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The transition from private to public ownership is a major step in the lifecycle of a company, involving a complex and often challenging process of dealing with regulators, investors and professional parties, while continuing to run the company’s business. As one of the world’s preeminent international financial centers, Hong Kong has become a destination of choice for many companies seeking to make this transition through an initial public offering (“IPO”) and listing on the Hong Kong Stock Exchange. The MoFo Guide to Hong Kong IPOs (“Guide”) aims to help companies and their advisers successfully navigate this transition by providing a comprehensive overview of the IPO process in Hong Kong, with an emphasis on listings on the Main Board of the Hong Kong Stock Exchange.

The Guide covers the IPO process from the preliminary planning stages and pre-IPO considerations all the way up to, and including, a listed company’s post-IPO obligations. The Guide also discusses listing issues pertinent to companies in specific industries, such as mineral and natural resources companies, as well as issues that arise when conducting an international offering to investors in other jurisdictions, such as the United States. Practical tips are included throughout the Guide based on our experience advising on Hong Kong IPOs over the years.

While we have tried to make the Guide as informative as possible, please kindly note that it is only an overview of the major legal, regulatory and practical issues involved in the Hong Kong IPO process as of November 5, 2012 and therefore should not be relied upon as legal advice in any jurisdiction. Because of the generality of the Guide, the information provided herein may not be applicable to all situations and should not be acted upon without specific legal advice based on particular situations.

Finally, we also invite you to visit our publications website for our China Capital Markets practice (www.mofo.com/hk-capital-markets), where you will be able to find even more resources, including our Hong Kong Capital Markets Quarterly News newsletter. If you wish to obtain a free subscription to our Hong Kong Capital Markets Quarterly News, please send an email to chinamarketing@mofo.com.

We hope that you enjoy the Guide and find it readable, helpful and useful. Please do not hesitate to contact any of the members of our capital markets team if you have any questions or comments.
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DECIDING TO GO PUBLIC

Going public is a monumental decision for any company. The preparation for “being public” is just as crucial as the preparation for “going public.” When considering an IPO, a company should carefully evaluate both the benefits and the burdens of becoming, and maintaining itself as, a public company. A company may also wish to evaluate alternatives to achieving capital raising, liquidity or other goals, such as a private sale, a merger or corporate partnering arrangements.

CONSIDERING THE BENEFITS AND BURDENS OF GOING PUBLIC

<table>
<thead>
<tr>
<th>PROS</th>
<th>CONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Raise capital and provide liquidity for current investors</td>
<td>Increased expenses</td>
</tr>
<tr>
<td>Increase market value and name recognition</td>
<td>Significant disclosure obligations</td>
</tr>
<tr>
<td>Research analyst coverage</td>
<td>Pressure for financial performance</td>
</tr>
<tr>
<td>Future access to capital for growth</td>
<td>Restrictions on insider dealing</td>
</tr>
<tr>
<td>Securities become attractive currency to potential acquisition targets</td>
<td>Increased risk of legal exposure</td>
</tr>
<tr>
<td>Improve corporate governance and transparency</td>
<td>Investor relations management</td>
</tr>
<tr>
<td>Ability to attract and keep key personnel</td>
<td></td>
</tr>
</tbody>
</table>

IS THE COMPANY READY?

Before embarking on an IPO, a company’s board and management should objectively assess their readiness for life as a public company, including:

- the company’s business and financial track record and outlook;
- the principal risks of the business;
- the level of experience and commitment of the company’s management team;
- the adequacy of the company’s internal control systems and procedures;
- the maturity of the company’s governance structures;
- the company’s willingness to comply with disclosure and reporting requirements; and
- the company’s readiness to deal with analysts, institutional investors and the public.
WHY LIST IN HONG KONG?

As an international financial center, Hong Kong is one of the world’s leading capital markets, with the Stock Exchange of Hong Kong Limited (the “Exchange”) being a favored venue for IPO fund-raising activities. In 2011, total IPO funds raised in Hong Kong amounted to approximately US$36.2 billion, making Hong Kong the world’s largest IPO exchange for a third consecutive year. Total equity funds raised on the Exchange in 2011, including IPOs and post-IPO fund-raising, were more than US$60 billion.

| IPO Funds Raised by Various Exchanges in 2011 (in US$ billions) |
|--------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| HKEx               | NYSE             | SZSE             | LSE              | SHSE             | NASDAQ           | SGX              | BME              | BM&P             | KRX              | TSE              |
| 36.2               | 31.4             | 26.2             | 19.4             | 16.3             | 10.7             | 7.6              | 5.3              | 4.7              | 3.6              | 1.8              |

At the end of September 2012, there were more than 1,500 companies listed on the Main Board of the Exchange, among which were more than 700 Mainland Chinese enterprises comprising approximately 56% of the total market capitalization.

While Hong Kong has long been a preferred venue for Chinese companies seeking to tap the international capital markets, it is increasingly becoming a popular listing venue for companies outside of Hong Kong and China looking to access the region’s capital pools and seeking to raise brand awareness in China and throughout Asia. The end of 2011 saw a dramatic increase in the number of overseas companies seeking a listing on the Exchange, including Swiss mining firm Glencore International, Italian fashion house Prada, U.S. luggage maker Samsonite and Japanese online financial services firm SBI Holdings.

For Chinese issuers, Hong Kong has a clear advantage over other countries and regions in that its investment community has an in-depth understanding of Mainland China’s business environment, economy and future development. Accordingly, Hong Kong is ideally positioned to support Mainland China’s immense capital and financial needs.
Other advantages of listing in Hong Kong include:

- Hong Kong acts as a gateway to Mainland China and Asia and offers opportunities for greater exposure to China and the rest of Asia.
- Hong Kong has a well-established legal system based on English common law, as well as a sound regulatory framework that promotes a high level of disclosure from listed companies.
- The Exchange promotes the use of international accounting standards, as well as other recognized accounting standards under certain circumstances, such as secondary listings.
- Hong Kong provides for the free flow of capital, with tax advantages, currency convertibility and the free transferability of securities.
- Hong Kong has continued to develop as an offshore RMB fund-raising center, which provides future fund-raising opportunities for companies seeking to expand in Mainland China.

EXPENSES OF A HONG KONG IPO

Many factors play a role in determining the cost of an IPO, but in all cases, the costs of going public are significant. Professional fees must be paid to sponsors, legal counsels, accountants and other experts. The total fees are highly dependent on the size and complexity of the offering, as well as the quality and reputation of the professionals.

The main categories of expenses for a Hong Kong IPO are as follows:

- sponsor(s) and underwriters;
- company legal counsel;
- underwriters’ legal counsel;
- local counsels, if any;
• auditors;
• internal control consultants;
• property valuers, if any;
• technical consultants, if any;
• financial printer;
• public relations firm;
• roadshow expenses, including travel and accommodation;
• share registrars and transfer agents;
• market research firm, if any; and
• the Exchange’s initial listing fee.

The table below sets out the Exchange’s initial listing fees:

<table>
<thead>
<tr>
<th>MONETARY VALUE OF EQUITY SECURITIES TO BE LISTED</th>
<th>INITIAL LISTING FEE</th>
</tr>
</thead>
<tbody>
<tr>
<td>(HK$ million)</td>
<td>(US$ million)</td>
</tr>
<tr>
<td>not exceeding 100</td>
<td>13</td>
</tr>
<tr>
<td>200</td>
<td>26</td>
</tr>
<tr>
<td>300</td>
<td>38</td>
</tr>
<tr>
<td>400</td>
<td>51</td>
</tr>
<tr>
<td>500</td>
<td>64</td>
</tr>
<tr>
<td>750</td>
<td>96</td>
</tr>
<tr>
<td>1,000</td>
<td>128</td>
</tr>
<tr>
<td>1,500</td>
<td>192</td>
</tr>
<tr>
<td>2,000</td>
<td>256</td>
</tr>
<tr>
<td>2,500</td>
<td>321</td>
</tr>
<tr>
<td>3,000</td>
<td>385</td>
</tr>
<tr>
<td>4,000</td>
<td>513</td>
</tr>
<tr>
<td>5,000</td>
<td>641</td>
</tr>
<tr>
<td>Over 5,000</td>
<td>641</td>
</tr>
</tbody>
</table>

Notes:
1. For secondary listings on the Main Board, the initial listing fee is normally 25% of the fees listed above, subject to a minimum payment of HK$150,000 (US$19,231).
2. In addition to the initial listing fees, once a company’s securities are listed on the Exchange, it must pay an annual listing fee to the Exchange.
CHAPTER 2

REGULATORY OVERVIEW

A. PRINCIPAL STATUTORY AND NON-STATUTORY RULES

The principal statutory and non-statutory rules governing the marketing of new issues in Hong Kong are:

- the Companies Ordinance (Cap. 32) (the “CO”);
- the Securities and Futures Ordinance (Cap. 571) (the “SFO”);
- the non-statutory Listing Rules of the Exchange; and
- the Securities and Futures (Stock Market Listing) Rules.

The principal rules regulating the conduct of sponsors and licensed or registered persons in Hong Kong are:

- the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (June 2012) (the “SFC Code of Conduct”);
- the Corporate Finance Adviser Code of Conduct (October 2011) (the “CFA Code”); and
- the Fit and Proper Guidelines (September 2006) (the “Sponsor Guidelines”).

COMPANIES ORDINANCE

CO Prospectus Regime

The CO sets out the prospectus regime which regulates public offerings of shares and debentures in Hong Kong. Unless exempted pursuant to one of the safe harbors discussed more fully below, it is a criminal offense to issue any prospectus offering shares in or debentures of a company (including companies incorporated outside Hong Kong) to the public for subscription or purchase, unless such prospectus complies with the requirements in the CO and has been registered with the Registrar of Companies under section 38D or 342C of the CO.

The CO prospectus regime follows a “document-based” approach, which focuses on the existence of a document containing an offer to the public. Two core prohibitions in the CO prospectus regime concern:

1. the issue of an application form without a prospectus (sections 38(3) and 342(3) of the CO); and
2. the issue of a document containing an offer to the public, or likely to invite offers from the public, where the document does not comply with the requirements for prospectuses in the CO (sections 38(1B) and 342(1) of the CO).

The CO does not define the term “public,” although it does specifically provide that references to offering shares to the public includes offers to “any section of the public, whether selected as ... clients of the person issuing the prospectus or in any other manner.”
**Exempt Offers**

The CO contains the following safe harbors, under which offers of shares and debentures can be made without authorization of a prospectus under the CO:

1. an offer to not more than 50 persons;
2. an offer with a minimum denomination of HK$500,000;
3. an offer with a maximum size of HK$5 million;
4. an offer made only to “professional investors” as defined in Schedule 1 to the SFO (see below);
5. an offer made in connection with an invitation to enter into an underwriting agreement;
6. an offer in compliance with the Takeovers Code;
7. an offer for no consideration or as a dividend alternative;
8. an offer to “qualifying persons,” which includes bona fide current and former directors, employees, consultants of the company, or of another company in the same group, and their respective dependants;
9. an offer of an exchange of shares in the same company not resulting in an increase of the issued share capital; and
10. an offer made in connection with an SFO-authorized collective investment scheme and with authorization under the SFO.

While the above types of offers do not require the offer documents to comply with the prospectus content and registration requirements of the CO, they must nevertheless contain an appropriate warning in the form stipulated by the CO.

---

**WHO QUALIFIES AS A “PROFESSIONAL INVESTOR”??**

Professional investors are defined in Schedule 1 to the SFO to include, among others:

- any individual, either alone or in a joint account with his spouse or children, with a portfolio worth no less than HK$8 million;
- any corporation or partnership with either a portfolio worth no less than HK$8 million or total assets worth no less than HK$40 million;
- any corporate investment vehicle owned by an individual, alone or jointly with his spouse or children, with a portfolio worth no less than HK$8 million;
- any trust corporation with total assets worth no less than HK$40 million;
- any authorized financial institution in Hong Kong or bank regulated outside Hong Kong;
- any intermediary licensed or registered under the SFO or any other person carrying on the business of the provision of investment services regulated outside Hong Kong;
- any authorized insurer in Hong Kong or any other person carrying on insurance business and regulated outside Hong Kong; and
- any authorized collective investment scheme.
PRACTICAL TIP: MAXIMIZING THE SAFE HARBORS

All of the above safe harbors (except exemptions 2 (offers with a minimum denomination of HK$500,000) and 3 (offers with a maximum size of HK$5 million)) may be used in combination with each other, and the entire offer will remain excluded from the prospectus regime.

Note that offers made to persons who are outside Hong Kong are not included in the 50-person limit in exemption 1 above. Hence, an offer may be made to an unlimited number of professional investors and overseas investors (subject to compliance with the applicable rules of the relevant overseas jurisdictions) and up to 50 persons in Hong Kong who do not qualify as professional investors.

CO Content Requirements

The CO prospectus regime also prescribes certain content requirements as set out in Parts II (for companies incorporated in Hong Kong) or XII (for companies incorporated outside Hong Kong) of, and the Third Schedule to, the CO. In addition to the specific disclosure requirements, such as material contracts, valuation reports and accountant’s reports, a prospectus must contain sufficient particulars and information to enable a reasonable person to form a valid and justifiable opinion of the shares or debentures and the financial condition and profitability of the company at the time of the issue of the prospectus.

Registration of the Prospectus

Upon approval of the listing application, a copy of the prospectus is required to be authorized by the Exchange for registration, and registered with the Registrar of Companies, before publication by the issuer. See Chapter 6 of this Guide for details of the registration process.

Prospectus Liability

The CO provides for civil and criminal liabilities for untrue or misleading statements in prospectuses. See Chapter 8 of this Guide for details.

SECURITIES AND FUTURES ORDINANCE

One of the regulatory objectives of the SFO is to provide protection for the investing public.

Section 103 of the SFO makes it an offense for a person to issue, or possess for the purpose of issue, in any place any advertisement, invitation or document (“advertisement”) which, to the person’s knowledge, is or contains an invitation to the Hong Kong public to enter into or offer to enter into an agreement to deal in securities, subject to certain exceptions including:

- a prospectus that complies with or is exempt from compliance with the CO (this avoids duplication with the CO prospectus regime); or
• an advertisement of securities that are (or are intended to be) disposed of only to professional investors, or only to persons outside Hong Kong; or
• where the Securities and Futures Commission ("SFC") authorizes such issue under section 105 of the SFO.

See Chapter 7 of this Guide for publicity restrictions in connection with a securities offering.

**Liability for Contents**

The SFO prohibits the issue of materially false or misleading information that is likely to induce another person to buy or underwrite securities if the issuing person knows or is reckless as to whether the information is false or misleading. The SFO also provides for civil and criminal liabilities for false or misleading statements in prospectuses. See Chapter 8 of this Guide for details.

