventing restrictions under PRC law on foreign investment in China's banking sector and were thus invalid and unenforceable since they "concealed illegal intentions with a lawful form". Some commentators have argued that the case undermines the viability of the VIE structure. However, the issues in the Chinachem decision were different to those arising in a typical VIE structure. For example, the case was concerned with the validity of entrustment arrangements which are not normally used in a VIE structure.

Listing applicants which adopt a VIE structure for restricted businesses are required to demonstrate that they have taken all reasonable steps to comply with all applicable PRC rules (other than the restriction on foreign ownership).

Where PRC laws and regulations specifically prohibit foreign investors from using agreements or contractual arrangements to gain control of or operate a foreign restricted business (e.g. on-line gaming business which is subject to GAPP's notice 13³), the PRC legal opinion on the structured contracts must:

- a) include a positive confirmation:
 - (i) that the use of the structured contracts does not constitute a breach of those laws and regulations; or
 - (ii) that the structured contracts will not be deemed invalid or ineffective under those laws and regulations; and

² Paragraph 19(k) of Listing Decision HKEx-LD43-3.

³ "Notice Regarding the Consistent Implementation of the 'Stipulations on "Three Provisions"' of the State Council and the Relevant Interpretations of the State Commission Office for Public Sector Reform and the Further Strengthening of the Administration of Pre-examination and Approval of Internet Games and the Examination and Approval of Imported Internet Games" (Xin Chu Lian [2009] No. 13) published jointly by PRC General Administration of Press and Publication, National Copyright Administration, and National Office of Combating Pornography and Illegal Publications on 28 September 2009.

- b) be supported by appropriate regulatory assurance, where possible, to demonstrate the legality of the structured contracts.

The Exchange also expects the Contractual Arrangements to be narrowly tailored to achieve the applicant's business aims and minimise the potential for conflict with PRC laws and regulations.

The listing applicant using a VIE structure and its sponsor are required to:

- (1) provide reasons for the use of structured contracts in its business operation;
- (2) unwind the structured contracts as soon as the law allows the business to be operated without them. The shareholders of the OPCO must undertake that, subject to relevant laws and regulations, they will return to the listing applicant any consideration they receive in the event that the applicant acquires the OPCO shares when unwinding the structured contracts. This undertaking must be included in the listing document;
- (3) ensure that the structured contracts:
 - (a) include a power of attorney granted by the OPCOs' PRC shareholders to the applicant's directors and their successors (including a liquidator replacing the listing applicant's directors) giving them the power to exercise all rights of the PRC shareholders (the OPCO's shareholders must ensure that the power of attorney does not give rise to potential conflicts of interest; the power of attorney should be granted in favour of officers or directors of the applicant who are not also shareholders of the OPCO);
 - (b) include dispute resolution clauses providing:
 - (i) for arbitration and that arbitrators may award remedies over the shares or land assets of the OPCOs, injunctive relief or order the winding up of the OPCOs;
 - (ii) provide the courts of competent jurisdictions with the power to grant interim remedies in support of the arbitration pending formation of the arbitral tribunal. The courts of HK, the applicant's place of incorporation, the place of incorporation of the OPCOs and the place where the principal assets of the OPCOs are located should be specified as having jurisdiction for this purpose; and
 - (c) encompass dealing with the assets of the OPCOs and not only the right to manage its business and the right to revenue. This is to ensure that the liquidator can seize the OPCOs' assets in a winding-up for the benefit of the listing applicant's shareholders or creditors.

The Exchange revised Listing Decision 43-3 in August 2015 to note heightened concerns over the legality and validity of VIE structures to hold interests in PRC businesses which are subject to foreign ownership restrictions following publication of the Draft FIL. The amendments encourage listing applicants which use structured contracts to hold interests in PRC businesses to contact the Exchange at the earliest possible opportunity to seek informal and confidential guidance. The undertakings typically required by the Exchange will be to ensure that the listing applicant is controlled by PRC nationals. The aim is to ensure that the listing applicant will not be regarded as controlled by foreign investors which are prohibited from investing in certain industries and subject to

restrictions on investing in others. The types of undertakings typically required by the Exchange are as discussed above.

Disclosure Requirements

Listing applicants using Contractual Arrangements for the entire or part of their business are required to disclose the following information in the prospectus:

1. detailed discussion about the OPCOs' registered shareholders and a confirmation that appropriate arrangements have been made to protect the applicant's interests in the event of their death, bankruptcy or divorce;
2. the extent to which the applicant has arrangements to address the potential conflicts of interest between the applicant and the OPCO's registered shareholders;
3. reasons why the directors believe that each of the Contractual Arrangements is enforceable under PRC laws and regulations;
4. the economic risks the applicant bears as the primary beneficiary of the OPCO, such as its share of OPCO's financial losses, the circumstances in which the applicant would be required to provide financial support to the OPCO, and other events that could expose the applicant to loss;
5. whether the applicant has encountered any interference from any PRC governing bodies in operating their business through the OPCO under the structured contracts;
6. the limitations in exercising the option to acquire ownership in the OPCO with a separate risk factor explaining the limitations;
7. the structured contracts must be included as material contracts in the "Statutory and General Information" section and must be available on the applicant's website;
8. a corporate structure table in the "Summary" section must be included for the purpose of illustrating the Contractual Arrangements;
9. details of any insurance purchased to cover the risks relating to the structured contracts or prominent disclosure that those risks are not covered by any insurance;
10. separate disclosure of revenue from structured contract arrangements if the listing applicant generates revenue from other subsidiaries apart from the OPCO;
11. the prospectus should include at least the following structured contracts-related risk factors:
 - a. the PRC government may determine that the structured contracts do not comply with applicable regulations;
 - b. the structured contracts may not provide control as effective as direct ownership;

- c. the PRC shareholders may have potential conflicts of interest with the applicant; and
- d. structured contracts may be subject to scrutiny by the PRC tax authorities and additional tax may be imposed.

Disclosure of the structured contracts (other than the risk factors associated with them) should be presented in a standalone section.

PRC property issues

The listing of PRC companies often involves properties situated in the PRC. Despite the rapid development of the property market and title registration system, many issues relating to titles of PRC properties remain unresolved. Therefore, potential PRC listing applicants may face difficulties in evidencing their ownership in those properties due to uncertainty involved in the application process for the relevant land use right certificate and/or building ownership certificate.

The Exchange issued a guidance letter in relation to the requirements for title certificates of PRC properties (HKEx-GL19-10). Below is a summary of the guidance letter:

- For infrastructure project companies and property companies, the relevant title certificates of PRC properties are a pre-requisite for listing approval;
- For mineral and exploration companies, the Listing Rules require them to obtain adequate rights to participate actively in the exploration and extraction of resources. Title certificates are normally required to prove their rights;
- For other companies, the Exchange no longer requires title certificates of PRC properties. Instead, it expects listing applicants to disclose in the prospectus the risks to their operations of not having the relevant title certificates

Practice Note 12 of the Listing Rules provides that where the issue of a land use right certificate is pending, a properly approved land grant or land transfer contract in writing accompanied by a PRC legal opinion as to the validity of the approval may be acceptable as evidence of a transferee's pending title to the land to be granted or transferred.

II. QUALIFICATIONS FOR MAIN BOARD LISTING OF H SHARE COMPANIES

The Listing Rules set out the basic requirements that must be met before any initial listing of equity securities on the Hong Kong Exchange.

(a) Incorporation

The issuer must be duly incorporated as a joint stock limited company in China. This is in order to ensure that the issuer is subject to the Chinese Company Law.

(b) Suitability for Listing (Rule 8.04)

The company and its business must, in the opinion of the Exchange, be suitable for listing. This means, for example, that the nature of the company's business and its management must be in keeping with the standards of integrity which the Exchange endeavours to uphold and that there will be sufficient public interest in the business of the company and in its shares. The Exchange may have concerns if a company is heavily dependent on one product or customer. In such situations, it is advisable to seek a preliminary view of the Listing Committee at an early stage of the application process.

In addition, the Exchange will not normally regard as suitable for listing a company or its group (other than an investment company) whose assets consist wholly or substantially of cash or short-dated securities, except where the issuer or group is solely or mainly engaged in the securities brokerage business. Other factors which the Exchange will take into account in determining suitability are set out in the Exchange's Guidance Letters HKEx-GL 68-13 and 68-13A.

(c) Operating History and Management

The basic requirement is that a Main Board listing applicant must have a trading record period of at least 3 financial years with:

- a. management continuity for at least the 3 preceding financial years; and
- b. ownership continuity and control for at least the most recent audited financial year.