**Market Misconduct**

The SFO creates a mutually exclusive dual civil and criminal regime for market misconduct through which civil offenses are generally referred to the Market Misconduct Tribunal ("MMT") and more serious misconduct to the criminal courts.

Under section 213 of the SFO, the SFC can apply to the Court of First Instance for a variety of orders, including injunctions and remedial orders, to void a transaction or provide restitution where there has been market misconduct.

In June 2012, the Court of First Instance granted orders under section 213 of the SFO requiring Hontex International Holdings Company Limited to make a repurchase offer totaling approximately HK$1 billion to its current public shareholders as a result of its false and misleading prospectus. This was the first time a share repurchase order had been made against a Hong Kong-listed corporation as a result of market misconduct.

**LISTING RULES**

The Listing Rules of the Exchange contain requirements which have to be met before securities may be listed, as well as certain continuing obligations which an issuer must comply with after listing has been granted. The Listing Rules, as contractual obligations that listed companies undertake to the Exchange to fulfill, do not have the force of statute and do not provide the Exchange with statutory regulatory powers. See Chapter 6 of this Guide for the general principals of the Listing Rules.
SECURITIES AND FUTURES (STOCK MARKET LISTING) RULES

The statutory regulator is the SFC. Under a dual-filing regime established by the above rules, the Exchange passes to the SFC copies of materials submitted by listing applicants and listed issuers, and they are treated as having been submitted to the SFC by the applicant/issuer. Through this dual-filing arrangement, the SFC is able to exercise its statutory powers of investigation in respect of persons whom it suspects of knowingly or recklessly providing false or misleading information in statutory filings with the SFC.

CODES OF CONDUCT

The SFC has published various non-statutory codes regarding its supervision of securities professionals licensed by it. Brief summaries of the main codes follow.

**Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission**

This SFC Code of Conduct applies to all licensed or registered persons and sets out both general principles and specific requirements to be observed by them in conducting their regulated activities. These are mainly directed at providing ethical and responsible services to clients. The SFC applies this code in considering whether its licensees remain “fit and proper,” as required. In doing so, the SFC considers their levels of responsibility within their firms, any supervisory duties they may perform and the levels of control or knowledge they may have concerning any failure by their firms or persons under their supervision to follow the SFC Code of Conduct.

**Corporate Finance Adviser Code of Conduct**

This CFA Code is an additional benchmark to measure a corporate finance adviser’s fitness and properness. Among other provisions, it includes specific requirements on the management of IPOs and other transactions involving publication of documents. Breaches may result in disciplinary or other actions by the SFC.

**Fit and Proper Guidelines**

These Sponsor Guidelines, and others which amplify them, set out specific, continuing requirements on the qualities of SFC licensees (as opposed to their conduct), including competence requirements for sponsors, as well as the responsibilities of sponsors’ management and principals.
B. PRINCIPAL REGULATORS

THE EXCHANGE AND THE LISTING DIVISION

The Exchange is the frontline regulator of stock market participants, in respect of trading matters, and of companies listed on the Main Board and the Growth Enterprise Market ("GEM") of the Exchange.

The Listing Division of the Exchange is responsible for supervising the listing process and the ongoing compliance by issuers with their obligations under the Listing Rules, subject to the review of the Listing Committee under procedures set out in the Listing Rules.

The Listing Division is made up of the following departments:

**Listing Division**

- **IPO Transactions**
  - Process applications for new equity listings, including transactions by listed companies deemed to be new listings
  - Handle pre-IPO inquiries

- **Compliance & Monitoring**
  - Monitor compliance with continuing obligations by listed companies
  - Process applications for listing of further equity and debt issues

- **Listing Enforcement**
  - Investigate possible breaches of the Listing Rules
  - Conduct disciplinary proceedings

- **Listing Policy, Secretariat Services & Support**
  - Provide advice, training and technical support
  - Coordinate policy initiatives and developments
  - Draft policy consultation papers and Listing Rule amendments
  - Manage the operations supporting issuers' public disclosure filings

- **Listing Operations**

- **Policy Framework & Strategy**
  - Responsible for principle-based review of the Listing Rules
  - Develop listing policy proposals
  - Identify regulatory gaps and propose enhancements to the listing regime
THE LISTING COMMITTEE

The Listing Committee acts as both an independent administrative decision maker and an advisory body for the Exchange. It has four principal functions:

- to oversee the Listing Division;
- to provide policy advice to the Listing Division on listing matters and to approve amendments to the Listing Rules;
- to approve listing applications, cancellations of listings and disciplinary matters; and
- to act as a review body (in its role as the Listing (Review) Committee) for decisions made by the Listing Division and by the Listing Committee.

Decisions of the Listing Committee, particularly in a policy context, often have an operational impact for the Listing Division. For each decision to be made by the Listing Committee, the Listing Division will make a recommendation and prepare a report with suitable analysis to assist committee members in reaching an informed decision.

THE SECURITIES AND FUTURES COMMISSION

The principal regulator of Hong Kong’s securities and futures markets is the SFC, which is an independent statutory body established in 1989.

Its regulatory objectives as set out in the SFO are:

- to maintain and promote the fairness, efficiency, competitiveness, transparency and orderliness of the securities and futures industry;
- to promote public understanding of the operation and functioning of the securities and futures industry;
- to provide protection for members of the public investing in or holding financial products;
- to minimize crime and misconduct in the securities and futures industry;
- to reduce systemic risks in the securities and futures industry; and
- to assist the Financial Secretary in maintaining the financial stability of Hong Kong by taking appropriate steps in relation to the securities and futures industry.

The SFC’s Corporate Finance division handles dual-filing functions in relation to listing matters, oversees the Exchange and administers the Takeovers Code, as well as securities and company legislation relating to listed and unlisted companies. Licensed intermediaries are overseen by the Intermediaries Supervision department. The Enforcement Division investigates market misconduct and institutes disciplinary procedures for misconduct by licensed intermediaries.
KEY REQUIREMENTS FOR A LISTING IN HONG KONG

A. SUMMARY OF KEY MAIN BOARD LISTING REQUIREMENTS

Chapter 8 of the Listing Rules sets out the basic qualifications which have to be met as a prerequisite for the listing of equity securities on the Main Board of the Exchange. Potential new applicants are encouraged to contact the Exchange for confidential advice prior to submitting a listing application, in order to avoid incurring unnecessary expenditure when it is clear that they will not be able to meet these requirements. The key listing requirements for the Main Board and GEM are set out below.

QUALIFICATIONS FOR LISTING

<table>
<thead>
<tr>
<th>Suitability for listing (Listing Rule 8.04)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Both the issuer and its business must, in the opinion of the Exchange, be suitable for listing. An issuer or its group (other than a Chapter 21 investment company) whose assets consist wholly or substantially of cash or short-dated securities will not normally be regarded as suitable for listing (Listing Rule 8.05C).</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Financial Criteria (Listing Rule 8.05)</th>
<th>An issuer must satisfy one of the following standards:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit Attributable to Shareholders</td>
<td>At least HK$50 million in the last three financial years (with profits of at least HK$20 million recorded in the most recent year and aggregate profits of at least HK$30 million recorded in the prior two years)</td>
</tr>
<tr>
<td>Market Capitalization</td>
<td>At least HK$200 million at the time of listing</td>
</tr>
<tr>
<td>Revenue</td>
<td>---</td>
</tr>
<tr>
<td>Cash Flow</td>
<td>---</td>
</tr>
</tbody>
</table>

1. Factors which may affect suitability for listing include heavy reliance on transactions with closely related persons (Listing Decision LD92-1) and serious incidents of regulatory noncompliance (Listing Decision LD97-1).
A trading record of at least three financial years is required, with:

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

**Management Continuity**

The Exchange ordinarily considers management continuity under Listing Rule 8.05(1)(b) and Practice Note 3 to be a question of fact. Paragraph 4 of Practice Note 3 sets out the factors the Exchange will take into account where the company has acquired new businesses during the track record period.

The management continuity requirement is primarily aimed at allowing the Exchange to assess the management’s ability to manage the issuer’s business and likely performance of that business in the future.

As set out in Listing Decision LD45-1, the Exchange concentrates on the substance of the management, particularly considering whether:

- an identifiable group of individuals most relevant and responsible for the track record results of a listing applicant remained in positions of responsibility with the enterprise under review throughout the relevant track record period; and
- such group of individuals would form the core management of the applicant at the time of listing and thereafter.

In this respect, the Exchange will ordinarily attribute proportionately greater responsibility to officers with more senior positions than those with more junior positions.
In Listing Decision LD54-2, where the management function was largely vested in one dominant director throughout the track record period, the Exchange’s review therefore involved an assessment of the demonstrated importance of the responsibilities of such director with respect to the business operations of the group and whether, on the facts presented, the contributions from such director had been proved to have continued throughout the track record period and up to the time of listing.

Ownership Continuity and Control

The requirement for ownership continuity and control is aimed at preventing listing applicants from “packaging” their businesses so as to meet the profit record requirement. The Exchange defines “ownership continuity and control” as the continuous ownership and control of the voting rights attaching to their shares by:

- a controlling shareholder; or
- where there is no controlling shareholder, the single largest shareholder; or
- a group of individual shareholders aggregating their shareholding interests and control where they can, on the facts, be regarded as a controlling group for the purposes of the Listing Rules (Listing Decision LD44-4).

In Listing Decision LD51-4, where there were two separate groups of controlling shareholders, the Exchange determined that:

- the two separate groups of controlling shareholders could be viewed as the controlling shareholders that exerted management influence on the operations of the company for the purposes of Listing Rule 8.05(1)(c);
- as such, the management influence exerted by the controlling shareholders had, in fact, not been changed during the last financial year of the track record period; and
- given that both relevant shareholder groups had continued as controlling shareholders during the relevant time periods, the Exchange considered that the company satisfied the ownership continuity and control requirement of Listing Rule 8.05(1)(c).
| **Relaxation of Operating History and Management Requirement**  
**Listing Rules 8.05A and 8.05B)** | The Exchange may accept a shorter trading record and/or waive or vary the operating history and management requirement for:  
- applicants applying under the Market Cap/Revenue test when the new applicants’ directors and management have sufficient and satisfactory experience of at least three years in the line of business and industry of the applicant and the new applicant has management continuity for the most recent audited financial year;  
- mineral companies; and  
- newly formed “project” companies.  
Guidance Letter GL22-10 (October 2010) provides guidance on applications for waiver of the financial standard requirements of Listing Rule 8.05 under Listing Rule 18.04 for mineral companies. Please refer to Chapter 9 of this Guide for more details. |
|---|---|
| **Latest Financial Accounts**  
**Listing Rule 8.06** | The latest reported financial period must not have ended more than six months before the date of the prospectus. |
| **Sufficient Public Interest**  
**Listing Rule 8.07** | The Exchange must be satisfied that there will be sufficient public interest in the company. |
| **Minimum Public Float**  
**Listing Rule 8.08** | At least 25% of the issuer’s total issued share capital must at all times be held by the public. Where expected market capitalization is over HK$10 billion at the time of listing, the Exchange may accept a lower percentage of between 15% and 25%.  
Where there is more than one class of securities, the class of securities to be listed must not be less than 15% of the issuer’s total issued share capital, with an expected market capitalization at the time of listing of not less than HK$50 million.  
**Definition of “Public” (Listing Rule 8.24)**  
The following persons will not be recognized as members of the “public” for the purpose of calculating the public float:  
- any connected person of the issuer;  
- any person whose acquisition of securities has been financed by a connected person; and  
- any person who is accustomed to taking instructions from a connected person relating to the acquisition, disposition and voting of securities of the issuer held by him. |
<table>
<thead>
<tr>
<th><strong>Minimum Public Float (Listing Rule 8.08) continued</strong></th>
<th><strong>Spread of Shareholders</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>At least 300 public shareholders are required, and 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.</td>
<td></td>
</tr>
</tbody>
</table>

| **Minimum Market Capitalization (Listing Rule 8.09)** | **At least HK$200 million at the time of listing, of which at least HK$50 million must be held by the public.** |

| **Competing Business (Listing Rule 8.10)** | **Competing businesses of directors and controlling shareholders are allowed, provided that full disclosure is made at the time of listing and on an ongoing basis. However, in extreme cases where the Exchange believes there are inadequate arrangements to manage conflicts of interest and delineation of businesses between the applicant and other businesses under common control, the Exchange will consider the impact on the applicant’s suitability for listing. Please refer to Chapter 9 of this Guide for more details.** |

| **Voting Power of Shares (Listing Rule 8.11)** | **The share capital must not include shares of which the proposed voting power does not bear a reasonable relationship to their equity interest when fully paid.** |

| **Sufficient Management Presence (Listing Rule 8.12)** | **Unless waived by the Exchange, at least two of the executive directors must be ordinarily resident in Hong Kong. Guidance Letter GL9-09 (July 2009) sets out the conditions for such a waiver.** |

| **Transferability (Listing Rule 8.13)** | **Shares for which listing is sought must be freely transferable.** |

| **Directors’ Qualifications and Board Requirements (Listing Rule 8.15)** | **Every director must satisfy the requirements of Chapter 3 of the Listing Rules, and in particular:** |
| | • satisfy the Exchange that he has the character, experience and integrity and is able to demonstrate a standard of competence commensurate with his position as a director of a listed issuer; and |
| | • satisfy the required levels of skill, care and diligence. Please refer to Chapter 10 of this Guide for more details.** |

**Independent Non-Executive Directors (Listing Rule 3.10)**

Independent non-executive directors (“INEDs”) must represent at least one-third of the directors from December 31, 2012 (until then, the board must have at least three INEDs), and at least one of them must have appropriate professional qualifications or accounting or related financial management expertise.
ACCEPTABLE OVERSEAS JURISDICTIONS

The Hong Kong listing regime is open to both local and overseas issuers. Chapter 19 of the Listing Rules provides the general framework applicable to all overseas companies seeking a listing on the Exchange.

Companies seeking a primary listing in Hong Kong are assessed on a case-by-case basis and have to show they are subject to appropriate standards of shareholder protection, which are at least equivalent to those required under Hong Kong law. A schedule of key shareholder protection matters is set out in a Joint Policy Statement of the Exchange and the SFC dated March 7, 2007, to help applicants in providing submissions to show they are subject to appropriate measures. See Chapter 9 of this Guide for details.

Guidance Letter GL12-09 (September 2009) sets out streamlined vetting practices for listing overseas companies. In particular, the Exchange adopts a purposive interpretation of the shareholder protection equivalence requirement and does not rigidly require issuers to change their constitutional documents. Additionally, the Exchange allows second comers to ride on a first issuer’s arrangements, as well as to cross-benchmark to accepted jurisdictions in order to demonstrate the acceptability of a new jurisdiction.