An exception exists for companies applying to list under the market capitalisation/revenue test. For these companies, the Exchange may accept a shorter trading record period under substantially the same management if the applicant can demonstrate that:

- i. its directors and management have sufficient and satisfactory experience of at least 3 years in the line of business and industry of the new applicant; and
- ii. management continuity for the most recent audited financial year.

(d) Financial Tests

Main board listing applicants are required to satisfy one of the following 3 tests: the Profit Test; the Market Capitalisation/Revenue Test; or the Market Capitalisation/Revenue/Cash Flow Test.

The Profit Test (Rule 8.05(1))

The applicant or its group (excluding any entities whose results are recorded in the applicant's financial statements using the equity method of accounting) must have recorded profits of at least **HK\$20 million** in the most recent financial year and aggregate profits of at least **HK\$30 million** in the two years before that. Such profit must exclude any income or loss of the applicant (or its group) generated by activities outside the ordinary and usual course of its business.

Applicants listing under the profits test must also have an expected market capitalisation at the time of listing of at least **HK\$200 million**. This is calculated on the basis of all issued share capital of the applicant including the class of

shares to be listed and all other classes of securities that are either unlisted or listed on other regulated markets at the time of listing. The expected issue price of the shares for which listing is sought is used to determine the market value of securities that are unlisted or listed on other markets.

The Market Capitalisation/Revenue/Cash Flow Test (Rule 8.05(2))

If a listing applicant has an expected market capitalisation at the time of listing of at least HK\$2 billion at the time of listing, there is no profit requirement. Instead the applicant will meet the financial requirement if it has:

- revenue of at least **HK\$500 million** for the most recent audited financial year; and
- positive cash flow from operating activities carried out by the applicant or its group of at least **HK\$100 million** in aggregate for the three preceding financial years.

The Market Capitalisation/Revenue Test (Rule 8.05(3))

- If an applicant has an expected market capitalisation at listing of at least **HK\$4 billion**, it will meet the financial requirement for listing if it has revenue of at least HK\$500 million for the most recent audited financial year.

This test is for larger listing applicants that are able to generate substantial revenue.

Financial Requirement Waivers

The Exchange may also accept a shorter trading record period and/or may vary or waive the financial standards requirements for:

- mineral companies whose directors and management have at least five years' relevant experience in mining and/or exploration activities;
- newly formed "project" companies (for example a company formed to construct a major infrastructure project); or
- in exceptional circumstances, if the applicant or its group has a trading record of at least two financial years and the Exchange is satisfied that the applicant's listing is in the interests of the applicant and its investors.

Calculation of revenue:

For both the Market Capitalisation/Revenue Test and the Market Capitalisation/Revenue/Cashflow Test, only revenue arising from the applicant's principal activities and not items of revenue or gains arising incidentally will be recognised.

Revenue from "book transactions" is disregarded.

(e) Shares in Public Hands (Rule 8.08)

There must be an open market in the securities for which listing is sought. In general, this means that not less than 25% of the listing applicant's total issued

share capital having an expected market capitalisation at the time of listing of at least HK\$50 million, must be held by the public (Rule 8.08(1)(a)), i.e. owned by persons who are not “connected persons” of the issuer or persons whose securities have been financed by a connected person or who are accustomed to take instructions from a connected person in relation to their shares (Rule 8.24). “Connected persons” of a PRC issuer include directors, supervisors, chief executives or substantial shareholders (i.e. holders of 10% of the voting power at general meetings) of the PRC issuer or any of its subsidiaries or an associate of any of them (Rule 1.01).

Where a listing applicant has more than one class of securities apart from the H shares, the total securities of the listing applicant held by the public (on all regulated markets including the Hong Kong Stock Exchange) must be at least 25% of the issuer’s total issued share capital. However, the H shares must not be less than 15% of the issuer’s total issued share capital, and have an expected market capitalisation at the time of listing of not less than HK\$50 million (Rule 8.08(1)(b)).

Exchange’s Discretion to Accept Lower Public Float (Rule 8.08(1)(d))

For large companies, with an expected market capitalisation in excess of HK\$10 billion, the percentage required to be in public hands, may, at the Exchange’s discretion, be lower (but not lower than 15%) provided that:

- (i) the Exchange is satisfied that the number of securities and their distribution will enable the market to operate properly with a lower percentage;
- (ii) the issuer makes appropriate disclosure of the lower prescribed percentage of public float in the listing document;
- (iii) the issuer confirms the sufficiency of public float in successive annual reports after listing; and
- (iv) a sufficient proportion (to be agreed in advance with the Exchange) of any securities to be marketed contemporaneously in and outside Hong Kong, must normally be offered in Hong Kong.

This public float waiver is available only on initial listing. It cannot be applied for post-listing if the issuer subsequently satisfies the HK\$10 billion market capitalisation requirement.

(f) Minimum Number of Shareholders at Time of Listing

Securities new to listing must have an adequate spread of shareholders. The number will depend on the size and nature of the issue, but there must be a minimum of 300 holders.

In addition, not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders (Rule 8.08(3)).

After listing, there is no requirement for a minimum number of shareholders. The issuer must however comply with the minimum public float requirement.

(g) Market Capitalisation

The expected market capitalisation at the time of listing of a new applicant must be at least HK\$200 million and the expected market capitalisation of the securities held by the public must be at least HK\$50 million. If a PRC issuer is listing under the Market Capitalisation/Revenue/Cash Flow Test or Market Capitalisation/Revenue Test it must have an expected market capitalisation at the time of listing of HK\$2 billion or HK\$4 billion, respectively. Most companies at the time of initial flotation have a market capitalisation of around HK\$200 million. Further issues of securities of a class already listed are not subject to this limit, and, in exceptional cases, a lower expected initial market capitalisation may be acceptable, although the Exchange will have to be satisfied as to the marketability of the securities.

Determination of Market Capitalisation at Time of Listing

The expected market capitalisation at the time of listing is calculated on the basis of all issued share capital of the issuer including not only the class to be listed on the Exchange but also any other classes of securities of the issuer that are either unlisted or listed on other regulated markets at the time of listing (Rule 1.01).

The expected issue price of the securities to be listed on the Exchange is used in determining the market value of other classes of securities which are unlisted or listed on other regulated markets (Rule 8.09A). Accordingly, in the case of an H share issuer which also has an A share listing, the expected issue price of the H shares will also be applied to the A shares and any unlisted shares in determining the PRC issuer's market capitalisation at the time of listing.

(h) Working Capital Sufficiency (Rule 8.21A)

A listing applicant must include a working capital statement in the listing document. In making the statement, the applicant must be satisfied after due and careful enquiry that it and its subsidiary undertakings have sufficient working capital for the group's present requirements, that is for at least the next 12 months from the date of publication of the listing document. Applicants whose business is wholly or substantially the provision of financial services and whose solvency and capital adequacy are subject to prudential supervision by another regulatory body are not required to comply with this provision. The applicant's sponsor must provide written confirmation to the Exchange that:

- (i) it has obtained written confirmation from the listing applicant as to the sufficiency of the working capital available to the group for at least 12 months from the date of the listing document; and
- (ii) it is satisfied that this confirmation has been given after due and careful enquiry by the applicant and that the persons or institutions providing finance have stated in writing that the financing facilities exist.

(i) Competing Businesses

The Main Board Rules allow competing businesses of an applicant's directors and controlling shareholders provided that full disclosure is made at the time of listing and, in the case of the directors, on an on-going basis (Rule 8.10). The Exchange may also require the appointment of a sufficient number of INEDs to ensure that the interests of the general body of shareholders are adequately represented.

In the case of a PRC issuer, “controlling shareholder” means any shareholder or other person or group of persons together entitled to exercise, or control the exercise of 30% (or such other amount as may from time to time be specified in applicable PRC law as being the level for triggering a mandatory general offer or for otherwise establishing legal or management control over a business enterprise) or more of the voting power at general meetings of the new applicant or who is in a position to control the composition of a majority of the board of directors of the new applicant. According to Article 217 of the Chinese Company Law, “controlling shareholder” means a shareholder whose shareholding accounts for 50% or more of the total share capital of the new applicant, or a shareholder whose shareholding is less than 50% but whose voting rights pursuant to such shareholding are sufficient to have a major impact on the resolutions of the shareholders' meeting or shareholders' assembly. For the purposes of Listing Rule 8.10, the Exchange will normally not consider a PRC Governmental Body (including central, provincial or local level governments but excluding entities under the PRC government that engage in commercial business or operate another commercial entity) as a “controlling shareholder” of a PRC issuer.