ACCOUNTING STANDARDS

A listing applicant’s accounts must be prepared in accordance with one of the following standards (Listing Rule 4.11):

- Hong Kong Financial Reporting Standards;
- International Financial Reporting Standards; or

An applicant must apply one of these standards consistently and not change from one body of standards to another. Where the Exchange allows a report to be drawn up otherwise than in conformity with these standards, the report will be required to conform with accounting standards acceptable to the Exchange. In such cases, the Exchange will normally require the report to contain a statement of the financial effect of the material differences (if any) from the standards set forth above.

B. SUMMARY OF GEM LISTING REQUIREMENTS

A GEM listing applicant must satisfy the following listing criteria:

- a market capitalization of at least HK$100 million at the time of listing (GEM Rule 11.23(6));
- a positive cash flow from operating activities of at least HK$20 million in the aggregate for the two financial years before listing (GEM Rule 11.12A);
- a trading record of at least two financial years, with management continuity in the two financial years before listing and ownership continuity and control in the full financial year before listing (GEM Rule 11.12A); and
- at least 25% of the issuer’s total issued share capital, subject to a minimum of HK$30 million, must at all times be held by the public (GEM Rule 11.23).

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

- natural resources exploitation companies (GEM Rule 11.14(2)) or
- newly formed “project” companies (GEM Rule 11.14(1)),

provided that the applicant must nevertheless meet the cash flow requirement of HK$20 million for that shorter trading record period (GEM Rule 11.14).
CHAPTER 4

PRE-IPO PREPARATION

In preparing for an IPO, companies generally undertake a comprehensive review of their financial, legal and business processes and corporate structures in order to meet public market expectations. This may include, to name a few, streamlining and restructuring the corporate structure of the group, strengthening corporate governance and internal controls, establishing efficient tax structures and reporting and introducing strategic investors.

A. CORPORATE RESTRUCTURING

The restructuring steps undertaken in preparation for an IPO will vary, depending on the existing and intended group structure. One of the key steps is determining the jurisdiction of incorporation of the listing entity. The jurisdictions recognized under the Listing Rules are Hong Kong, the PRC, Bermuda and the Cayman Islands, but the Exchange has accepted many other jurisdictions in recent years and publishes a list of acceptable overseas jurisdictions on a timely basis on its website. Please refer to Chapter 9 of this Guide for a list of acceptable overseas jurisdictions and an explanation of the streamlined vetting practices for listing overseas companies.

It is also essential to ensure that the listing group will hold all assets, intellectual property and contractual rights necessary to carry on a focused line of business operations, in addition to complying with the track record and other requirements under the Listing Rules. Part of the group restructuring may involve the transfer of certain assets that are currently held by related parties outside of the group. More significantly, a company should consider whether the inclusion or exclusion of certain businesses may positively or negatively affect its equity story and, hence, the ability to market the IPO.

PRACTICAL TIP: IDENTIFY PRC REGULATORY ISSUES EARLY

All corporate reorganization steps should ideally be completed prior to the A1 submission to the Exchange. Various approvals and confirmations from PRC regulators and bureaus may be required for a successful restructuring of PRC businesses for the IPO. These approvals and confirmations may require extensive documentary submissions and often take time to obtain, particularly where there are incidents of noncompliance and rectification measures are required. Hence, it is important to undertake a comprehensive review of the business early on, and identify any PRC regulatory issues in advance in order to minimize the impact on the timing of the IPO.
CONSIDERATIONS FOR REORGANIZATION

Set forth below are several typical regulatory and legal considerations relevant to a pre-IPO corporate restructuring:

<table>
<thead>
<tr>
<th><strong>Assets and material contracts</strong></th>
<th>A listing applicant should ensure that it has good title to all assets necessary to carry on its business operations. This includes securing or registering material intellectual property rights. In addition, material contracts should be properly documented, valid and enforceable.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Acquisitions of new businesses</strong></td>
<td>If a company acquires a new business that forms a material part of the company’s existing business, materially contributes to its profits or is dissimilar to its previous business activities, the Exchange may take the view that the company’s track record for purposes of the three-year track record requirement begins from the date of the acquisition. This may delay the listing until the company is able to satisfy the three-year track record period (i.e., from the date of acquisition of the new business).</td>
</tr>
<tr>
<td><strong>Competing business</strong></td>
<td>A listing applicant that has a controlling shareholder or director with a competing or potentially competing business will have to demonstrate to the Exchange that it is capable of carrying on business independently of, and at arm’s length from, the excluded business. See Chapter 9 of this Guide for a discussion on competition with controlling shareholders/directors.</td>
</tr>
<tr>
<td><strong>Spin-offs</strong></td>
<td>The Listing Committee will not normally consider a spin-off application within three years of the date of listing of the parent company because the original listing will have been approved on the basis of the portfolio of businesses at the time of listing and an expectation that the company would continue to develop those businesses. Accordingly, a listing applicant may wish to spin off any such assets prior to listing.</td>
</tr>
<tr>
<td><strong>Employment contracts</strong></td>
<td>The company should enter into employment and service agreements with its directors, key employees, officers and consultants that contain, <em>inter alia</em>, confidentiality obligations, noncompetition clauses and grounds for termination.</td>
</tr>
<tr>
<td><strong>Share option schemes</strong></td>
<td>It is not unusual for a listing applicant to adopt a pre-IPO option plan to reward its current employees for their past contribution to the success of the business and, at the same time, to serve as an employment retention tool for key employees. Pre-IPO option plans also offer more discretion on the option exercise price, as well as the category of grantees entitled to participate in the option plan. The requirements in the Listing Rules with respect to share option schemes apply only to option schemes that will continue to be effective post-IPO. See Chapter 9 of this Guide for a discussion on share option schemes.</td>
</tr>
</tbody>
</table>
B. STRATEGIC INVESTORS AND PRE-IPO PLACINGS

Listing applicants and their controlling shareholders may engage in certain forms of pre-IPO investments with private equity investors for various purposes, including raising funds for general working capital. However, certain timing requirements apply, and certain types of investor rights are not allowed to continue upon listing. Also, any pre-IPO investment that will result in the pre-IPO investors obtaining shares of a listing applicant at a price other than the IPO price must be disclosed in detail in the prospectus.

FAIR AND EQUAL TREATMENT FOR ALL UNDER LISTING RULE 2.03

While pre-IPO investments shortly before listing are not considered to be objectionable, any preferential investment terms that extend beyond the listing and are available only to pre-IPO investors will be deemed inconsistent with the principles under Listing Rule 2.03 (i.e., that all holders of listed securities are to be treated fairly and equally) and will be required to be amended so as to be consistent. This is particularly so where the terms of the pre-IPO investment mean that the pre-IPO investors would be protected from certain investment risks in a significantly different way from public investors. See Guidance Letter GL43-12 (October 2012) for details.

TIMING OF PRE-IPO INVESTMENTS (“28/180 DAY REQUIREMENT”)

Except in very exceptional circumstances, the Exchange generally requires (under “Interim Guidance” issued in 2010) that pre-IPO investments must be completed either (a) at least 28 clear days before the date of the first submission of the first listing application form or (b) 180 clear days before the first day of trading of the applicant’s securities. Pre-IPO investments are considered completed when the funds are irrevocably settled and received by the applicant. Where a pre-IPO investment does not comply with the interim guidance, the applicant will be requested to unwind it, adjust the terms of the pre-IPO investment or defer its listing date to six months after the payment date.

Clear days exclude the completion date of the pre-IPO investment, the submission date of the listing application form and the first day of trading of securities.

APPLICATION OF 28/180 DAY REQUIREMENT

Qualified IPOs

Investment agreements with pre-IPO investors often provide that the pre-IPO investors are entitled to compensation if an applicant does not achieve a qualified IPO (i.e., a public offering of securities valued at or above an agreed total amount) within a specified period of time. Such arrangements may be allowed if the amount of compensation is set out in the investment agreement or can be derived from its provisions. Otherwise, the subsequent determination of the amount would be viewed as an amendment or variation to the original terms of the agreement, and the 28/180 Day Requirement would apply, pursuant to Guidance Letter GL43-12 (October 2012). The applicant would then be required to unwind the pre-IPO investment or defer its listing to six months after the compensation amount was determined.
Issue of Securities to Independent Investors by a Secondary Listing Applicant

Applicants with an existing primary listing on a recognized exchange may be able to raise funds from independent investors without observing the 28/180 Day Requirement. As a case in point, a listing applicant with a primary listing on the Australian Stock Exchange (“ASX”) was seeking a secondary listing of the same class of shares on the Exchange and proposed to issue shares and convertible bonds to certain independent investors in order to finance its business operations. The Exchange considered the 28/180 Day Requirement not applicable to these pre-IPO investments, taking into account, *inter alia*, the following factors:

- ASX is an exchange accepted by the Exchange as providing comparable protection to shareholders;
- it is normal for a listed company to enter into financial arrangements, like the proposed pre-IPO investments, to finance its operations;
- shareholders’ approval was required under ASX rules for the pre-IPO investments, and the terms would be fully disclosed to shareholders for approval purposes;
- the pre-IPO Investors were independent third parties;
- the pricing of the shares was based on the prevailing market price of the shares traded on ASX, and there would be no price adjustment after issue;
- the initial conversion price of the convertible bonds represented a premium to the prevailing market price of the shares, although there would be some conversion price adjustments, including, for example, if the Hong Kong IPO price was lower than the market price upon which the initial conversion price was set; and
- the sponsors were satisfied that the pre-IPO investments complied with Listing Rule 2.03 (*Listing Decision LD12-2011*).

Warrant Issue

A listing applicant entered into a loan agreement with independent third parties (“Lenders”), which was conditional on the controlling shareholders issuing to the Lenders warrants to purchase shares in the applicant at a pre-set price. The loan had been fully drawn down more than 28 days before the A1 submission, but the warrants remained exercisable. The Exchange determined that the 28/180 Day Requirement was applicable to the warrant issue, as it took the view that the loan and warrants were separate transactions (and did not view as material the fact that the warrants were issued by the controlling shareholders rather than the applicant). Hence, as the Lenders had not settled the consideration for the shares under the warrants 28 clear days before the A1 submission, the pre-IPO investment in the applicant was not considered completed as the funds were not irrecoverably settled and received by the applicant (*Listing Decision LD15-2011*).
**Treatment of Common Cases**

In order to treat all shareholders fairly and equally, the Exchange does not permit special investor rights to survive upon listing if they are atypical or do not extend to all shareholders. Set out below is a list of special rights commonly granted to pre-IPO investors, and their treatment by the Exchange:

**Special Rights That Can Not Survive upon Listing**

| Price Adjustment Provisions | These provisions effectively create two different prices for the same securities for pre-IPO investors and other shareholders at the time of listing, potentially creating a disruptive effect at that time. Examples include guaranteed discounts to the IPO price or share price, and adjustments linked to the market capitalization of the shares. |
| Put or Exit Options | All put or exit options granted to pre-IPO investors, to put back the investments to the applicant or its controlling shareholder, are against the general principle of even treatment of shareholders, as the pre-IPO investors do not bear any investment risk. This is allowed only if the applicant’s listing does not take place. |
| Director Nomination Rights | Any contractual right of a pre-IPO investor to nominate a director should not survive after listing, as such a right is not generally available to other shareholders. However, pre-IPO investors may nominate or appoint a director to the board before the applicant’s listing. That director would be subject to the retirement and re-appointment requirements under the applicant’s articles of association after listing. |
| Veto Rights | Any contractual rights to exercise veto power over the applicant’s major corporate actions (e.g., winding-up, carrying on a new business, or effecting an amalgamation or merger) should be terminated upon listing. |
| Antidilution Rights | Anti dilution rights should be extinguished upon listing, to comply with Listing Rule 13.36 on pre emptive rights. However, exercise of these antidilution rights by the pre-IPO investors is permissible at the time of the listing when:  
  - the allocation is necessary to give effect to the pre existing contractual rights of the pre-IPO investors under the relevant investor rights agreement;  
  - full disclosure of the preexisting contractual entitlement of the pre-IPO investors, and the number of shares to be subscribed by them, will be made in the prospectus and the allotment results announcement; and  
  - the proposed subscription will be conducted at the IPO offer price. |
| Profit Guarantee | A profit guarantee is disallowed if it is settled by the applicant or if the compensation is linked to the market price or market capitalization of the shares. |
### Special Rights Allowed to Survive upon Listing

| Negative Pledges | To survive upon listing, any negative pledges: (a) must be widely accepted provisions in loan agreements; (b) must not be egregious; and (c) must not contravene the fairness principle in the Listing Rules. Widely accepted provisions include:  
- not to create or effect any mortgage, charge, pledge, lien or other security interest on an applicant’s assets and revenues; and  
- not to dispose of any interest in the economic rights or entitlements of a share the controlling shareholder owns or controls to any person. The Exchange will review all other negative pledges and may require confirmation from the sponsor that those that remain after listing are in line with normal terms of debt issues. |
| Prior Consent for Corporate Actions | The applicant must be able to demonstrate that the relevant terms are not egregious and do not contravene fundamental principles to the disadvantage of other shareholders (as well as not amounting to veto rights falling within the prohibition noted above). |
| Exclusivity Rights and No More Favorable Terms | These rights prevent an applicant from issuing or offering securities or other rights to a pre-IPO investor’s direct competitor, or to other third parties on more favorable terms than those granted to the pre-IPO investor. Such rights can survive after listing if the investment agreement is modified to include an explicit “fiduciary out” clause, which allows directors to ignore the terms if complying with the terms would constitute a breach of their fiduciary duties. This avoids the directors being prevented from exercising their judgment on whether to undertake corporate actions in the best interest of the applicant. |
| Information Rights | Information rights can survive after listing only if the pre-IPO investor is entitled to receive only published information or information that is at the same time made available to the general public, so as to avoid unequal dissemination of information. If the issuer provides price-sensitive information to the pre-IPO investor, the issuer needs to comply with the disclosure requirement under Listing Rule 13.09, unless safe harbors in that rule apply. |
| Representation/Attendance Rights | These contractual rights allow a pre-IPO investor to nominate senior management and committee representatives, but any such appointment is subject to the decision of the board. The board of directors is not contractually obligated to approve a pre-IPO investor’s nominations without further review, as they owe fiduciary duties to all the shareholders. |
| Right of First Refusal and Tag-along Rights Granted by Controlling Shareholder | The Exchange considers that these rights, which intend to protect the pre-IPO investor’s interest in the applicant by limiting the controlling shareholder’s freedom to sell its shares to other parties, are purely contractual rights between two shareholders. |
In relation to pre-IPO investments in convertible instruments (i.e., convertible or exchangeable bonds, notes or loans and convertible preference shares (collectively, “CBs”)), the Exchange clarified its practices in Guidance Letter GL44-12 (October 2012):