(j) Accountants' Report and Accounting Standards

An issuer must include in its listing document an accountants' report prepared in accordance with Chapter 4 of the Listing Rules. The accountants' report must be prepared by professional accountants qualified under the Professional Accountants Ordinance who are independent of the issuer to the same extent as is required of an auditor under the Companies Ordinance and in accordance with the Hong Kong Institute of Certified Public Accountants' requirements on independence.

The accountants' report must cover the 3 financial years immediately preceding the listing and the latest financial period reported on must not have ended more than 6 months before the date of the listing document.

The financial history of results and balance sheets included in the accountants' report of a PRC issuer may be prepared in accordance with Chinese financial reporting standards as an alternative to Hong Kong or International Financial Reporting Standards (Rule 4.11) and to be audited under Chinese accounting standards. The Exchange will also accept a firm of practising accountants which has been approved by China's Ministry of Commerce and the China Securities Regulatory Commission as being suitable to act as a reporting accountant and auditor for a PRC company listing in Hong Kong.

(k) Directors and Supervisors

The board of directors of a listed company is collectively responsible for the issuer's management and operations. Directors of listed companies are expected to fulfill fiduciary duties and duties of skill, care and diligence to a standard established by Hong Kong law (Rules 3.08). Each director and supervisor of a PRC company must satisfy the Exchange that he has the character, experience and integrity and is able to demonstrate a standard of competence commensurate with his position as director or supervisor of a listed company (Rules 3.09 and 19A.18(2)).

(l) Independent Non-Executive Directors (“INEDs”)

The board of directors is required to include a minimum of 3 INEDs, and INEDs must make up at least one third of the board (Rule 3.10A). One INED must have appropriate professional qualifications or accounting or related financial management expertise (Rule 3.10). The Rules (MB Rule 3.13) contain guidelines for the determination of INED's independence.

INEDs are required to provide the Exchange with written confirmation of their independence in accordance with those guidelines at the time of submission of their declaration and undertaking. They must also provide annual confirmations of their independence to the listed issuer.

Issuers are required to inform the Exchange and publish an announcement if they fail to comply with the requirements in relation to INEDs. The issuer will have three months to rectify the situation.

Every INED must satisfy the Exchange that he has the character, integrity, independence and experience to fulfill his role effectively. INEDs of PRC issuers must additionally be able to demonstrate an acceptable standard of competence and adequate commercial or professional experience to ensure that the interests of the general body of shareholders will be adequately expressed. In addition, at least one INED of a PRC issuer must be ordinarily resident in Hong Kong (Rule 19A.18(1)).

(m) Audit Committee and Remuneration Committee

Audit Committee

The establishment of an audit committee is a compulsory requirement under Rule 3.21. The committee must be made up of non-executive directors only, the majority of which must be INEDs of the listed issuer. The committee must have 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 committee must be chaired by an INED.

The duties and procedures of the audit committee are Code provisions under Section C.3 of the Corporate Governance Code set out in Appendix 14 to the Main Board Rules.

Remuneration Committee

Listed issuers are also required by Rule 3.25 to establish a remuneration committee which must be chaired by an INED and have INEDs as a majority of its members. The issuer's board of directors must approve and provide written terms of reference for the remuneration committee which deals clearly with its authority and duties. The terms of reference of the remuneration committee are required to include, as a minimum, the duties specified in Code Provision B.1.2 of the Corporate Governance Code.

If an issuer fails to comply with the requirements in relation to audit and remuneration committees, it must inform the Exchange, publish an announcement giving reasons for such failure and must ensure that it complies with the requirements within three months.

(n) Sponsor

A new applicant seeking a listing of equity securities on the Main Board must appoint one or more sponsors under a written engagement agreement to assist with its listing application (Rule 3A.02). Only firms that are licensed under part V of the Securities and Futures Ordinance for Regulated Activity Type 6 (Advising on Corporate Finance) and are permitted by their licence to conduct sponsor work are allowed to act as sponsors to new listing applicants. At least one sponsor must be independent of the listing applicant. The sponsor must be appointed (and if there is more than one sponsor, the last sponsor to be appointed must be appointed) at least 2 months before the submission of the listing application.

(o) Compliance Adviser

A PRC issuer is required to retain a compliance adviser for the period commencing on the date of listing and ending on the publication of its financial results for the first full financial year after listing (Rule 3A.19). A compliance adviser must be either a corporation licensed or an authorised institution registered to advise on corporate finance matters under the Securities and Futures Ordinance. Only firms who are permitted by their SFC licence or registration to conduct sponsor work are allowed to act as compliance advisers to companies listed on the Main Board or GEM. A compliance adviser must act impartially but is not required to be independent of the issuer. An issuer is not obliged to appoint as its compliance adviser the same firm that acted as the sponsor of its initial public offering.

Issuers are required to consult with, and if necessary, seek advice from their compliance advisers on a timely basis in the following 4 situations:

- i. before publication of any regulatory announcement, circular or financial report;
- ii. where a notifiable or connected transaction is contemplated;
- iii. where the issuer proposes to use the IPO proceeds differently to the manner detailed in the listing document or where the issuer's business activities, developments or results deviate from any forecast, estimate or other information in the listing document; and
- iv. where the Exchange makes an inquiry of the issuer under Rule 13.10 regarding unusual movements in the price or trading volume of its securities (Rule 3A.23).

The Exchange may also require an issuer to appoint a compliance adviser at any other time after the first full financial year after listing, for example if the issuer has breached the Listing Rules (Rule 3A.20). In this case the Exchange will specify the period of appointment and the circumstances in which the compliance adviser must be consulted.

A compliance adviser to a PRC issuer is additionally required to inform the issuer on a timely basis of any amendment or supplement to the Listing Rules and any change to Hong Kong's laws, regulations or codes which apply to the issuer. The compliance adviser is further required to advise the PRC issuer on continuing compliance with the Listing Rules and applicable laws and regulations (Rule 19A.06(3)). Where the PRC issuer's authorised representatives are expected to be frequently outside Hong Kong, the compliance adviser must act as the issuer's principal channel of communication with the Exchange (Rule 19A.06(4)).

(p) Mandatory Provisions for Articles of Association

The mandatory provisions which must be incorporated in the issuer's Articles of Association, (as set out in Appendix 3 and Appendix 13 Part D Section 1) of the Main Board Listing Rules) are designed to provide a sufficient level of shareholder protection. Additional requirements for PRC issuers include, among others, provisions to reflect the different nature of domestic shares and overseas listed foreign shares (including H shares) and the different rights of their respective holders (Rule 19A.01(3)).

(q) Arbitration (Rule 19A.01(3))

Disputes involving holders of H shares arising from the issuer's articles of association or from any rights or obligations conferred or imposed by the Company Law of the PRC or other relevant PRC laws and regulations must be settled by way of arbitration. The dispute may be heard, at the option of the claimant, at either the China International Economic and Trade Arbitration Commission or the Hong Kong International Arbitration Centre. The arbitral award will be final and binding on the parties to it.

(r) Service Agent (Rule 19A.13(2))

The issuer must appoint, and maintain throughout the period its securities are listed on the Exchange the appointment of, a person authorised to accept service of process and notices on its behalf in Hong Kong. The Exchange must be notified of such appointment, any termination of such appointment, and contact details of the appointee.

If changes in PRC law or market practices materially alter the validity or accuracy of the rules relating to PRC companies, the Exchange may impose additional requirements or make listing of the equity securities of a PRC issuer subject to special conditions, as the Exchange thinks appropriate.

(s) Receiving Agent (Rule 19A.51)

A PRC issuer must appoint a receiving agent in Hong Kong who will receive from the issuer, and hold, pending payment, in trust for H shareholders, dividends declared and other monies owing in respect of H shares.

(t) Share Register

PRC issuers must maintain a register for H shares in Hong Kong (Rule 19A.13(3)(a)). Any rectification of such register will fall under the jurisdiction of the Hong Kong courts.

(u) Management Presence

A new applicant applying for a listing on the Exchange must have sufficient management presence in Hong Kong. This will normally mean that at least two of its executive directors must be ordinarily resident in Hong Kong (Rule 8.12). This requirement applies to Chinese issuers, except as otherwise permitted by the Exchange at its discretion. PRC issuers will generally seek a waiver from the Exchange from this requirement. In considering such waiver application, the Exchange will have regard to, among other considerations, the new applicant's arrangements for maintaining regular communication with the Exchange,

including but not limited to, retaining a compliance adviser and ensuring that its authorised representatives are readily contactable by the Exchange.

(v) Authorised Representatives

Every issuer must appoint 2 authorised representatives to act at all times as the issuer's principal channel of communication with the Exchange (Rule 3.05). The authorised representatives must be either 2 directors or a director and the company secretary unless the Exchange, in exceptional circumstances, agrees otherwise. The responsibilities of an authorised representative include:

- (i) at all times (particularly prior to commencement of trading in the morning) being the principal channel of communication between the Exchange and the listed issuer and supplying the Exchange with his contact details (including home and office telephone and facsimile numbers);
- (ii) to ensure that whenever he is outside Hong Kong suitable alternates are appointed, available and known to the Exchange and to give the Exchange their contact details in writing.

Where a PRC issuer's authorised representatives are expected to be frequently outside Hong Kong, the Compliance Adviser must act as the issuer's principal channel of communication with the Exchange.

(w) Company Secretary (Rule 3.28)

A person will be qualified to act as company secretary if by virtue of his/her academic or professional qualifications or relevant experience he/she is, in the opinion of the Exchange, capable of discharging the functions of a company secretary. The academic or professional qualifications which the Exchange considers acceptable are membership of The Hong Kong Institute of Chartered Secretaries and being a Hong Kong solicitor, barrister or certified public accountant.

In assessing a person's relevant experience, the Exchange will consider the individual's length of employment with the issuer and other issuers and the roles he has played, the person's familiarity with the Listing Rules and other relevant Hong Kong laws and regulations, relevant training undertaken and professional qualifications in other jurisdictions.

A company secretary is not required to be resident in Hong Kong.

(x) Communication

There must be adequate communication and cooperation agreements in place between the Exchange and the relevant securities regulatory authorities in the PRC. If the PRC issuer has securities listed on another stock exchange, there must also be adequate communication arrangements in place with that stock exchange.

Main Board Application Procedure

At the time of applying to list, an applicant must submit a draft listing document (the **Application Proof**), the information in which must be "substantially complete" except

in relation to information that by its nature can only be finalised and incorporated at a later date (Main Board Rule 9.03(3)).

The Exchange has the power **to return** a listing application on the grounds that the information in the listing application or the Application Proof is not “substantially complete” (Main Board Rule 2B.01A and 9.03(3)).

If the Exchange returns a listing application to a sponsor before issuing its first comment letter to the sponsor, the initial listing fee will be refunded but in other cases it will be forfeited. If an application is returned, a new application cannot be submitted until 8 weeks after the Return Decision. The names of the applicant and sponsor(s) together with the return date will also be published on the Exchange’s website.

Before submitting the listing application, the sponsor is required to perform all reasonable due diligence on the listing applicant (except in relation to matters that can only be dealt with later). Sponsors also have a duty to report to the Exchange any material information concerning non-compliance with the Listing Rules or other regulatory requirements relevant to the listing. This duty continues after the sponsor ceases to act for a listing applicant if the information came to the knowledge of the sponsor whilst it was acting as the sponsor.

Other documents which are required to be submitted with the listing application include:

- (i) Written confirmation by each director/supervisor that the information in the Application Proof is accurate and complete in all material respects and not misleading or deceptive;
- (ii) Confirmation from the reporting accountants that no significant adjustment is expected to be made to their draft reports included in the Application Proof (Guidance Letter HKEx-GL58-13));
- (iii) Confirmations from experts that no material change is expected to be made to their reports included in the Application Proof (see Guidance Letter HKEx-GL60-13);
- (iv) Draft letter from the sponsor confirming that it is satisfied that the directors’ statement as to sufficiency of working capital has been made by the directors after due and careful enquiry; and
- (v) A certified copy of the applicant’s certificate of incorporation or equivalent.

The Exchange will comment on the Application Proof within 10 business days from receipt of the application.

Assuming only one round of comments and the submission of a response within 5 business days, the Exchange expects a listing application to be able to be heard by the Listing Committee within 25 business days from the submission of the application. If there are 2 rounds of Exchange comments, assuming sponsor takes 5 business days to respond, the listing application can be heard by the Listing Committee within around 40 business days.

If the listing is approved at the Listing Committee hearing, the Exchange will issue a letter requiring the posting of a near-final draft of the listing document (“PHIP”) on the Exchange’s website. This must be submitted for publication before distribution of the red-herring prospectus to institutional or other professional investors and before book-building commences.

The most important thing is to ensure that the Application Proof which is submitted with the listing application contains all required information to avoid the application being returned by the Exchange. This requirement means that sponsors must complete the vast majority of their due diligence on the listing applicant’s group before submitting the listing application.

III. QUALIFICATIONS FOR GEM LISTING

Chapter 11 of the GEM Listing Rules sets out the basic requirements that must be met before any initial listing of equity securities on the GEM. Chapter 25 contains additional requirements, modifications and exceptions to those requirements which apply to PRC incorporated companies.

(a) Incorporation

The PRC issuer must be duly incorporated in the PRC as a joint stock limited company.

(b) Suitability for Listing

Both the issuer and its business must, in the opinion of the Exchange, be suitable for listing (Rule 11.06). The Exchange may, in its discretion, refuse a listing of a PRC issuer’s securities if it believes that it is not in the interest of the Hong Kong public to list them (Rule 25.07(1)). Factors considered by the Exchange in determining suitability are set out in the Exchange’s Guidance Letters HKEx-GL 68-13 and 68-13A.

(c) Cash Flow Requirement

A GEM listing applicant must have a positive cashflow from operating activities in the ordinary and usual course of business of at least HK\$20 million in total for the 2 financial years immediately preceding the issue of the listing document.

(d) Statement of Business Objectives (Rule 14.19)

A new applicant must include in its listing document a statement of business objectives setting out the following information:

- (i) general information as to (a) the overall business objectives of the new applicant; and (b) the market potential for the new applicant’s business pursuits over the period comprising the remainder of the current financial year of the applicant and the 2 financial years thereafter;
- (ii) a detailed description of the new applicant’s objectives for each of the products, services or activities (and any other objectives) analysed over the period comprising the remainder of the current financial year of the applicant and the 2 financial years thereafter;

- (iii) a detailed explanation as to how the applicant proposes to achieve the stated business objectives.

GEM issuers are required to report on the achievement of the business objectives stated in their listing documents in the annual and half year reports published in the first 2 full financial years after listing.

(e) Operating History and Management

A GEM listing applicant must have:

- (i) management continuity for at least two completed financial years; and
- (ii) ownership continuity and control for at least 1 completed financial year,

immediately before the issue of the listing document. In both cases, continuity must continue until the date of listing.

The Exchange may accept a trading record period of less than 2 financial years and waive or vary the ownership and management requirements for:

- (i) newly formed project companies; (for example a company formed for the purpose of major infrastructure project)
- (ii) mineral companies where the directors and senior management have > 5 years' relevant experience; and
- (iii) in exceptional circumstances under which the Exchange considers it desirable to accept a shorter period.

Where the Exchange accepts a shorter period, the applicant must nevertheless meet the cash flow requirement of HK\$20 million for that shorter trading record period.

(f) Market Capitalisation

The required expected market capitalisation of a new listing application at the time of listing is HK\$100 million.

(g) Public Float

There must be an open market in the securities for which listing is sought. The minimum public float requirement is in line with the Main Board requirement, that is 25% or, in the Exchange's discretion, between 15% and 25% for companies with a market capitalisation of more than HK\$10 billion. Shares held by the public must however have a market capitalisation of at least HK\$30 million at the time of listing (Rule 11.23(2)(a)). If the issuer has more than one class of shares, the total shares in public hands (on all regulated market(s) including the Exchange) at the time of listing must be at least 25% of the issuer's total issued share capital and the shares for which listing is sought must be at least 15% of the total issued share capital with an expected market capitalisation of HK\$30 million at the time of listing.

(h) Minimum Number of shareholders

The equity securities in the hands of the public should, as at the time of listing, be held among at least 100 persons (including those whose equity securities are held through CCASS) (Rule 11.23(2)(b)).

In addition, not more than 50% of the securities in public hands at the time of listing can be beneficially owned by the three largest public shareholders.

(i) Accountants' Report

A new applicant must have an accountants' report covering at least the 2 financial years immediately preceding the issue of the listing document. The Exchange also encourages an issuer with a longer operating history of more than two years to voluntarily disclose three years' financial results in the accountants' report. The latest financial period reported on by the reporting accountants must not have ended more than 6 months before the date of the listing document (Rule 11.11).