<table>
<thead>
<tr>
<th><strong>Convertible Instruments</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Conversion Price</strong></td>
</tr>
<tr>
<td><strong>Linked to IPO</strong></td>
</tr>
<tr>
<td><strong>Price or Market Capitalization</strong></td>
</tr>
<tr>
<td>The conversion price for the CBs should be at a fixed dollar amount or at the IPO price. If the CBs will be converted into shares at a price based on a guaranteed discount to the applicant’s IPO price or the conversion is linked to market capitalization, this essentially creates two different prices for the same securities at listing, which is inconsistent with the principles of the Listing Rules. A discount to the applicant’s IPO price or any linkage to the market capitalization of shares may also give rise to concerns that the pre-IPO investor does not bear the same investment risk as public investors.</td>
</tr>
<tr>
<td><strong>Conversion Price Reset</strong></td>
</tr>
<tr>
<td>Any conversion price reset mechanisms of the CBs should be removed as they are considered to be contrary to the “fair and equal treatment” principle under Listing Rule 2.03.</td>
</tr>
<tr>
<td><strong>Mandatory or Partial Conversions</strong></td>
</tr>
<tr>
<td>Partial conversion of CBs is allowed only if all atypical special rights are terminated after listing. This prevents a pre-IPO investor from enjoying the special rights it held as bondholder by converting a significant portion of its CBs into shares and yet still being entitled to special rights by holding a small portion of the CBs.</td>
</tr>
<tr>
<td><strong>Redemptions and Early Redemptions</strong></td>
</tr>
<tr>
<td>Certain CBs give bondholders an option to redeem the outstanding CBs early at a price that would enable the bondholders to receive a fixed internal rate of return on the principal amount of the CBs being redeemed. Such early redemption is allowed and should be distinguished from other cases in which the bondholders do not undertake any risk and the investment money is not yet paid.</td>
</tr>
<tr>
<td><strong>Disclosure Requirements</strong></td>
</tr>
<tr>
<td>Certain prescribed information must be disclosed in the “Financial Information” and “Risk Factors” sections of the prospectus to explain the impact of the CBs on the applicant, including if the applicant was called upon to redeem the CBs before the maturity date. Certain additional information should also be disclosed in the applicant’s interim and annual reports to make investors aware of the dilutive impact on the applicant’s shares in the event that all outstanding CBs were converted as at the relevant year end or period end.</td>
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</table>
LOCKUPS

Listing Rule 10.07 imposes a lockup on the disposal of any shares by the controlling shareholders for a period of six months from the date of listing, and for a further period of six months on any disposal of shares that would result in such persons ceasing to be controlling shareholders of the company. The lockup restriction includes the obligation not to create any options, rights, interests or encumbrances with respect to the relevant shares. In practice, a sponsor would also customarily expect a lockup undertaking from substantial shareholders for a period of six months from the date of listing.

Pre-IPO investors are usually requested by the applicant to lockup their pre-IPO shares for a period of six months or more. These shares are counted as part of the public float so long as Listing Rule 8.24 is fulfilled (i.e., the shares are not financed directly or indirectly by a connected person of the applicant).

CONNECTED PERSONS

A pre-IPO investor will typically ensure that its shareholding after the IPO will be less than 10% of the shares of the issuer, to avoid becoming a connected person of the issuer, and therefore needing to comply with the connected transaction rules in Chapter 14A of the Listing Rules. In addition, shares held by connected persons do not count toward the minimum public float. See Chapter 9 of this Guide for a discussion of connected persons.

C. SELECTING A SPONSOR AND UNDERWRITER

SELECTION OF A SPONSOR

Every new application for listing must be sponsored. Each sponsor is required to demonstrate to the Exchange its independence or lack of independence from the date of submission of a listing application to the Exchange up to the date of listing. At least one sponsor must be independent of the listing applicant. Listing Rule 3A.07 sets out a series of tests under which a sponsor would not be considered independent, as described below.

Note that the tests do not require complete independence:

- A sponsor group (defined below) may not hold more than 5% of the applicant's shares, if such shareholding interest does not exceed 15% of the sponsor’s net equity.
- Up to 15% of the net proceeds from the IPO may be used to settle applicant debts due to the sponsor group.
- An issuer may be indebted to (or guaranteed by) a sponsor group in an amount up to 30% of the applicant’s total assets, provided that this amount does not exceed 10% of the total assets of the sponsor’s ultimate holding company (or when there is no ultimate holding company, the sponsor).

1. In a consultation paper on the regulation of sponsors published in May 2012, the SFC proposed that each of the sponsors should be independent of the applicant.
A director (or his associate) of a sponsor or any of the sponsor’s holding companies may not directly or indirectly have shareholdings of more than HK$5 million in the applicant.

An employee or director (or his associate) of a sponsor who is directly engaged in providing sponsorship services to the applicant may not hold shares or beneficial interest in the applicant.

A current business relationship may not exist between any of the sponsor group, the applicant and their related parties that could reasonably give rise to a perception that the sponsor’s independence would be affected, except where that relationship arises for the purpose of providing sponsorship services.

For these purposes, the sponsor group means the sponsor, any holding company of the sponsor, any subsidiary of any holding company of the sponsor, any controlling shareholder of the sponsor or any holding company of the sponsor, and any “associate” of any such controlling shareholder (Listing Rule 3A.01(9)).

**SELECTION OF UNDERWRITERS**

Listing Rule 7.03 states that an offer for subscription must be fully underwritten. To comply with this requirement, a listing applicant would typically enter into an underwriting agreement for each of the Hong Kong public offer and the placing tranche. See Chapter 6 of this Guide for details on underwriting arrangements.

Some of the typical considerations when choosing underwriters are:

- **Industry Experience**: Underwriters who have successfully placed stock of companies of a similar size, stage of development and industry may be more likely to have relationships with investors interested in buying the shares of the listing applicant.

- **Quality and Reputation of its Research Arm**: A good research analyst may help position the company properly and reduce volatility by setting realistic expectations for performance.

- **Individual Bankers**: The management of the listing applicant should have a certain amount of rapport with the individual bankers assigned to the transaction.

- **Distribution Strength**: Some underwriters cater primarily to institutional clients, while others appeal primarily to individual retail investors. Targeted investors, geographies and proceeds may be relevant factors.

- **Aftermarket Support**: The aftermarket price performance record of companies recently taken public by an underwriter may be indicative of how well it priced previous transactions.
Staging a successful IPO typically involves expert direction and assistance from a team of professionals, including a sponsor (or in some cases multiple sponsors), lawyers, auditors, underwriters and various other professional parties. The new applicant should carefully consider the ability, experience and commitment of the working group it appoints, given the importance of the advice and assistance they will provide throughout the process. For this reason, assembling a high-quality team is one of the more important tasks the issuer will undertake at the beginning of the IPO process.

It is also worth noting that both the Exchange and the SFC play a significant part in the IPO vetting and approval process. Keeping in mind the impact they can have on the IPO process is also an important factor when choosing the working group.

### Key Parties

<table>
<thead>
<tr>
<th>Key Parties</th>
<th>Roles and Key Responsibilities</th>
</tr>
</thead>
</table>
| **Board of Directors and Management** | The applicant’s board of directors and its management, usually led by the chief executive officer and chief financial officer, play a critical role in the listing process. In consultation with the sponsor and the company’s legal counsels, they make the major structural and timing decisions affecting the IPO. The directors are collectively, and each director is individually, responsible for the accuracy and completeness of the information contained in the prospectus.  
Key responsibilities include:  
• assisting the working group to understand and describe in the prospectus the business, strategies and strengths, as well as the risk factors, of the listing applicant;  
• providing the working group with information and documents about the company for due diligence, drafting sessions and the prospectus verification process;  
• reviewing the draft prospectus and submissions to the Exchange and the SFC; and  
• making presentations to the financial and investor community during roadshows.  
**Sufficiency of Management Presence**  
Unless waived by the Exchange, at least two of the executive directors must be ordinarily resident in Hong Kong (*Listing Rule 8.12*). |
### Board of Directors and Management continued

**Independent Non-Executive Directors**

With effect from December 31, 2012, an issuer must appoint INEDs representing at least one-third of the board (Listing Rule 3.10A). Until then, the board must have at least three INEDs. At least one of the INEDs must have appropriate professional qualifications, or accounting or related financial management expertise (Listing Rule 3.10).

**Committees**

As discussed in greater detail in Chapter 10 of this Guide, a company that wishes to list on the Exchange will need to comply with various corporate governance and listing standards found in the Listing Rules and the Corporate Governance Code. This includes setting up the following committees of the board of directors:

- audit committee;
- remuneration committee;
- nomination committee; and
- corporate governance committee (optional: corporate governance functions may be managed by the board or delegated to a committee).

### The Sponsor

Every applicant must appoint a sponsor to assist it with its initial application for listing (Listing Rule 3A.02). The Exchange considers the role of sponsor critical in bringing a new applicant to listing, and the sponsor forms an integral part of the IPO assessment process.

Key responsibilities include:

- overall management of the IPO;
- being closely involved in the preparation of the listing documents;
- conducting a due diligence review (under Practice Note 21 to the Listing Rules) on the issuer to ensure that (i) the issuer is suitable for listing and (ii) the prospectus contains sufficient information so that public investors are in a position to form a valid and justifiable opinion on its business and prospects;
- assessing the public’s likely interest in the offer;
- putting in place sufficient arrangements and resources to ensure that the IPO and all ancillary matters are conducted in a fair, timely and orderly manner;
- using reasonable endeavors to address all matters raised by the Exchange in connection with the listing application; and
- accompanying the new applicant to any meetings with the Exchange and attending any other meetings and discussions with the Exchange.
**Independence of Sponsor**

A sponsor’s independence is a question of fact and must be disclosed in the prospectus. At least one sponsor must be independent of the new applicant from the date of submission to the Exchange of a listing application on Form A1 until the date of listing *(Listing Rule 3A.07)*.¹

The sponsor is required to demonstrate its independence to the Exchange under various bright-line tests and must make a statement relating to independence to the Exchange in the form of Appendix 18 of the Listing Rules.

See Chapter 4 of this Guide and the Exchange’s Guidance Letters 2-06 and 4-06 (April 2006) for guidance on assessment of a sponsor’s independence.

For guidance regarding changes in sponsorship (such as replacement, addition, resignation or termination), see Guidance Letter 7-09 (July 2009).

**Conduct of Sponsor**

Sponsors are subject to:

- the SFC Code of Conduct, which sets out overall principles and requirements applicable to the conduct of all licensed and registered persons, to which they must adhere in ensuring that they are fit and proper to remain licensed and registered;
- the CFA Code, which provides specific conduct guidance to corporate finance advisers; and
- the Sponsor Guidelines, which set out continuing compliance requirements, including specific competence requirements for sponsors, as well as the responsibilities of sponsors’ management and principals.

**The Underwriters**

All offers for subscription during an IPO must be fully underwritten *(Listing Rule 7.03)*. Key responsibilities include:

- coordinating the “bookbuilding” process; and
- selling and distributing the securities of the issuer during the offering process.

Generally, the underwriters’ commitment with respect to the IPO can come in two basic forms: soft underwriting and hard underwriting. See Chapter 4 of this Guide for details.

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¹ In a consultation paper on the regulation of sponsors published in May 2012, the SFC proposed that each of the sponsors should be independent of the applicant.
### Legal Advisers to the Issuer

The applicant’s Hong Kong legal advisers represent the applicant’s legal interests throughout the process and provide it with assistance and advice on Hong Kong legal and regulatory requirements.

**Key responsibilities include:**

- advising and guiding the directors throughout the IPO process;
- advising on the corporate structures and steps required to effect any group reorganization;
- drafting and preparing the listing documents;
- assisting the applicant in drafting responses to questions from the Exchange and the SFC;
- reviewing and negotiating the underwriting agreements on behalf of the applicant; and
- drafting lockup agreements.

Most larger IPOs involve a Rule 144A offering to institutional investors in the United States. Accordingly, the applicant would also appoint U.S. legal advisers. Their key responsibility is to provide legal advice to the applicant and to prepare the relevant documentation in relation to U.S. legal and regulatory requirements in the course of the IPO.

Depending on the jurisdiction of incorporation of the applicant and the location of its key operations, other foreign legal counsels may also be retained to provide advice on the legal and regulatory requirements of a particular foreign jurisdiction.

### Legal Advisers to the Sponsor and Underwriters

The sponsor’s and underwriters’ Hong Kong legal advisers provide them with assistance and advice on Hong Kong legal and regulatory matters.

**Key responsibilities include:**

- being involved in gathering and reviewing information about the applicant in order to assist the underwriters in meeting their due diligence obligations under Practice Note 21;
- assisting the sponsor in addressing all matters raised by the Exchange in connection with the listing application;
- drafting and negotiating underwriting agreements on behalf of the sponsor and underwriters;
- negotiating the content of comfort letters with the reporting accountants; and
- leading the prospectus verification process.
### Reporting Accountants
The reporting accountants are primarily responsible for (i) preparing the accountants' report and the unaudited pro forma financial information which will be included in the prospectus and (ii) delivering comfort letters to the sponsor and underwriters in relation to the financial information contained in the prospectus.

They also work closely with the rest of the working group during the company’s preparation of the various financial disclosures in the prospectus, including reviewing and reporting on the applicant’s accounting policies and calculations for the profit forecast, if any.

### Financial Printer
The financial printer is responsible for editing and printing the prospectus and application forms, and usually also coordinates the translation of the prospectus into Chinese.

Typically, printers also provide conference rooms and business services to the working group during the drafting process.

### Property Valuer
The independent property valuer is responsible for determining the valuations of, and providing information on, certain property interests of the applicant for inclusion in the prospectus.

### Internal Control Consultant
The internal control consultant is responsible for conducting internal control reviews of the issuer’s internal control systems and procedures (e.g., accounting and finance) and providing recommendations to enhance the relevant processes. This will assist the sponsor in assessing the applicant’s ability to meet the internal control requirements under the Listing Rules.

### Receiving Banks
The receiving banks are responsible for making available the prospectuses and application forms to the public and processing the applications and monies received.

### Share Registrar and Transfer Agent
During the IPO process, the share registrar and transfer agent maintains the applicant’s register of members in Hong Kong and processes and records any transfers in the applicant’s shares.