(j) Directors and Supervisors

The board of directors of an issuer is collectively responsible for the management and operations of the issuer (Rule 5.01). Every director and supervisor must satisfy the Exchange that he has the character, experience and integrity and is able to demonstrate a standard of competence commensurate with his position as a director or supervisor of the issuer (Rules 5.02 and 25.13(2)).

(k) Independent Non-executive Directors

Independent non-executive directors ("INEDs") must make up at least one third of the issuer's board of directors and there must be at least 3 INEDs. At least one INED must have appropriate professional qualifications or accounting or related financial management expertise (Rule 5.05). Each INED must confirm his independence in accordance with guidelines under Rule 5.09 to the Exchange at the time of submission of his declaration, undertaking and acknowledgement.

INEDs of PRC issuers are further required to demonstrate an acceptable standard of competence and adequate commercial or professional experience to ensure that the interests of the general body of shareholders will be adequately represented (Rule 25.13).

(l) Audit Committee and Remuneration Committee

Every issuer must establish an audit committee comprising non-executive directors only and a minimum of 3 members, at least one of whom is an INED with appropriate professional qualifications or accounting or related financial management expertise (Rule 5.28). The majority of the committee members must be INEDs of the issuer. The audit committee must be chaired by an INED. The duties of the audit committee must include at least the following matters:

- (i) reviewing, in draft form, the issuer's annual report and accounts, half-year report and quarterly reports and providing advice and comments thereon to the issuer's board of directors; and
- (ii) reviewing and supervising the issuer's financial reporting and internal control procedures.

Listed issuers must also establish a remuneration committee with specific written terms of reference which deal clearly with its authority and duties. A majority of the members of the remuneration committee should be independent non-

executive directors and the committee must be chaired by an INED. The terms of reference of the remuneration committee should include, as a minimum, the duties as specified in paragraph B.1.3 of Appendix 15.

If an issuer fails to comply with the requirements in relation to audit and remuneration committees, it must inform the Exchange, publish an announcement giving reasons for such failure and must ensure that it complies with the requirements within three months.

(m) Sponsor

A new applicant seeking a listing of equity securities on GEM must appoint one or more sponsors to assist with its listing application. At least one sponsor must be independent of the listing applicant. The listing application cannot be submitted less than 2 months after the appointment of the last sponsor to be appointed.

(n) Compliance Adviser

A PRC issuer is required to retain a compliance adviser for the period commencing on the date of listing and ending on the publication of its financial results for the second full financial year after listing (Rule 6A.19). A compliance adviser must be either a corporation licensed or authorised institution registered to advise on corporate finance matters under the Securities and Futures Ordinance. It must also be permitted to undertake sponsor work.

GEM issuers are required to consult with, and if necessary, seek advice from their compliance advisers in the same situations as MB issuers.

(o) Compliance Officer

A GEM issuer must appoint one of its executive directors as its compliance officer. The compliance officer's responsibilities must include, as a minimum:-

- (i) advising on and assisting the board of directors of the issuer in implementing procedures to ensure that the issuer complies with the GEM Listing Rules and other relevant laws and regulations applicable to the issuer; and
- (ii) responding promptly and efficiently to all enquiries directed at him by the Exchange.

(p) Mandatory Provisions for Articles of Association

The mandatory provisions which must be incorporated in a PRC issuer's Articles of Association are set out at Appendix 3 and at Section 1 of Part C of Appendix 11 to the Listing Rules. The additional requirements for PRC issuers include:

- (i) provisions which reflect the different nature of domestic shares and overseas listed foreign shares (including H shares) and the different rights of their respective holders (Rule 25.01(3)); and
- (ii) the appointment of a receiving agent in Hong Kong to receive from the issuer, and hold, pending payment, in trust for H shareholders, dividends declared and other moneys owing in respect of the H shares (Rule 25.38).

(q) Competing Businesses

A new applicant will not be rendered unsuitable for listing on the grounds that any director or shareholder has an interest in a business which competes or may compete with the new applicant's business (Rule 11.03).

Full and accurate information of any business or interest of each director, controlling shareholder and, in relation only to the initial listing document, substantial shareholder and the respective associates of each that competes or may compete with the business of the group and any other conflicts of interest which any such person has or may have with the group must be disclosed in (i) each listing document and circular required under the GEM Listing Rules and (ii) in the annual report and accounts, half-year report and quarterly reports of the listed issuer (Rule 11.04).

A "controlling shareholder" of a PRC listing applicant is any shareholder or persons together entitled to exercise or control the exercise of 30% (or such other amount as may from time to time be specified in applicable PRC law as the level for triggering a mandatory general offer or for otherwise establishing legal or management control over a business enterprise) or more of the voting power at general meetings of the new applicant or who is in a position to control the composition of the majority of the applicant's board of directors (Rule 25.10). According to Article 217 of the new Chinese Company Law, "controlling shareholder" means a shareholder whose shareholding accounts for 50% or more of the total share capital of the new applicant, or a shareholder whose shareholding is less than 50% but whose voting rights pursuant to such shareholding are sufficient to have a major impact on the resolutions of the shareholders' meeting or shareholders' assembly. For the purposes of the Listing Rule 11.04, the Exchange will not normally regard a PRC Governmental Body (as defined at Rule 25.04) as a controlling shareholder of a PRC issuer.

(r) Arbitration

Disputes involving holders of H shares and arising from a PRC issuer's articles of association, or from any rights or obligations conferred or imposed by the PRC Company Law and any other relevant laws and regulations concerning the affairs of the PRC issuer, are to be settled by arbitration in either Hong Kong or the PRC at the election of the claimant.

(s) Service Agent

The PRC issuer must appoint, and maintain throughout the period its securities are listed on the GEM the appointment of, a person authorised to accept service of process and notices on its behalf in Hong Kong.

(t) Receiving Agent

A PRC issuer must appoint one or more receiving agents in Hong Kong and pay to such agents dividends declared and other monies owing in respect of its H shares in trust for the holders of such shares.

(u) Register of Shareholders

Provision must be made for a register of holders to be maintained in Hong Kong, or such other place as the Exchange may agree, and for transfers to be registered locally (Rule 25.07).

(v) Authorised Representatives

Every issuer must ensure that, at all times, it has 2 authorised representatives (Rule 5.24). The authorised representatives must be 2 individuals from amongst the issuer's executive directors and company secretary (unless the Exchange, in exceptional circumstances, agrees otherwise). The responsibilities of an authorised representative are as follows (Rule 5.25):

- (i) supplying the Exchange with details in writing of how he can be contacted including home, office and mobile phone telephone numbers and, where available, facsimile numbers and electronic mail addresses;
- (ii) for so long as the issuer continues to have a Sponsor or Compliance Adviser, assisting the Sponsor or Compliance Adviser in their roles under the Listing Rules and, in particular the Sponsor's role as the principal channel of communication with the Exchange concerning the affairs of the issuer.

(w) Company Secretary

The secretary of the issuer must be a person who has the requisite knowledge and experience to discharge the functions of the secretary of the issuer and who possesses the qualifications prescribed under the GEM Listing Rules (Rule 5.14).

APPLICATION PROCEDURES FOR GEM LISTING

GEM Listing Division

The power to approve new listings has been delegated from the Listing Committee to the Listing Division. GEM applicants have a right of appeal to the Listing Committee against the Listing Division's initial decision on an IPO.

Application for listing on the GEM is to be made to the Listing Division. All documents have to be submitted to the Listing Division which reviews all applications.

The process is similar to that for the Main Board and requires submission with the listing application of an advanced draft of the listing document, the Application Proof. The information contained in the Application Proof must be substantially complete except for matters which can only be finalised at a later date.

IV. RESTRICTIONS FOLLOWING LISTING

Restriction on Controlling Shareholders' Disposal of Shares

The Listing Rules impose restrictions on the disposal of shares by controlling shareholders following a company's new listing. Essentially, any person who is a controlling shareholder at the time of listing must not:

- (i) dispose of, nor enter into any agreement to dispose of, or create any options, rights, interests or encumbrances in respect of his shares in the listed issuer in the 6 months after the commencement of dealing in the issuer's securities on the Exchange; or

- (ii) in the 6 months following the expiry of the period in (i) above, dispose of, nor enter into any agreement to dispose of, or create any options, rights, interests or encumbrances in respect of his shares in the listed issuer that would result in such person ceasing to be a controlling shareholder of the company.

Restriction on New Issues of Shares

A listed issuer cannot issue (or agree to issue) any shares or securities convertible into shares of the issuer in the 6 months following listing except for:

- (i) the issue of shares under a share option scheme under Chapter 17 of the Main Board Rules or Chapter 23 of the GEM Rules;
- (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;
- (iv) the issue of shares or securities pursuant to an agreement entered into before the listing and disclosed in the issuer's listing document;
- (v) the issue of shares or securities to be traded on the Main Board by a listed issuer that has successfully transferred its listing from GEM to the Main Board;
- (vi) for GEM issuers, the issue:
 - (a) for the purpose of an acquisition of assets which would complement the listed issuer's business and the acquisition does not constitute a major (or above) transaction; and
 - (b) does not result in a controlling shareholder ceasing to be a controlling shareholder after the issue.

V. CONTINUING OBLIGATIONS OF LISTED COMPANIES

Companies listed on the Exchange have a number of obligations under the Listing Rules and the Securities and Futures Ordinance (the "SFO"). The Listing Rule obligations for Main Board and GEM issuers are virtually the same, the principal difference being in relation to the publication of quarterly financial reports and the deadlines for publication of financial statements.

1. Disclosure of Inside Information

Listed companies have a statutory obligation to disclose price sensitive (or inside) information under Part XIVA of the SFO. Breach of this obligation is a civil offence for which listed companies and their directors may be liable to a fine of up to HK\$8 million.

The information which listed companies are required to announce under the statutory disclosure obligation is the same information which, if possessed by a listed company's directors and other insiders, prohibits them from dealing in the company's securities under the insider dealing offences in Parts XIII and XIV SFO.

1.1 What is Inside Information?

"Inside information" is defined as:

"specific information that:

- (a) is about:
 - i. the corporation;

- ii. a shareholder or officer of the corporation; or
 - iii. the listed securities of the corporation or their derivatives; **and**
- (b) is not generally known to the persons who are accustomed or would be likely to deal in the listed securities of the corporation but would if generally known to them be likely to materially affect the price of the listed securities.

Key elements of the definition

The three key elements of the definition are that:

- (a) the information must be **specific**;
- (b) the information must not be generally known to that segment of the market which deals or which would likely deal in the corporation’s securities; and
- (c) the information would, if generally known be likely to have a material effect on the price of the corporation’s securities.

The SFC has published Guidelines on Disclosure of Inside Information (the “**SFC Guidelines**”) which provide guidance as to how these terms have been interpreted by the Market Misconduct Tribunal in the past.

The board of directors must give careful consideration to significant or unexpected events to determine whether it constitutes “inside information” which must be announced.

In assessing whether inside information is likely to materially affect the price of the issuer’s securities, the test to be applied is: whether the inside information would influence persons who are accustomed to or would be likely to deal in the issuer’s shares, in deciding whether or not to buy or sell such shares.

The SFC Guidelines set out examples of inside information including:

- Changes in performance, or the expectation of the performance, of the business or its financial condition;
- Changes in financial condition, e.g. cashflow crisis, credit crunch;
- Changes in directors and (if applicable) supervisors and their service contracts;
- Changes in auditors or any other information related to the auditors’ activity;
- Changes in the share capital, e.g. new share placing, bonus issue, right issue, share split, share consolidation and capital reduction;
- Takeovers and mergers;
- Purchase or disposal of equity interests or other major assets or business operations;
- Legal disputes and proceedings;
- Changes in expected earnings or losses;
- Insolvency of relevant debtors;
- Reduction of real properties’ values; and
- Orders received from customers, their cancellation or important changes.

1.2 Timing of disclosure

A company must announce inside information **as soon as reasonably practicable** after any inside information has come to its knowledge. Inside information has come to the company’s knowledge if the inside information has, or ought reasonably to have, come to the knowledge of an officer (that is a

director, manager or secretary) of the corporation in the course of performing functions as an officer of the company.

Listed companies 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.

The company must ensure that the information is kept strictly confidential until it is publicly disclosed. If the company believes that confidentiality cannot be maintained or that there may have been a breach of confidentiality, it should immediately disclose the information to the public. A company can also issue a “holding announcement” to give it time to clarify the details and likely impact of an event before issuing a full announcement.

Inside information must be disclosed to the public by means of an announcement published on the websites of the Exchange and the listed company.

1.3 The Safe Harbours

There are four situations where listed companies are not required to disclose inside information. These are where:

1. disclosure would **breach an order by a Hong Kong court or any provisions of other Hong Kong statutes**;
2. the information relates to an **incomplete proposal or negotiation** (e.g. a contract is being negotiated but has not been finalised);
3. if the information is a **trade secret**; or
4. if the information concerns the provision of **liquidity support** from the Government’s Exchange Fund or a Central Bank (or institution performing such functions, inside or outside HK).

Companies can only rely on the safe harbours in paragraphs 2, 3 and 4 above if they have taken reasonable precautions to preserve the confidentiality of the inside information and the inside information has not been leaked.

If confidentiality is lost or the information is leaked, the company must announce the inside information as soon as practicable.

1.4 Liability of Officers

A listed company’s officers are required to take all reasonable measures to ensure that proper safeguards exist to prevent the company’s breach of the disclosure requirement. If a listed company breaches the disclosure obligation, an officer of the company will also have breached the obligation if either:

- (a) the breach resulted from the officer’s intentional, reckless or negligent conduct; or
- (b) the officer has not taken all reasonable measures to ensure that proper safeguards exist to prevent the breach).

In relation to officers’ obligation to take all reasonable measures to ensure the existence of proper safeguards, 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 company 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.

Possible penalties which can be imposed include:

- (a) a fine of up to HK\$8 million on the company, a director or chief executive (but not officers) of the company; and
- (b) disqualification of the director or officer from being a director or otherwise involved in the management of a corporation for up to five years.

2. Obligation to Respond to Exchange Enquiry

Under Main Board Rule 13.10 (GEM Rule 17.11) the Exchange may make an 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. An issuer is required to respond promptly to the Exchange's enquiries in one of the following two ways:

1. provide to the Exchange and, if requested by the Exchange, announce any information relevant to the subject matter(s) of the enquiries available to it, so as to inform the market or to clarify the situation; or
2. 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(s) of the enquiries, or of any inside information which 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.

3. Announcements

The Listing Rules require listed companies to publish announcements in a wide range of situations. Announcements must be published on the websites of the Exchange and the listed company. Matters which must be announced include (among others):

Inside information 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 (chapter 19 of the GEM Rules).

Connected transactions – any connected transaction (unless an exemption is available) within Chapter 14A of the Main Board Rules (Chapter 20 of the GEM Rules).

Board meeting for approval of results – an issuer must publish an announcement at least 7 clear business days before 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/GEM Rule 17.48).

Annual, half-year and quarterly results – must be published by way of announcement.

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 must be announced.

Memorandum and Articles of Association – any proposed alteration of the memorandum or articles of association of the listed issuer

Change in directors and supervisors – any change of directors, supervisors or the chief executive, including, in the case of the resignation or removal of a director, a supervisor or the chief executive, the reasons given by or to him for his resignation or removal.

Notice of general meetings – notice of an issuer’s annual general meeting and other general meetings must be announced.

Issues of securities – an issue of securities (including convertible securities or warrants, options or similar rights) will almost always require an announcement.

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).

Share Repurchases – any purchase, sale, drawing or redemption by the company or its group members of its listed securities (whether on the Exchange or not).

4. Disclosure of Financial Information

4.1 Qualifications of auditors

The annual accounts must be audited by practising accountants of good standing. Such auditors must be independent of the PRC issuer as required under the Companies Ordinance and in accordance with the statements on independence issued by the International Federation of Accountants. If the PRC issuer’s primary listing is or is to be on the Exchange, the auditors must be:

- 1) qualified under the Professional Accountants Ordinance; or
- 2) a firm of practising acceptable to the Exchange which has an international name and reputation and is a member of a recognised body of accountants; or
- 3) a firm of practising accountants acceptable to the Exchange which is a joint venture approved by the China Securities Regulatory Commission (“CSRC”) to act as an auditor of a listed company in the PRC and at least one of the principal joint venture partners is qualified under 1) or acceptable under 2); or
- 4) a firm of practising accountants approved by the China Ministry of Finance and CSRC as being suitable to act as an auditor or a reporting accountant for a PRC company listed in Hong Kong (Main Board Rule 19A.31).