### Public Relations Firm
The public relations firm will assist in the strategic marketing and public relations aspects of the IPO to ensure that the issuer is presented to the potential investors in a positive manner. It will also arrange and coordinate presentations and roadshows to be attended by potential investors and assist the applicant and its management in liaising with the press.
<table>
<thead>
<tr>
<th>Other Participants</th>
<th>Company Secretary</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The company secretary plays an important role in the corporate governance of an issuer, particularly in assisting the issuer, as well as its directors, in complying with the Listing Rules and the applicable company laws. See Chapter 10 of this Guide for details.</td>
</tr>
</tbody>
</table>

**Authorized Representatives**

Every listed issuer must appoint two authorized representatives to act at all times as the listed issuer’s principal channel of communication with the Exchange. They must be either two directors or a director and the listed issuer’s secretary, unless the Exchange, in exceptional circumstances, agrees otherwise (Listing Rule 3.05).

**Industry Consultant**

An applicant may wish to commission an industry consultant to provide market research and analysis and prepare an expert report for use in the prospectus.

**Competent Person (for Chapter 18 Mineral Companies)**

A competent person is responsible for preparing the technical and valuation report in relation to a listing applicant’s mining resources and/or reserves in compliance with an applicable reporting standard.

**Compliance Adviser**

A listed issuer must appoint a compliance adviser for the period from the date of listing until the publication of its financial results for the first full financial year following its listing. During this period, the issuer must consult with and, if necessary, seek advice from the compliance adviser in certain circumstances.

*Note:* The Exchange will normally consider directing the appointment of a compliance adviser when a listed issuer has been held to have breached the Listing Rules.

**Depositary**

If the applicant is listing depositary receipts under Chapter 19B of the Listing Rules, it must appoint a depositary as its agent, which must be a suitably authorized and regulated financial institution acceptable to the Exchange.
THE IPO PROCESS

A. METHODS OF LISTING

GENERAL PRINCIPLES

The listing of securities on the Exchange is governed with a view to ensuring that investors have and can maintain confidence in the market, and that:

• applicants are suitable for listing;
• the issue and marketing of securities are conducted in a fair and orderly manner, and potential investors are given sufficient information to enable them to make a properly informed assessment of an issuer;
• investors and the public are kept fully informed by listed issuers, and immediate disclosure is made of any information that might reasonably be expected to have a material effect on market activity in, and the prices of, listed securities;
• all holders of listed securities are treated fairly and equally;
• directors of a listed issuer act in the interests of its shareholders as a whole, particularly where the public represents only a minority of the shareholders; and
• all new issues of equity securities by a listed issuer are first offered to the existing shareholders by way of rights, unless they have agreed otherwise (Listing Rule 2.03).

LISTING METHODS

Securities may be listed in the following ways:

- Offer for Subscription: An offer to the public by, or on behalf of, an issuer of its own securities for subscription.
- Offer for Sale: An offer to the public by, or on behalf of, the holders or allottees of securities already in issue or agreed to be subscribed.
- Placing: The obtaining of subscriptions for, or the sale of securities by, an issuer or intermediary primarily from or to persons selected or approved by the issuer or the intermediary. The Exchange may not permit a new applicant to be listed by way of placing if there is likely to be significant public demand for the securities.
- Listing by Introduction: An application for listing of securities already in issue where no marketing arrangements are required. Introduction is typically used when the securities for which listing is sought are already listed on another stock exchange.
PRIMARY AND SECONDARY LISTINGS

Hong Kong, PRC and overseas issuers from an acceptable jurisdiction may apply for primary listing on the Exchange. Primary listed issuers may trade all their listed equity securities on the Exchange and need to comply fully with the Listing Rules, unless specifically waived.

Secondary listed issuers are primarily listed on another stock exchange, and the majority of their equity securities are not usually traded on the Exchange. Secondary listing is available to overseas issuers, excluding Greater China issuers, seeking a Main Board listing and having sufficient connections with a foreign market.

In determining whether an issuer has sufficient connections with a foreign market to warrant a secondary listing, the Exchange will not only consider the issuer's place of incorporation but also look at other factors to determine its center of gravity, including:

- the number of Hong Kong shareholders;
- the likely extent of equity securities trading on the Exchange;
- the location of the head office and place of central management;
- the location of business and assets with reference to its corporate and tax registration; and
- the protection available to Hong Kong investors under any foreign laws or regulations.

This test is intended to prevent Hong Kong- or PRC-incorporated issuers from circumventing the Listing Rules by taking up a foreign shell.

Stock short names for secondary listings are identifiable by the suffix “S”. New secondary listed companies must disclose, through the Exchange's website upon their listing, the Listing Rule waivers they obtained, their constitutive documents, a summary of applicable laws and regulations and any other information requested by the Exchange. The information should be updated annually.

REVIEW OF THE LISTING RULES FOR SECONDARY LISTED ISSUERS

In practice, secondary listed issuers are granted more Listing Rule waivers. All waivers are considered on their individual merits to balance the legitimate expectations of investors who trade through the Exchange against the burden on issuers of having to comply with two sets of rules, where trading in the related securities is predominantly overseas and listing is primarily on a foreign stock exchange that has acceptable shareholder protection standards.

The Exchange and the SFC are considering proposals to revise the rules for secondary listings. These aim to provide certainty, reduce unnecessary regulatory burden and expense and, at the same time, preserve Hong Kong's reputation for high standards of regulation, investor protection and corporate governance. We expect that they will shortly issue further guidance to clarify the requirements for secondary listed issuers and the waivers available.
**B. LISTING TIMETABLE AND DOCUMENT SUBMISSION**

An IPO typically requires a few months of intensive preparatory work before the A1 submission. Often there are important and interrelated business decisions to be made, and these decisions are rarely decided definitively at the outset. This chart illustrates the various milestones in the IPO process from a sponsor’s perspective.

<table>
<thead>
<tr>
<th>KICK-OFF</th>
<th>PN21 DUE DILIGENCE</th>
<th>VERIFICATION</th>
<th>A1 SUBMISSION</th>
</tr>
</thead>
</table>
| **Hong Kong IPO Sponsor’s Milestones** | Circulate memo on publicity restrictions to all parties¹  
*Listing Rule 9.08* | Review PN21 work plan with counsel³  
*Practice Note 21 of the Listing Rules* | Sponsor’s undertaking  
*Listing Rule 3A.03* |
|  | Review SFC’s information flow requirements for research analysts and discuss with syndicate members and counsel if any additional control measures are required²  
*Guidance Letters GL29-12, GL43-12 and GL44-12* | Document PN21 plan and progress, including any significant deviations | Sponsor’s statement of independence²  
*Listing Rule 3A.08* |
|  | Circulate memo on publicity restrictions to all parties¹  
*Listing Rule 9.08* | Review compliance with pre-IPO investment guidelines⁴  
(if applicable) |  |
|  | Review SFC’s information flow requirements for research analysts and discuss with syndicate members and counsel if any additional control measures are required²  
*Guidance Letters GL29-12, GL43-12 and GL44-12* | Review compliance with pre-IPO investment guidelines⁴  
(if applicable) |  |
| **VETTING PROCESS** | Review working capital and profit forecast prior to submission | Sponsor’s letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* | Sponsor’s confirmation with regard to the posting of WPIP  
*Checklist VI.E* |
|  | Dual-filing regime⁶  
• Responses to regulators’ comments  
• Prospectus drafts  
Continuing due diligence | Submission of executed waiver applications on sponsor’s letterhead | Sponsor’s final letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* |
| **15-DAY SUBMISSION** | Review working capital and profit forecast prior to submission | Sponsor’s letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* | Bring down due diligence |
| **4-DAY SUBMISSION** | Sponsor’s letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* | Review draft research reports and document review process |  |
| **PRE-DEAL RESEARCH** | Sponsor’s letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* | Review draft research reports and document review process |  |
| **BEFORE BULK PRINT** | Sponsor’s letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* | Sponsor’s confirmation with regard to the posting of WPIP  
*Checklist VI.E* |  |
|  | Sponsor’s letter regarding sufficiency of working capital  
*Listing Rule 9.11(19)* | Sponsor’s confirmation with regard to the posting of WPIP  
*Checklist VI.E* |  |
| **AFTER LISTING HEARING** | Sponsor’s declaration on Listing Rules compliance²  
*Listing Rule 3A.13, Appendix 19 of the Listing Rules* | Marketing statement⁶  
*Form D, Appendix 5 of the Listing Rules* | Exercise over-allotment option |
|  | Sponsor’s confirmation with regard to publication of the prospectus on the Exchange website  
*Checklist VII.C* | Sponsor’s declaration on placings and Listing Rules compliance  
*Form E, Appendix 5 of the Listing Rules* | Bring down due diligence |
| **PROSPECTUS REGISTRATION** | Sponsor’s declaration on Listing Rules compliance²  
*Listing Rule 3A.13, Appendix 19 of the Listing Rules* | Sign International Underwriting Agreement, pricing agreement, etc.  
Bring down due diligence | Stabilizing manager to note Disclosure of Interests obligations  
*Part XV of the SFO* |
| **PRICING** | Sign Hong Kong Underwriting Agreement  
Sponsor’s certificate relating to competency of translator  
*Listing Rule 9.11(33)(c)* | Marketing statement⁶  
*Form D, Appendix 5 of the Listing Rules* |  |
| **BEFORE DEALINGS COMMENCE** | Marketing statement⁶  
*Form D, Appendix 5 of the Listing Rules* | Sponsor’s declaration on placings and Listing Rules compliance  
*Form E, Appendix 5 of the Listing Rules* |  |
Notes:

1. In addition to Listing Rule 9.08, see Guidance Letter GL18-10 (June 2010), Guidelines on Use of Offer Awareness and Summary Disclosure Materials in Offerings of Shares and Debentures under the CO issued by the SFC in March 2003, Guidelines for Electronic Public Offerings issued by the SFC in April 2003, sections 38B(1), (2), Nineteenth Schedule of CO (cap. 32) and sections 103(1), (2) and (3) and 105 of SFO (cap. 571).

2. See the SFC Code of Conduct and the CFA Code for details. For a discussion of the pre-deal research rules, see the Consultation Conclusions on the Regulatory Framework for Pre-deal Research published by the SFC in June 2011.

3. Practice Note 21 requires that sponsors conduct reasonable inquiries (“due diligence”) to enable the sponsor to make a declaration under Listing Rule 3A.13 and sets out the Exchange’s expectations of due diligence sponsors will typically perform.

4. See Chapter 4 of this Guide for details on the various guidance letters.

5. Sponsor independence is continuously assessed from the date of the A1 submission up to the date of listing.

6. Section 384 of the SFO: criminal offense to provide false or misleading information knowingly or recklessly to the SFC and the Exchange.

7. Sponsor’s declaration must include the terms of Listing Rules 3A.14 to 3A.16, comprising: (i) confirmation that all requisite documents have been submitted to the Exchange; (ii) due diligence declaration; and (iii) expert sections declaration.

8. Please refer to Chapter 7 and Appendix 6 of the Listing Rules.

THE EXCHANGE’S PRACTICE ON ACCEPTING EARLY FILING OF THE A1

The Exchange will accept an early filing of the A1 if certain conditions set out in Guidance Letter GL6-09 (July 2009) are followed. Applicants should plan their listing timetable to allow the Exchange sufficient time to review the final year-end financials or latest stub-period financials in order not to delay the listing timetable. The Exchange’s conditions for accepting certain types of listing applications filed after the end of the trading record period are summarized below. Note that listing applications filed before the trading record period end will be returned.

<table>
<thead>
<tr>
<th>Filing within 45 days after end of trading record period and unable to include the last financial year figures</th>
<th>Filing within 230 days of latest audited financial statements</th>
<th>Filing over 230 days after date of latest audited financial statements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Applicant must include in its listing application:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• sponsor’s confirmation that, <em>inter alia</em>, it considers beyond a reasonable doubt that the applicant will satisfy Listing Rule 8.05;</td>
<td>• sponsor’s confirmation that, <em>inter alia</em>, it considers beyond a reasonable doubt that the applicant will satisfy Listing Rule 8.05; and</td>
<td>• audited figures for the three financial years and related management discussions; and</td>
</tr>
<tr>
<td>• audited figures for the preceding two financial years and related management discussions; and</td>
<td>• audited figures for three financial years and related management discussions.</td>
<td>• stub-period figures (audited or advanced draft form) no more than six months old at the time of the A1 filing, prior-year stub period comparative figures and related management discussions.</td>
</tr>
<tr>
<td>• stub-period figures (audited or advanced draft form) as of a date within 230 days of the A1 filing application.</td>
<td></td>
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</tr>
</tbody>
</table>
C. DUE DILIGENCE – PN21 AND RULE 10B-5

SPONSOR’S DECLARATION

A significant part of the responsibilities of a sponsor is the due diligence work that it undertakes with respect to a new applicant. Under the Listing Rules, at the time of issue of a listing document, a sponsor is required to conduct reasonable due diligence inquiries in order to make a declaration to the Exchange pursuant to Listing Rule 3A.13 that the listing applicant fulfills all principal listing requirements.

The sponsor’s declaration covers:

- compliance with the qualifications for listing (except to the extent that compliance has been waived);
- sufficiency of particulars and information in the listing document to enable a reasonable person to form a valid and justifiable opinion of the shares and the financial condition and profitability of the applicant;
- the truthfulness of the information in the nonexpert sections of the listing document with no material omissions;
- the establishment of adequate procedures and systems to ensure that the applicant complies with the relevant regulatory requirements and to enable the directors to make a proper assessment of the financial position and prospects of the applicant; and
- the appointment of experienced, qualified and competent directors.

Although the declaration is required to be made at the time of issue of a listing document, the Exchange expects that a sponsor should have completed substantive due diligence at an early stage.

PRACTICE NOTE 21

A summary of the requirements for due diligence under the Listing Rules is set out below.

Requirement to Conduct Due Diligence

Under Listing Rule 3A.12, a sponsor must consider Practice Note 21 of the Listing Rules in determining the reasonable due diligence inquiries it must make. Practice Note 21 sets out the Exchange’s expectations on the due diligence that sponsors will typically perform. It is important to remember that Practice Note 21 is not a set of prescribed minimum procedures that are applicable to all issuers. Each new applicant is unique and so will be the due diligence steps necessary for the purpose of its listing application. The sponsor must exercise its judgment as to what investigations or steps are appropriate for a particular new applicant and the extent of each step.

Sponsors should ensure that their staff are given guidance on the scope of due diligence work, the handling of questionable or doubtful information, conducting due diligence on the listing applicant’s major stakeholders and senior management, documentation standards and record retention.

The Standard of Due Diligence: Professional Skepticism

A sponsor should make such inquiries as are necessary for the sponsor to satisfy itself reasonably in relation to the disclosure in the listing document. In undertaking its role, a sponsor must examine with professional skepticism the accuracy and completeness of statements and representations made,
or other information given to it, by the new applicant or its directors, rather than simply relying on management representations.