4.2 Audit standards

The accounts of a PRC issuer must be audited to a standard comparable to that required in Hong Kong or under International Standards on Auditing or China Auditing Standards. Also, the auditors' report must be annexed to all copies of the annual accounts required to be sent by the PRC issuer and indicate whether the accounts give a true and fair view. If the PRC issuer is not required to draw up its accounts so as to give a true and fair view, the PRC issuer can draw them up to an equivalent standard only if allowed by the Exchange. Reference must be made to the Exchange.

4.3 Annual Reports and Accounts

Listed companies must send a copy of their annual report and accounts and, if it prepares group accounts, its group accounts, together with a copy of the auditors' report to every shareholder and every holder of its listed securities not less than 21 days before the date of its annual general meeting ("AGM") and no later than 4 months after the end of the financial year (in the case of Main Board listed companies) or 3 months after the financial year end (in the case of GEM listed companies).

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

In the case of overseas shareholders, it is sufficient for the listed issuer to mail the English language version of the relevant documents provided that such documents contain a prominent statement in English and Chinese that a Chinese language version is available from the company on request.

4.4 Half-year Reports and Accounts

Main Board listed companies must send half-year reports to the company's shareholders and holders of their listed securities within 3 months of the end of the first 6 months of each financial year.

Companies listed on GEM are required to publish half-year reports within 45 days of the end of the first 6 months of each financial year and must send the report to shareholders and holders of their listed securities as soon as practicable after publication.

The financial statements included in the half-year report will generally be unaudited. If this is the case, this fact must be stated. If the financial statements are audited, the auditors' report and any qualifications must be included in the half-year report.

Half-year reports must be reviewed by the listed issuer's audit committee.

4.5 Quarterly Reporting

For Main Board listed companies, quarterly reporting is a Recommended Best Practice only under the Corporate Governance Code, not a mandatory obligation under the Main Board Rules. If a Main Board listed issuer decides to publish quarterly financial results, it should do so within 45 days of the end of each quarter. Once a Main Board listed company decides to publish quarterly results,

an announcement is required disclosing the reasons for any decision not to publish results for any particular quarter.

Companies listed on GEM are required to publish quarterly reports within 45 days of the end of the relevant quarter.

4.6 Preliminary Announcements of Results

A company listed on the Main Board must publish a preliminary announcement of its annual and half-year results on the websites of the Exchange and the listed company as soon as possible and, in any event, not later than 30 minutes before the earlier of the commencement of the morning trading session or any pre-opening session on the business day after their approval by the board.

Preliminary year-end results must be published no later than 3 months after the financial year end and preliminary half-year results must be published no later than 2 months after the half-year end.

A company listed on GEM must publish a preliminary announcement of its annual, half-year and quarterly results as soon as possible and, in any event, not later than 30 minutes before the earlier of the commencement of the morning trading session or any pre-opening session on the business day after their approval by the board.

GEM listed companies must publish preliminary year-end results no later than 3 months after the financial year end and must publish preliminary half-year and quarterly results no later than 45 days after the end of the relevant period.

The Exchange may suspend dealings in a listed company's shares or cancel the listing if a listed company fails to publish its financial information on time.

5. Notifiable Transactions

Chapter 14 of the Main Board Listing Rules (Chapter 19 of the GEM Rules) sets out detailed requirements in respect of certain transactions, principally acquisitions and disposals, entered into by a listed issuer and its subsidiaries.

The requirements include obligations to notify the Exchange of the transaction, disclose the transaction to the public by publication of an announcement and to obtain prior shareholders' approval depending on the size of the transaction.

5.1 Definition of Transaction

A "transaction" includes (among others):

- (a) an acquisition or disposal of assets;
- (b) the grant, acceptance, transfer, exercise or termination of an option to acquire or dispose of assets or to subscribe for securities;
- (c) entering into or terminating finance leases where the financial effects of such leases have an impact on the balance sheet and/or profit and loss account of the listed issuer;
- (d) entering into or terminating operating leases which, by virtue of their size, nature or number, have a significant impact on the operations of the listed

- issuer;
- (e) granting an indemnity or a guarantee or providing financial assistance, except to the listed issuer's own subsidiaries; and
 - (f) entering into a joint venture entity in any form.

To the extent not expressly provided in (a) to (f) above, the definition of "transaction" excludes any transaction of a revenue nature in the ordinary and usual course of business of the listed issuer.

5.2 Classification of Notifiable Transactions

The requirements for a notifiable transaction depend upon which of the 6 categories of notifiable transaction it falls into. Classification is made on the basis of the percentage ratios as set out in the table below.

<u>Transaction Type</u>	<u>Assets ratio</u>	<u>Consideration ratio</u>	<u>Profits ratio</u>	<u>Revenue ratio</u>	<u>Equity capital ratio</u>
Share transaction	less than 5%	less than 5%	less than 5%	less than 5%	less than 5%
Discloseable transaction	5% or more but less than 25%	5% or more but less than 25%	5% or more but less than 25%	5% or more but less than 25%	5% or more but less than 25%
Major transaction - disposal	25% or more, but less than 75%	25% or more, but less than 75%	25% or more, but less than 75%	25% or more, but less than 75%	Not Applicable
Major transaction – acquisition	25% or more, but less than 100%	25% or more, but less than 100%	25% or more, but less than 100%	25% or more, but less than 100%	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	100% or more	100% or more	100% or more	100% or more

The categories of notifiable transactions are:

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

- A **major transaction** is a transaction or a series of transactions by a listed issuer or one of its subsidiaries where any percentage ratio is 25% or more, but less than 100% for an acquisition or 75% for a disposal;
- A **very substantial disposal** is a disposal or a series of disposals of assets by a listed issuer or one of its subsidiaries where any percentage ratio is 75% or more;
- A **very substantial acquisition** is an acquisition or a series of acquisitions of assets by a listed issuer or one of its subsidiaries where any percentage ratio is 100% or more; and
- A **reverse takeover** is an acquisition or a series of acquisitions of assets by a listed issuer 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 .

A “reverse takeover” includes:

- (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 of the listed issuer** that had not been regarded as a reverse takeover, which individually or together **reach the threshold for a very substantial acquisition**.

5.3 Percentage Ratios

The percentage ratios normally referred to as the “five tests” are the figures expressed as percentages resulting from each of the following calculations:

- **Assets ratio** —the total assets which are the subject of the transaction divided by the total assets of the listed issuer;
- **Profits ratio**— the profits attributable to the assets which are the subject of the transaction divided by the profits of the listed issuer;
- **Revenue ratio**— the revenue attributable to the assets which are the subject of the transaction divided by the revenue of the listed issuer;
- **Consideration ratio** — the consideration divided by the total market capitalisation of the listed issuer. The total market capitalisation is the average closing price of the listed issuer’s securities as stated in the Exchange’s daily quotations sheets for the five business days immediately preceding the date of the transaction; and
- **Equity capital ratio** — the nominal value of the listed issuer’s equity capital issued as consideration divided by the nominal value of the listed issuer’s issued equity capital immediately before the transaction. The value of the listed issuer’s debt capital (if any), including any preference shares, is not included in the calculation of the equity capital ratio.

Aggregation of Transactions

Pursuant to Rule 14.22, the Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are all completed within a 12 month period or are otherwise related.

5.4 Consequences of entering into a notifiable transaction

The actions required to be taken by the issuer depend on the category of notifiable transaction within which the transaction falls. The requirements under applicable to each category are as follows:

	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 inside information	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 *No shareholder approval is necessary if the consideration shares are issued under a general mandate. However, if the shares are not issued under a general mandate, the listed issuer is required to obtain shareholders' approval in general meeting prior to the issue of the consideration shares.*
- 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 *A listed issuer may at its option include an accountants' report.*

6 *Approval of the Exchange is necessary.*

Notification and Announcement Requirements

As soon as possible after the terms of a notifiable transaction have been finalised, the listed issuer must:

- (1) inform the Exchange; and
- (2) publish an announcement on the websites of the Exchange and the listed issuer.

Circular to Shareholders

The circular for major transactions to be approved in general meeting, very substantial acquisitions and very substantial disposals, must be sent to shareholders on or before the deadline for giving notice of the general meeting under the PRC Company Law. The deadline for giving notice under PRC Company Law is 20 days in the case of a general meeting and 15 days for a special general meeting.

Shareholders' Approval Requirements

Major Transactions, Very Substantial Disposals, Very Substantial Acquisitions and Reverse Takeovers must be made conditional on approval by shareholders in general meeting.

Any shareholder that has a material interest in the transaction must abstain from voting.

Requirements for Reverse Takeovers

The Exchange will treat a listed issuer proposing a reverse takeover as a new listing applicant. The enlarged group or the assets to be acquired must be able to meet the financial tests for listing and the enlarged group must be able to meet all other listing criteria.

The listed issuer must comply with the procedures and requirements for new listing applicants and must appoint a sponsor, issue a listing document and pay the initial listing fee. A PRC issuer must send the listing document to shareholders on or before the deadline for giving notice of the general meeting under the PRC Company Law.

6. Connected Transactions

The Listing Rules contain detailed rules on transactions between the listed issuer's group and its connected parties. Their objectives are:

- a) to ensure that a listed issuer takes into account the interests of shareholders as a whole when it enters into connected transactions;
- 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.

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.

6.1 **Definition of Transaction**

The term “transaction” for the purposes of the connected transaction requirements includes the following, regardless of whether any such transaction is of a revenue nature and entered into in the ordinary and usual course of the listed issuer’s business:

- a) the acquisition or disposal of assets;
- b) any transaction involving an option to acquire or dispose of assets or to subscribe for securities;
- c) entering into or terminating finance or operating leases;
- d) granting an indemnity or a guarantee or providing financial assistance;
- e) entering into a joint venture;
- f) issuing new securities;
- 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.

6.2 **Connected Persons**

“Connected persons” are defined to include:

- (a) a **director, supervisor, 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;
- (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 **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.

The associates of an individual include:

- a) his spouse, his (or his spouse’s) child or step-child (natural or adopted) under the age of 18 years (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”).

- c) a company in which the **individual**, his **immediate family members** and/or the **trustees** (individually or together) control the exercise of **30%** or more of the voting power or control the composition of a majority of the board of directors, and **any subsidiary** of such company.
- 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 the exercise of **50%** or more of the voting power or control the composition of a majority of the board of directors, and any of its **subsidiaries**;
- 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; and
- 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 the exercise of **50%** or more of the voting power or control the composition of a majority of the board of directors, 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.

Associates of a company

The associates of a connected person which is a company include:

- a) its **subsidiary** or **holding company**, or **fellow subsidiary** of such a holding company (together, the “**group companies**”);
- b) the trustees of any trust of which the company is a beneficiary or, to the company’s 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).

The Exchange will not normally treat a PRC Governmental Body as a connected person of a PRC issuer

Deemed Connected Persons

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

- a) the person or entity 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, supervisor or substantial shareholder of the issuer or any of its subsidiaries or a person who was such a director within the previous 12 months; and
- b) the person or entity should, in the Exchange's opinion, be considered as a connected person .

6.3 Connected Transactions where there is no transaction with a connected person

A group acquiring an interest in a company (the "**target company**") from a person who is not a connected person is a connected transaction if the target company's substantial shareholder:

- (i) is (or is proposed to be) a **controller** (i.e. a director, chief executive or controlling shareholder of the listed issuer); or
- (ii) is, or will, as a result of the transaction, become, an associate of a controller or proposed controller of the listed issuer.

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

6.4 Financial assistance

Financial assistance includes granting credit, lending money, providing security for, or guaranteeing a loan.

Financial assistance provided **by** a listed issuer or its subsidiaries will constitute a connected transaction where it is provided **to**:

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

"Commonly Held Entity" refers to 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.

Financial assistance provided to a listed issuer or its subsidiaries will constitute a connected transaction where it is provided by:

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

6.5 Options involving Connected Persons

The grant, acceptance, transfer, exercise or non-exercise of an option by a listed issuer or its subsidiaries to or from a connected person is a connected transaction and is classified by reference to the percentage ratios (except the profits ratio).

Termination of an option by a listed issuer is a “transaction” unless termination is in accordance with the terms of the original agreement and there is no payment of any penalty, damages or other compensation.

6.6 Joint ventures involving Connected Persons

The entering into of any arrangement or agreement involving the formation of a joint venture entity in any form, such as a partnership or company or any other form of joint venture arrangement, by a listed issuer and a connected person constitutes a connected transaction (Rule 14A.10(13)(f)).

6.7 Continuing Connected Transactions

Continuing connected transactions are connected transactions that:

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

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

6.8 Classification of Connected and Continuing Connected Transactions

Connected and continuing connected transactions fall into three categories:

- i. Non-exempt transactions which must be: (a) reported in the listed issuer’s annual report; (b) announced on the websites of the Exchange and the listed issuer; and (c) made conditional on being approved by the issuer’s independent shareholders;
- ii. Transactions exempt from the reporting, announcement and independent shareholders’ approval requirements (“**wholly exempt**” transactions); and
- iii. Transactions exempt from the independent shareholders’ approval requirement only (but subject to the reporting and announcement requirements) (“**partially exempt**” transactions).

6.9 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.

Independent board committee and financial adviser requirements

Where a connected transaction must be approved by the issuer's independent shareholders, an **independent board committee** 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.

An **independent financial adviser** must be appointed to make recommendations to the independent board committee as to the matters set out above.

Additional requirements apply to continuing connected transactions. These include requirements that:

- (i) the agreement governing the transaction must be on normal commercial terms and must 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.
- (ii) The listed issuer must set a maximum aggregate annual cap expressed in monetary terms.
- (iii) Continuing connected transactions must be reviewed annually by the company's independent non-executive directors and its auditors.

6.10 Exemptions from Connected Transaction Requirements

There are a number of exemptions which are available. These include the following:

Intra-group transactions

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

- a) none of the subsidiaries concerned are connected persons; 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 (Rule 14A.18).

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:

- a) less than 0.1%;
 - b) less than 1% and the transaction is a connected transaction only because it involves a connected person at the subsidiary level; or
 - c) 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.

Partially exempt connected transactions

Connected transactions are exempt from the independent shareholders' approval requirement only (and are subject to the reporting and announcement requirements) where the connected transaction is on normal commercial terms or better to the listed issuer and 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.

7. The Corporate Governance Code

The Corporate Governance Code (the "Code") contains two levels of recommended practices. The first tier contains the "Code Provisions". Listed companies must state in their half-year and annual reports whether they have complied with the Code Provisions (CP) and give reasons for any non-compliance.

The second level 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 non-compliance in their financial 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.

8. The Model Code for Securities Transactions by Directors and Supervisors of Listed Companies ("Model Code")

Listed Companies must adopt rules governing dealings by directors and supervisors in their listed securities on terms no less stringent than the terms set out in the Listing Rules.

Absolute Prohibition

The Model Code provides that a director or supervisor of a listed company **must not** deal in the securities of the company:

- at any time when he is in possession of unpublished inside information in relation to those securities, or if clearance to deal has not been given;
- on the publication date of the company's financial results;
- during the period of 60 days preceding the publication date 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

- during the period of 30 days preceding the publication date of the quarterly results (if any) or half-year results or, if shorter, the period from the end of the relevant quarterly or half-year period up to the publication date of the results.

Further, a director or supervisor of a listed issuer must not deal in its securities 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 also apply equally to dealings by directors' and supervisors' spouses and children under the age of 18 and to other dealings in which they are deemed to be interested for the purposes of Part XV of the SFO.

Duty of Notification

Listed companies must establish a procedure whereby a director or supervisor is required to give 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 company.

9. The Environmental, Social and Governance Reporting Guide

According to Main Board Rule 13.91 (GEM Rule 17.103), listed issuers are required to disclose the Environmental, Social and Governance (**ESG**) matters set out in the Environmental, Social and Governance Reporting Guide (Appendix 27 to the Main Board Rules/ Appendix 20 to the GEM Rules). These matters must be disclosed in the annual report of the relevant financial year or in a separate ESG report. There are two levels of ESG disclosures: "comply or explain" and "recommended disclosures".

"Comply or explain" – The listed issuer must comply with these disclosure provisions, but may deviate from these provisions if they can provide considered reasons for the deviation in its ESG report.

"Recommended disclosures" – The listed issuer is encouraged, but not required, to report on these matters.

ESG reports must be published on an annual basis and regarding the same period as their annual reports.

Currently, key performance indicators in the "Environmental" subject area are only recommended disclosures. Beginning on 1 January 2017, those key performance indicators will be a "comply or explain" disclosure.

August 2016

This note is provided for information purposes only and does not constitute legal advice. Specific advice should be sought in relation to any particular situation. This note has been prepared based on the laws and regulations in force at the date of this note which may be subsequently amended, modified, re-enacted, restated or replaced.