An attitude of professional skepticism means making a critical assessment with a questioning mind and being alert to information, including information from experts, that contradicts or brings into question the reliability of such statements, representations and information. Procedurally, the SFC is of the view that it is more effective if the sponsor is the one sending out and receiving the relevant due diligence questionnaires and confirmations, minimizing involvement of the listing applicant to avoid any interception or tainting.

Failure to exercise professional skepticism and any attempt to avoid full disclosure of material information until requisitions or inquiries by the regulators only create inefficiencies and unnecessary delays in the listing process. More importantly, they also reflect negatively on the credibility of the applicant and the sponsor concerned.

**Documenting Due Diligence Planning and Significant Deviations**

Record retention is the key to evidencing the trail of due diligence. The Exchange expects sponsors to document their due diligence planning and significant deviations from their plans. This includes demonstrating that they have considered the question of what inquiries are necessary and reasonably practicable in the context and circumstances of the case.

The SFC is of the view that in a situation where the matter bears some significance, even if a conclusion has been reached that the matter is not sufficiently material to warrant disclosure, the sponsor is expected to document how such a conclusion has been reached. Only then would a sponsor be able to demonstrate that it has considered the question of what due diligence inquiries were necessary in the circumstances. In the absence of any satisfactory documentary proof, the SFC may not be convinced that the sponsor has actually considered the relevant issue and conducted reasonable due diligence on that aspect.

An audit trail should also demonstrate that the sponsor’s management adequately supervised major issues, such as the review of the due diligence plan, the actual due diligence work and its progress pursuant to the plan.

**Third-party Professionals**

Practice Note 21 contemplates that a sponsor may, in appropriate circumstances, engage third-party professionals to assist in undertaking tasks related to certain due diligence inquiries. The sponsor must satisfy itself that it is reasonable to rely on information or advice provided by the third-party professional and should not place uncritical reliance on experts’ work, including accountants’ and valuers’ reports.

A sponsor should satisfy itself that it is reasonable to rely on the expert’s report or opinion, taking into account its own in-depth and wide-ranging knowledge of the listing applicant accumulated since it was first engaged by the applicant, whether formally or informally. If the sponsor has any information (including the history of the applicant, the markets in which it operates and its business model) which may cast doubt on the accuracy and completeness of any expert report, or any information in any expert report is of relevance to the accuracy or completeness of other information relied on by the sponsor in preparing the applicant for listing, it is essential that the sponsor makes further inquiries.
rule 10B-5

In addition to satisfying requirements under the Listing Rules, a sponsor, in its role as global coordinator, may also use due diligence to address potential liabilities under U.S. securities laws, particularly when the listing involves an international offering. See Chapter 11 – “International Offerings.”

More specifically, Rule 10b-5 under the U.S. Exchange Act prohibits any person, in connection with the purchase or sale of a security (whether public or private), from making any untrue statement of a material fact or omitting to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading. In order to be successful in an action under Rule 10b-5, a plaintiff must show, among other things, that the defendant acted with “scienter,” which generally means an intent to deceive, manipulate or defraud or reckless disregard for the truth. Due diligence can be used to refute this “scienter” element of the claim and thus establish a defense against potential 10b-5 liability.

EXAMPLES OF GOOD DUE DILIGENCE

Understanding what constitutes reasonable due diligence inquiries and a reasonable ground for belief, in the context of establishing a defense against liability, turns on understanding what constitutes adequate due diligence. While Practice Note 21 is not a one-size-fits-all shield for sponsors from discipline, the regulators use the Practice Note as part of a post-listing appraisal of whether sponsors have fulfilled their obligations.

The following due diligence actions, among others, are advisable as appropriate:

• interviewing company officers from various departments to explore all aspects of the company’s business;
• contacting major customers, suppliers, distributors, licensees and/or bankers to verify management’s representations;
• inspecting the factory in which the company’s products are manufactured;
• reviewing the internal financial model with the company’s management and inquiring about expected financial results;
• reviewing trade journals and industry-related publications to ascertain industry trends, market trends and competitive information;
subjecting the company’s budget to line-by-line scrutiny;

reviewing material contracts, board minutes and other corporate documents; and

maintaining close involvement of management throughout the prospectus-drafting process.

PRACTICAL TIP: DUE DILIGENCE INTERVIEW PRACTICES

The manner in which due diligence interviews are conducted can directly affect the quality and reliability of information obtained and, to the extent that such information is relied on when preparing the listing documents, undermine the ability of the sponsor (and, in turn, the investors) to properly assess the listing applicant’s financial condition.

In order to ensure that the results of the interviews with major business stakeholders (e.g., customers, suppliers, creditors and bankers) are accurate, complete and reliable, it is important that the sponsor properly plans, manages and carries out the interviews. In order to do so, the sponsor should:

- independently select those to be interviewed based on objective and proportionate criteria (e.g., those with whom the listing applicant has entered into high-value transactions or entities with special or unusual characteristics);
- carry out direct interviews with the selected person or entity with minimal involvement of the listing applicant;
- ascertain the identity of the interviewee to ensure that the interviewee has the appropriate authority and knowledge for the interview;
- hold an in-depth discussion to obtain adequate and satisfactory responses to all questions raised and follow up on any incomplete responses or outstanding matters; and
- identify any irregularities noted during the interview (e.g., reluctance on the part of the interviewee to cooperate) and ensure any irregularities are adequately explained and resolved.

POTENTIAL ISSUES ARISING IN LISTING APPLICATIONS

In its dual-filing updates, the SFC has identified potential issues that may arise in the course of prospectus vetting, some of which occur as a result of inadequate due diligence, including:

- inaccuracy of information and significant errors in listing documents and responses to the regulators;
- failure to demonstrate a basic understanding of the key factors affecting the historical performance of the listing applicant, such as the customer profile and competitive advantages;
- failure to identify and explain relationships of significant stakeholders (such as distributors and suppliers) to the listing applicants;
- failure to identify material noncompliance with rules and regulations;
- critically important statements based on assumptions that conflict with observable facts; and
• failure to provide meaningful disclosures on the risks, historical financial performance and future plans of the company.

D. APPROVAL AND REGISTRATION OF PROSPECTUS

When securities are offered to the “public” in a listing, a prospectus must be prepared in accordance with the requirements of the Listing Rules, the CO and the SFO.

Every application for listing, together with a draft prospectus, should be submitted to the Listing Division for vetting, and the Listing Division may reject or recommend the application. Under the dual-filing regime, the Exchange passes to the SFC copies of materials submitted by listing applicants. The SFC may object to a listing if the disclosure in the listing materials appears to the SFC to contain false or misleading information.

The Exchange’s Listing Committee will consider the application only after the Listing Division has processed it. If the Listing Committee approves a listing, the Listing Division will issue a formal approval letter in due course. The Exchange will then issue an authorization for registration of the prospectus with the Registrar of Companies.

REVIEW PROCESS

The Exchange’s purpose in reviewing a draft prospectus is to ensure adequate disclosure, not to determine the merits of the offering. In other words, the Exchange’s comments and the applicant’s responses to them will focus on whether investors are being provided with sufficient information to “make an informed assessment of the activities, assets and liabilities, financial position, management and prospectus of the issuer and of its profits and losses and of the rights attaching to such securities,” not whether investing in the company at the proposed offering price is a good or bad idea.

Once the applicant’s draft prospectus is filed with the Exchange, it will be assigned to a vetting team from the IPO Department of the Listing Division. The vetting team will review all aspects of the draft prospectus, including the financial statements and accounting-related issues. The sponsor will typically receive the first comment letter around three weeks after the A1 filing.

When the comment letter is received, it should be promptly circulated to the working group. A conference call or meeting should be scheduled for the working group to discuss the comments, the proposed responses and the timing of the response letter. The working group then will prepare amendments to the draft prospectus and a response letter to the Exchange. The response letter will address each comment made by the Exchange. Where the comment letter asks for supplemental information, the response letter will provide it or explain why the information is not available or should not be required. Depending on the extent of the revisions to be made in response to the Exchange’s comments, the working group may or may not convene at the financial printers for a drafting session prior to filing the amendment.

Once the amendment to the draft prospectus and the response letter are filed with the Exchange, the vetting team will review them and provide another comment letter to the sponsor. This process goes through several cycles until the vetting team is satisfied with the disclosure in the draft prospectus. The Exchange will not set a listing hearing date until all outstanding comments have been addressed to its satisfaction.
For disclosure issues that are particularly complex or sensitive, it may be helpful for the sponsor and its counsel to call the vetting team to discuss the matter and the proposed response. Most issues can be resolved during telephone conferences, and it is often helpful to put the applicant’s thoughts on the matter into a short letter that can be faxed to the Exchange in advance of the call.

The Exchange review process will span a few weeks, hence, the working group should consider whether the draft prospectus must be amended to reflect changes that have occurred in the business since the initial filing.

**PRACTICAL TIP: PREPARING FOR LISTING HEARINGS**

The Exchange has started to require sponsors to attend listing hearings in order to answer any questions which the Listing Committee may have. Sponsors should prepare early and thoroughly by ensuring that their principals are involved in and updated regularly on key decisions. The due diligence plan and results should be reviewed at various milestones, and familiarity with the prospectus is crucial.

**REGISTRATION PROCESS**

Upon approval of the listing application, a copy of the prospectus is required to be authorized for registration and registered with the Registrar of Companies before publication.

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<thead>
<tr>
<th>Documents for submission to the Exchange to apply for authorization for registration</th>
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<tr>
<td>• An application for authorization for registration</td>
<td>• A cover letter requesting registration of the prospectus</td>
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<td>• The prospectus duly signed by the directors and the share application forms</td>
<td>• The prospectus duly signed by the directors</td>
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<td>• Any power of attorney pursuant to which the prospectus is signed</td>
<td>• Application forms</td>
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<tr>
<td>• A translation certificate with respect to the Chinese translation of the prospectus and a certificate issued by the sponsor confirming that the translator is competent to give the certificate</td>
<td>• The consent of any expert named in the prospectus</td>
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<td>• Details of any selling shareholders</td>
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<td>• Any statement of adjustments</td>
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<td>• Any statement of adjustments (in connection with the accountants’ report)</td>
<td>• Certified copies of the material contracts referred to in the prospectus</td>
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<td>• A certificate of authorization for registration from the Exchange</td>
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<td>• Requisite fee</td>
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E. UNDERWRITING AND OTHER CONTRACTUAL ARRANGEMENTS

Main Board Listing Rule 7.03 requires that an offer for a public subscription of securities be fully underwritten. Therefore, as part of the IPO process, a listing applicant will typically enter into, among others, two important underwriting agreements: the Hong Kong Underwriting Agreement (the underwriting agreement for the Hong Kong public offer) and the International Underwriting Agreement (the underwriting agreement for the international placement, i.e., any placements outside of Hong Kong). The underwriting arrangements may be “hard” or “soft” as described below, but soft underwriting is generally the norm in Hong Kong IPOs.

SOFT UNDERWRITING

Soft underwriting refers to underwriting arrangements where the underwriters are entitled to terminate the underwriting agreement with immediate effect if any termination event stipulated in the agreement occurs prior to 8:00 a.m. on the day of listing. If the underwriting agreement is terminated, the listing will not proceed.

HARD UNDERWRITING

Occasionally, a listing applicant may enter into a “hard underwriting agreement” where the underwriters agree to commit to purchase a fixed value of shares not taken up under the public offer and/or placing on the condition that the final offer price is fixed at the low end of an indicative offer price range. The listing applicant agrees to pay a fee for the hard underwriting arrangement, in addition to the normal underwriting fees payable under the soft underwriting agreements. Hard underwriting arrangements are usually considered only when the demand for offer shares is expected to be weak, and therefore the listing applicant is willing to pay an extra fee to secure a certain amount of committed underwriting.

HARD UNDERWRITING ARRANGEMENTS REQUIRE DISCLOSURE

In accordance with the principles of Listing Rule 2.13(2), the Exchange requires disclosure of the salient terms of the hard underwriting agreement in the prospectus, including:

- the date of the hard underwriting agreement;
- the amount underwritten;
- the conditions;
- the grounds for termination; and
- the fees.

If the hard underwriting agreement is entered into after the issue of the prospectus, the issuer is required to issue a supplemental prospectus to disclose the above. See Guidance Letter GL34-12 (April 2012) for more details.
OVERVIEW

In tandem with the two underwriting agreements described above, other contractual arrangements will also be entered into, namely the Price Determination Agreement, the Intersyndicate Agreement, the Agreement Among International Underwriters and the Agreement Among Hong Kong Underwriters. The following chart summarizes the interplay among the various contractual arrangements.

HONG KONG UNDERWRITING AGREEMENT

Pursuant to Listing Rule 7.03, the listing applicant will enter into an underwriting agreement with the underwriters for the Hong Kong public offer. The Hong Kong Underwriting Agreement is usually concluded before the prospectus is issued and is one of the material contracts required to be registered and made available for public inspection. In this agreement, the issuer agrees to offer shares for subscription by the Hong Kong public (subject to certain conditions), and the underwriters severally agree to subscribe, or obtain subscribers for, their respective proportions of shares not bought up in the public offer (subject to certain conditions precedent, such as the successful registration of the prospectus and the Exchange’s approval of the listing). In return for these services, the underwriters are paid a commission by the listing applicant.

In addition to laying out these basic obligations on the part of the listing applicant and underwriters, the Hong Kong Underwriting Agreement will include, among other provisions, the processes for the allotment and issue of the public offer, clawback and reallocation provisions, arrangements for the delivery of shares, the payment of the IPO proceeds to the company (minus IPO fees and other commissions), lockup provisions (i.e., an arrangement which restricts the ability of the company and/or majority shareholders to sell any of their shares within a specified period of time after the IPO, in order to ensure that the market is not flooded with the company’s shares) and stabilization provisions (i.e., giving one of the underwriters the ability to take steps to stabilize or maintain the market price of the shares at a level higher than that which might otherwise prevail in the open market for a limited period after the application list closes).
The following are some other key sections in the Hong Kong Underwriting Agreement that often require close attention and negotiation:

**Representations and Warranties**

In this section, the listing applicant and other warrantors give the Hong Kong underwriters numerous representations and warranties covering and confirming, among other things, their legal capacity and authority to enter into the underwriting agreement, the legality of corporate reorganizations undertaken in preparation for the IPO, the truthfulness and accuracy of the prospectus and disclosed financial information, the procurement of all necessary approvals for the IPO, the absence of encumbrances on the marketability of the securities from the selling shareholders (if applicable to the IPO) and the absence (save as disclosed) of any litigation proceedings or indebtedness involving the listing applicant. This section constitutes an important part of the due diligence process in connection with an IPO and can form the basis for the underwriters to refuse to close the IPO transaction if any of the representations or warranties are untrue. Salient terms of the Hong Kong Underwriting Agreement are disclosed in the “Underwriting” section of the prospectus.

**Indemnity**

In this section, the listing applicant and other warrantors agree to indemnify the underwriters from claims, losses and liabilities arising directly or indirectly from, among other things, misstatements or omissions in the prospectus, any breaches or alleged breaches of the law by the listing applicant and warrantors in connection with the IPO, any failure by any of the listing applicant’s directors to comply with the Listing Rules or other applicable laws and inaccuracies in the representations and warranties section of the underwriting agreement.

**Termination**

In this section, events of termination are set out that, if occurring prior to a specified time (generally, prior to 8:00 a.m. on the day of listing), will give the underwriters the opportunity to terminate their obligations under the underwriting agreement. Such events typically include developments both within and outside of the listing applicant’s and/or underwriters’ control, including: any material misstatements or omissions in the prospectus; any material changes to the business affairs, profits or financial position of the listing applicant; rejection of listing by the Exchange; any breach of the warranties in the underwriting agreement; national or international crises and emergencies; adverse macroeconomic changes; and the adoption of new laws or judicial interpretations in various jurisdictions that may affect the IPO.

**AGREEMENT AMONG HONG KONG UNDERWRITERS**

Along with the Hong Kong Underwriting Agreement, the underwriters of the Hong Kong public offer will enter into a contractual agreement among themselves setting forth their own various rights and obligations. The Agreement Among Hong Kong Underwriters typically includes provisions pursuant to which the underwriters give the global coordinator authority and discretion to act on their behalf in managing the public offer shares (such as reallocating shares between the Hong Kong public offer and the international placement) and organizing public advertising activities associated with the IPO. This agreement also contains clauses both allocating the underwriting commissions among the underwriters and providing for certain steps should an underwriter not be able to fulfill its obligations, as well as
representations and warranties among the underwriters.

INTERNATIONAL UNDERWRITING AGREEMENT

For placements to investors other than the Hong Kong public, the listed company and underwriters will enter into an International Underwriting Agreement, usually after the issue of the prospectus and contemporaneous with the price determination date (see below). The basic provisions and overall purpose of the International Underwriting Agreement are generally similar to those of the Hong Kong Underwriting Agreement discussed above. In the International Underwriting Agreement, the international underwriters severally agree to subscribe, or obtain subscribers for, their respective proportions of shares in the international offering (subject to certain conditions, such as the successful registration of the prospectus and the Exchange’s approval of the listing). However, the International Underwriting Agreement will typically contain certain representations and warranties pertaining to U.S. law, and specifically, U.S. exemptions from registration of the international offering shares with the U.S. SEC. For example, the international underwriters will typically warrant that they are “qualified institutional buyers” under Rule 144A and that they have not undertaken any “directed selling efforts” as prohibited by Regulation S. On the other side, the listing applicant and warrantors will typically undertake, among other things, that they will remain in compliance with U.S. legal requirements on the sale of restricted securities after the IPO is concluded.

AGREEMENT AMONG INTERNATIONAL UNDERWRITERS

Similarly to the underwriters of the Hong Kong public offer, the underwriters of the international offering of shares will enter into an Agreement Among International Underwriters setting forth their various rights and obligations. Its provisions are similar to the Agreement Among Hong Kong Underwriters as discussed above, but instead it applies to the international placement tranche.

INTERSYNDICATE AGREEMENT

The Hong Kong public offer underwriters and the international offering underwriters will also enter into an Intersyndicate Agreement among themselves, governing, among other things, reallocation between the Hong Kong public and international offers, selling restrictions, stabilization activities and commissions and expenses.

PRICE DETERMINATION AGREEMENT

One of the key contractual arrangements in the IPO process, the Price Determination Agreement is entered into between the global coordinator and the listing applicant and sets forth the final offer price for the offered shares.

RECEIVING BANKS AGREEMENT

While not included in the charts and discussion above, the Receiving Banks Agreement is nevertheless an important agreement after pricing and near the end of the IPO process, entered into among the listing applicant, the global coordinator and one or more commercial banks. This agreement governs, among other things, the distribution of prospectuses and the various responsibilities of the commercial banks in coordinating and overseeing the application and payment process for the offered shares by the public.
F. COMFORT LETTERS, LEGAL OPINIONS AND CLOSING DOCUMENTS

COMFORT LETTERS

A comfort letter is a letter from the issuer’s independent auditors providing comfort (i.e., assurance) on financial information included in the offering documents. It may also include the accountants’ conclusions regarding their comparison of specified financial information in the offering document with the information contained in the issuer’s financial statements or accounting records. The purpose of the comfort letter is to assist the underwriters and other addressees in establishing a due diligence defense to potential liability under U.S. securities laws.

In a typical Hong Kong listing with Regulation S and Rule 144A offerings, three separate comfort letters are usually prepared: one for the listing and the Hong Kong public offer (the “Hong Kong Comfort Letter”); one for the Regulation S tranche (the “Regulation S Comfort Letter”); and one for the 144A tranche (the “144A Comfort Letter”). With respect to the Hong Kong Comfort Letter and the Regulation S Comfort Letter, the auditors are first expected to enter into separate arrangement letters with the underwriters before they issue such comfort letters. These arrangement letters generally outline the scope and nature of the audit procedures to be performed and also lay out the responsibilities of signing parties.

The form and content of the Rule 144A Comfort Letter is largely governed by the U.S. Statements on Accounting Standards No. 72, “Letters for Underwriters and Certain Other Requesting Parties,” as amended (“SAS 72”), which provides a template for the comfort letter and contains specific language that should be acceptable to accountants in various situations. Unlike the Regulation S Comfort Letter or the Hong Kong Comfort Letter, the Rule 144A Comfort Letter is not tied to a separate arrangement letter. However, the underwriters are required to sign and deliver a representation letter indicating that
they have conducted proper due diligence and that the due diligence review process was substantially consistent with the review process they would have performed had the transaction been registered under the U.S. Securities Act.

The form and content of the Hong Kong Comfort Letter, the Regulation S Comfort Letter and their respective arrangement letters are governed by the Hong Kong Standard on Investment Circular Reporting Engagement 400 (“HKSiR 400”), which similarly provides templates for such letters, as well as the specific language to be used in the letters.

An SAS 72 or HKSiR 400 comfort letter typically involves two types of assurance. First, it provides negative assurance on changes in the issuer’s financial position during the so-called “stub period,” which starts from the last date of audit up to the “cut-off date,” a date that is no more than five business days from the desired date of the comfort letter. Negative assurance consists of a statement by the accountants that, as a result of specified procedures, nothing came to their attention that caused them to believe that specified matters did not meet a specified accounting standard. If the accountants identify a change in a financial statement item in the course of conducting their negative assurance exercise, they will quantify it and disclose this in the comfort letter to bring it to the attention of the underwriters and any other addressees. During the stub period, the accountants may perform procedures such as an HKSiR 400 standard review of the interim financial statements, interviewing the issuer’s members of management responsible for financial and accounting matters and reading the issuer’s monthly management accounts and its shareholders’ and board meeting minutes. The procedures performed by the accountants are more limited and become less reliable when the account information is closer to the cut-off date.

The second type of assurance involved in an SAS 72 or HKSiR 400 comfort letter is on certain selected financial information in the offering circulars, where the accountants will perform certain procedures to make sure such information is correct to a certain level. These procedures normally involve comparisons with the audit report, the issuer’s accounting records or schedules prepared by the issuer, as well as arithmetic recalculation. The types of financial data and information to be covered by such procedures, as well as the scope of the procedures to be performed by the accountants, are subject to discussion among the accountants, the underwriters, their counsel and other working parties.
LEGAL OPINIONS

In addition to comfort letters issued by the independent auditors involved in the IPO, counsel to the issuer and counsel to the underwriters are both required to provide standard corporate and transaction opinions and letters. Such opinions and letters are conditions required to be satisfied for closing, and underwriters typically require them to make sure due diligence has been properly conducted and the transaction has been executed in compliance with various legal requirements.

In a typical listing with Regulation S and 144A offerings, there is generally one legal opinion covering various aspects of the listing and the Hong Kong public offer, and a separate legal opinion covering the Regulation S and/or 144A offering part of the transaction. For the latter, the following are some of the commonly requested legal opinions:

- a “no registration” opinion, opining that the sale of the securities to the underwriters/initial purchasers and the resale by the underwriters/initial purchasers to the placees do not require registration under the U.S. Securities Act;
- due execution and delivery of the International Underwriting Agreement;
- validity of submission of personal jurisdiction to a U.S. court (typically New York), of waiver of objection to venue and of appointment of service of process agent; and
- a “40 Act” opinion, opining that the issuer is not required to register as an “investment company” under the U.S. Investment Company Act of 1940.

In addition, the underwriters will require that both issuer’s and underwriters’ counsel give “10b-5 letters” (also referred to as negative assurance letters) consistent with standard U.S. public market underwriting practice, which are intended to help the underwriters establish the due diligence defense against potential liability under Rule 10b-5 of the U.S. Securities Act. The letter normally contains a statement in the form of negative assurance that no information has come to such counsel’s attention that causes it to believe that the offering documentation at the date of the letter contained an untrue statement of a material fact or omitted to state a material fact necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading.

TYPICAL CLOSING DOCUMENTS

Other than comfort letters and their respective arrangement letters from the auditors, the Hong Kong and U.S. legal opinions and the 10b-5 letters from the issuer’s legal counsel and the underwriters’ legal counsel, the underwriters will typically require the following documents as part of the closing conditions in the underwriting agreements.
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<thead>
<tr>
<th>Hong Kong Underwriting Agreement</th>
<th>International Underwriting Agreement</th>
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<tr>
<td>• Board resolutions approving, <em>inter alia</em>, the basis of allotment and the allotment of the shares</td>
<td>• Legal opinions of the local counsels¹</td>
</tr>
<tr>
<td>• Comfort letters from the reporting accountants giving comfort on the financial statements and certain financial information contained in the prospectus</td>
<td>• Closing certificates from the issuer, its controlling shareholders and certain of its directors and members of its senior management²</td>
</tr>
<tr>
<td>• Bring-down confirmations by the issuer, directors and certain senior management²</td>
<td></td>
</tr>
<tr>
<td>• Legal opinions of the local counsels¹</td>
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<tr>
<td>• Formal listing approval granted by the Exchange</td>
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</table>

**Notes:**

1. A closing legal opinion is required for each jurisdiction in which the issuer or one or more of its subsidiaries is incorporated or conducts a substantial part of its businesses. The underwriters may request additional legal opinions from other counsels based on specific issues related to the transaction.

2. Bring-down confirmations and closing certificates are typically given by these parties to represent that the representations and warranties given in the underwriting agreements and offering documents are true and correct as of the dates of the certificates. They may also be used to provide additional assurance on certain matters in relation to the listing, such as the validity of the board resolutions and the accuracy of financial information disclosed in the offering documents.
CHAPTER 7

MARKETING, SALES AND STABILIZATION

A. PUBLICITY RESTRICTIONS

Publicity restrictions arise in connection with an offering of securities in Hong Kong and are governed by the CO, the SFO and the Listing Rules. Chapter 2 gives a brief overview of these restrictions, and they are addressed in more detail in this Chapter.

GENERAL RESTRICTIONS

In general, restrictions apply as follows to the activities described below:

(1) Restrictions on issuing a prospectus by or on behalf of a Hong Kong company, or issuing in Hong Kong a prospectus offering for subscription shares or debentures of a company incorporated outside Hong Kong, in each case unless the prospectus complies with the requirements of the CO and has been registered by the Registrar of Companies of Hong Kong – sections 38D and 342C of the CO

Under the CO, a “Prospectus” means any document:

- offering any shares in or debentures of a company (including a company incorporated outside Hong Kong, and whether or not it has established a place of business in Hong Kong) to the public for subscription or purchase for cash or other consideration; or

- calculated to invite offers by the public to subscribe for or purchase for cash or other consideration any shares in or debentures of a company (including a company incorporated outside Hong Kong, and whether or not it has established a place of business in Hong Kong).

Prospectus Extracts and Advertisements

Under section 38B of the CO, it is also an offense to publish:

- by way of advertisement, any extract from or abridged version of a prospectus relating to shares or debentures of a company (whether incorporated in or outside Hong Kong); or

- an advertisement relating to such a prospectus (existing or proposed).
However, publications that have been authorized by the SFC (generally or specifically) or comply with the content requirements of Schedule 19 to the Co are exempted from the offense under section 38B. Such content requirements include:

- a statement that the advertisement is issued by the listing applicant to which the advertisement relates;
- a warning statement that potential investors should read the prospectus for detailed information about the listing applicant and the proposed offering before deciding whether or not to invest in the shares or debentures concerned; and
- a statement that the advertisement does not constitute an offer or an invitation to induce an offer by any person to acquire, subscribe for or purchase the shares or debentures concerned.

(2) Restrictions on any person issuing or having in his possession for the purpose of issue, whether in Hong Kong or elsewhere, an advertisement, invitation or document which to his knowledge is or contains an invitation to the Hong Kong public to enter into or offer to enter into any agreement to acquire, dispose of, subscribe for or underwrite securities — section 103 of the SFO

“Advertisement” includes every form of advertising, whether made orally or produced mechanically, electronically, magnetically, optically, manually or by any other means. A breach of this prohibition is a criminal offense. However, section 103 of the SFO provides a number of exceptions, including a prospectus that is registered under the Co.

Offer Awareness Materials

The SFC has issued its “Guidelines on Use of Offer Awareness and Summary Disclosure Materials in Offerings of Shares and Debentures under the Companies Ordinance” (the “Offer Awareness Guidelines”) on the content and manner of publication of certain publicity materials that may be issued to the public in Hong Kong in connection with an offer of shares made by a prospectus. The Offer Awareness Guidelines may be summarized as follows:
**Scope: Encompasses All Communications Media**
The scope includes brochures, correspondence, circulars, flyers, leaflets, mail shots, newspapers and magazines, posters and other visual advertising media, television or radio and electronic media, including the Internet, ATM services and telephone hotlines and any form of wireless video or audio transmission.

**Purpose of Publicity Materials**
The publicity materials must be designed only to raise investor awareness of a public offer of shares.

**General Principles**
- The materials must be issued by the listing applicant that issues the prospectus.
- The materials must not contain anything inconsistent with the information in the prospectus.
- The materials must use plain and clear language.
- The contents must not be false, biased, misleading or deceptive.
- All warning statements and legal legends in the materials must be of a certain font size.
- Other requirements also apply to materials designed for broadcast on a monitor or screen or by radio.

**General Prohibitions**
- Generally, offer awareness materials should not:
  - be published too far in advance of the launch of the proposed offer (normally, not more than 14 days before the date of the prospectus for a Hong Kong offering);
  - indirectly or impliedly promote the offer or the listing applicant, or otherwise condition the market ahead of the offer; or
  - be used after the close of the offer period and should be removed as soon as practicable thereafter.

**eIPO Advertisements**
Listing applicants often advertise through electronic channels for subscription of IPO shares. The Exchange normally considers these eIPO advertisements to be typical offer awareness materials, which need not be submitted for clearance, assuming that they fully meet the criteria under the Offer Awareness Guidelines and follow the “Guidelines for Electronic Public Offerings” issued by the SFC on April 2003 and, where the eIPO advertisement contains images or photos, the Exchange’s Guidance Letter GL13-09 (October 2009) regarding prospectus covers.
(3) Restrictions on releasing any publicity material in Hong Kong relating to an issue of securities by a new applicant before the Exchange has confirmed to the listing applicant that it has no further comments – Listing Rule 9.08

Under Listing Rule 9.08, all publicity material released in Hong Kong (or outside of Hong Kong if it will “flow back” into Hong Kong) relating to an issue of securities by a listing applicant must be reviewed by the Exchange before release and must not be released until the Exchange has confirmed to the listing applicant that it has no further comments.

All information released must be true, accurate and not misleading, and it must be consistent with, and not contradict or materially supplement, the prospectus.

Any publicity material or announcement referring to a proposed listing by a new applicant that is issued prior to the meeting of the Listing Committee held to consider the application must state that “application has been or will be made to the Exchange for listing of and permission to deal in the securities concerned.”

The Exchange will be inclined not to consent to publication of materials which are:

- not commensurate with the particular nature of the applicant’s business, products, customers or markets;
- presented in ways which make them likely to be read together with information relating to a public offering; or
- likely to condition the market ahead of the prospectus and affect perceptions of the upcoming offer.

The Exchange will consider all relevant circumstances, including the nature of the applicant’s business, its advertising history, the form of the publicity materials and the way they are presented, in assessing whether the information may condition the market (Guidance Letter GL18-10 (June 2010)).

Exceptions under Listing Rule 9.08

Circulation of the following is permitted:

- documents of a transaction-marketing nature, such as an invitation or offering telex (or its equivalent in another medium) or agreements in connection with the issue of securities, provided that any obligations which they create to issue, subscribe, purchase or underwrite the securities are conditional on listing being granted; and
- materials which are for the sole purpose of promoting the listing applicant or its products or business, and not the securities to be listed.
Consequences of a Breach

Supplemental Prospectus

As discussed in Chapter 2, the directors of the listing applicant can incur civil, criminal and regulatory liabilities in connection with the listing document. Accordingly, they must ensure that the prospectus includes the information required under the Co and the Listing Rules and that its contents are true, correct and not misleading in all material respects.

If, at any time after the issue of the prospectus and before the commencement of dealings in the shares of a listing applicant, it becomes apparent that there has been a significant change affecting any information in the prospectus or published with the prospectus, or additional information has arisen that would have been required to be disclosed, the listing applicant must submit the same to the Exchange for review and must issue, upon approval, a supplemental prospectus giving details of that change or additional information (Listing Rule 11.13).

Delay of Listing Timetable

When any material relating to a proposed listing by a new applicant is released without prior review by the Exchange, the Exchange may suspend vetting until all unauthorized publicity materials are withdrawn and/or delay the listing timetable by up to one month so that the influence of the unauthorized promotion has “cooled-off.”

If this will result in the A1 being more than six months old, the applicant may have to re-submit the application with a fresh initial listing fee (Listing Rule 9.08).

Posting of a Web Proof Information Pack (“WPIP”)

Pursuant to a Joint Policy Statement of the Exchange and the SFC (the “Joint Policy Statement”) dated November 5, 2007, a listing applicant is required to post a WPIP on the Exchange’s website prior to the issue of the prospectus. The rationale for requiring the WPIP posting at an earlier stage in the listing process is to address the apparent inequality of information available to institutional and retail investors shortly before the IPO and to assist in reducing media speculation around the IPO.

The WPIP is essentially a nearly final draft of the prospectus that omits pricing and related financial and offer size information and is substantially similar to the “red-herring” or “pathfinder” prospectus that is provided to institutional investors. Hence, the purpose of this posting requirement is to enable members of the public to receive, at or around the same time, substantially the same information that listing applicants ordinarily make available to the institutional investors for “bookbuilding” purposes.

The WPIP must be posted once the listing applicant receives a “request for posting” from the Exchange. This “request for posting” is typically issued around the same time that the Exchange sends out the post-hearing letter and requires the applicant to submit the WPIP to the Exchange for posting on the HKEx website on a business day not later than the earlier of:

- the first distribution by the applicant of any red-herring prospectus to institutional investors; and
- the first meeting (whether held physically or by video conference or any other media) with institutional investors for “bookbuilding” purposes, irrespective of whether any red-herring prospectus has been distributed.
The listing applicant should also observe the publicity restrictions and content requirements set out in the Joint Policy Statement.

**PRACTICAL TIP: BE AWARE OF ANONYMOUS LETTERS**

As a company prepares for its IPO, the Exchange may receive poison-pen letters containing various allegations about the company or its management, which are intended to disrupt the IPO process. Even if the allegations set forth in such letters are false and baseless, the company and the working group should carefully investigate the allegations and provide a complete response to the Exchange. The Exchange may require additional disclosure in the prospectus depending on the outcome of the investigation.

*Training on Publicity Restrictions*

To indicate its intention to list shares on the Exchange, a listing applicant may issue a press release or hold a press conference before the submission of its listing application to the Exchange. Such publicity activities, if handled inappropriately, could lead to breach of the CO, the SFO and/or the Listing Rules and to possible sanctions as discussed in Chapter 2 and this Chapter.

To prevent sanctions such as suspension or delay of the listing timetable, professional advisers should provide training to the listing applicant, its directors, senior management and other parties involved in an IPO on conducting marketing and publicity activities before listing.

Where there is any possibility of material nonpublic information being released or disclosed to an investment or research analyst, the listing applicant should first seek assistance and advice from its legal advisers and the sponsor(s) (see section B below for further details).
SUMMARY: GENERAL PRINCIPLES

To summarize the above, IPO publicity and marketing materials are subject to the following non-exhaustive general principles in Hong Kong:

- **Publicity materials should only contain information that is in the public domain and should be for the sole purpose of promoting the listing applicant or its products or business, not the IPO.**

- **Publicity materials must be true and accurate and not misleading in all material respects and must be consistent with the prospectus and not contradict or materially supplement it.**

- **To avoid being treated as an offer to sell or an invitation to subscribe for shares, publicity materials should not contain any direct or indirect reference to the proposed offering.**

- **The inclusion of any information regarding the listing timetable, the proposed financing, financial information, statistics of the listing applicant, forecasts, projections and valuations based on the proceeds of the proposed offering are not permitted.**

- **All publicity materials relating to the offering of shares by the listing applicant must be reviewed and approved by the Exchange.**

U.S. SECURITIES LAWS AND PUBLICITY GUIDELINES

As a listing on the Main Board of the Exchange will often include an international offering in jurisdictions other than Hong Kong, consideration must also be given to publicity restrictions under the laws of other jurisdictions, including applicable U.S. laws in the case of an international offering that includes a Rule 144A or Regulation S component. See Chapter 11, “International Offerings,” for further discussion.

U.S. securities laws are designed to protect investors and ensure that they have adequate information about a company prior to making a decision to invest in that company. The principal means of achieving this goal is Section 5 of the U.S. Securities Act of 1933 (the “U.S. Securities Act”). In general, Section 5 provides that unless an exemption is available, (i) an offer to sell a security cannot be made unless a registration statement is on file with respect to that offer with the U.S. SEC, (ii) a sale may not be made with respect to a security unless a registration statement with respect to that sale is “effective” (meaning that it has been approved by the U.S. SEC) and (iii) a security cannot be delivered after a sale unless it is preceded by or accompanied by a “prospectus” meeting the requirements of the U.S. Securities Act and included in the registration statement. A violation of Section 5 can result in civil or administrative
penalties. Most international offerings through a listing on the Exchange are structured to fall within
exemptions and exclusions from the registration requirements of Section 5, such as reliance on Rule
144A and Regulation S. However, the exemptions and exclusions being relied upon are highly fact-
dependent, and missteps in management of the offering process may result in a loss of the exemption
or exclusion. If the exemption or exclusion were lost, the offering would need to be registered under
Section 5. It is therefore critical to ensure that such offerings comply with U.S. securities laws on publicity
restrictions.

**Rule 144A and Publicity Considerations**

Listing applicants relying on Rule 144A, and their representatives, must not engage in any “general
solicitation” or “general advertising” in the U.S. with respect to the offering. The terms general solicitation
and general advertising are interpreted very broadly. General solicitation or general advertising relates to
activities undertaken or intended to influence persons in the U.S. and include, but are not limited to:

- any advertisement, article, notice or other communication published in any newspaper, magazine or
  similar media or broadcast over television or radio; and

- any seminar or meeting whose attendees have been invited by any general solicitation or general
  advertising.

General solicitations may also include communications that are viewed as conditioning the market in the
United States; such communications may include, without limitation, information regarding the issuer on
its website or third-party websites, or announcements or press releases regarding the issuer’s business
that are not consistent with its past practices. An issuer should carefully consider all communications
to the public during the offering period to ensure that they are not inadvertently engaging in a general
solicitation.

It is important to note that the publicity restrictions in Rule 144A are currently being revised by the U.S.
SEC, pursuant to the directive given in the U.S. Jumpstart Our Business Startups Act (the “JOBS Act”),
which was signed into law in the United States in April 2012. The U.S. SEC is still considering comments
from the public on its possible revisions to Rule 144A. While none of the revisions have yet been
finalized, Rule 144A is expected to be ultimately amended to allow for general solicitation and advertising
in Rule 144A offerings, provided that securities are sold only to persons that the seller (and any person
acting on behalf of the seller) reasonably believes are Qualified Institutional Buyers (“QIBs”). It is unclear
whether general solicitation and advertising will indeed be used by issuers even after Rule 144A is
revised because of concerns with antifraud liability under U.S. law and also possible conflicts with the
publicity restrictions in Regulation S. In any case, close attention should be paid to the U.S. SEC’s future
releases and announcements for relevant updates.

**Regulation S and Publicity Considerations**

Generally, Regulation S prohibits the issuer and any person acting on its behalf from engaging in
“directed selling efforts” in the United States. The listing applicant and its representatives must be careful
to ensure that their activities, including, without limitation, any announcements, press conferences or
other publicity activities with respect to the international offering in Hong Kong or elsewhere, do not
constitute directed selling efforts in the United States.
Directed selling efforts encompass activities undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the U.S. market for the shares being offered and include activities such as the following:

- sending non-U.S. offering materials to U.S. investors;
- conducting promotional seminars in the United States; and
- promoting press coverage about the company or interviews with officers, directors or shareholders of the company in any U.S. media.

It is important to note that anything that might constitute general solicitation would likely be considered directed selling efforts.

**Application of Rules to Specific Publicity Communications**

**Offshore Press**

When relying on exemptions and exclusions from registration under U.S. securities laws, no press release about the international offering may be distributed, and no other public statements about the international offering may be made, in the United States by those involved in the listing.

The U.S. SEC has established “safe harbor” procedures whereby a foreign private issuer, selling security holder or their representatives may provide foreign and U.S. journalists with access to offshore press conferences, offshore meetings and press materials released offshore in which a present or proposed offering of securities is discussed. Press activities conducted by the listing applicant and its representatives that are in accordance with the provisions of the safe harbor would not be viewed as making an “offer” or constituting general solicitation, general advertising or directed selling efforts.

Conditions to the safe harbor include, but are not limited to, the following:

- press activity must occur outside the United States;
- the offering must not be conducted solely in the United States;
- access must be provided to both U.S. and foreign journalists; and
- written materials released to journalists must have appropriate disclosure (usually, a legend on the written material) that such materials should not be considered an offer of securities for sale in the United States and that the shares in the offering may not be sold in the United States absent registration or an exemption from registration.

**Roadshow Meetings and Internet Considerations**

As part of the international offering, it is customary for the issuer and underwriters to hold “roadshows,” in which they visit several cities to meet with potential investors. For offerings relying on Rule 144A and Regulation S, only QIBs and non-U.S. persons can access the roadshow. For offerings which rely solely on Regulation S, roadshows may not be held in the United States.
The only written information provided to attendees of the roadshow is the offering memorandum prepared for the private placement with the appropriate U.S. private placement “wrap.” See Chapter 11, “International Offerings,” for more information on the wrap. No copies of slides or any other written materials should be made available to roadshow attendees, and any information not contained in the wrap should not be disclosed.

If roadshow materials are placed online, the listing applicant and the underwriter(s) should adopt certain protective procedures to ensure that only QIBs and non-U.S. persons, or persons which the company and underwriters reasonably believe are QIBs or non-U.S. persons, can access the website. In practice, this is accomplished often, but not exclusively, through password-protecting the roadshow materials and then distributing the password only to QIBs and non-U.S. persons. Furthermore, such websites will often have a pre-logon screen which requires that each visitor affirm it is a QIB and/or a non-U.S. person before the visitor can access the materials, or the website will contain a prominent disclaimer making it clear that the offering is directed only to countries other than the United States. Such procedures are necessary to prevent U.S. persons from participating in the international offering. If the procedures are inadequate, the U.S. SEC may consider such internet materials to constitute a directed selling effort into the United States and/or general solicitation or general advertising, in which case the issuer will lose the ability to rely on Regulation S and/or Rule 144A.

B. PRE-DEAL RESEARCH AND INVESTOR EDUCATION

Pre-deal research reports are typically prepared by the research departments of the syndicate of underwriters and provide an analysis of a listing applicant, its business and prospects. Such research reports can play an important role in price discovery in the IPO process.

The SFC Code of Conduct regulates reports by analysts covering companies listed or about to be listed in Hong Kong.

PREPARATION

General Content

Under the SFC Code of Conduct, the report should:

- be, and present itself as, an independent outsider’s view of the listing applicant, independently produced;
- make clear any published or historical information, statements and source of the information;
- make clear that it does not contain everything material relating to the listing applicant; and
- not make any reference to the offering.
To the extent that general publicity restrictions (see part A of this Chapter) may apply, the report should:

- not contain any “offer to sell” or “invitation to buy” characterization;

  Note: It is important that a research report complies with this restriction. As the SFC noted in its “Consultation Paper on Possible Reforms to Prospectus Regime in the Companies Ordinance” dated August 2005, if a research report is drafted such that it is “calculated to invite offers” by the public to subscribe for or purchase shares, it would constitute a prospectus and be regulated in the same way as a conventional prospectus. Issuers of such research reports would be subject to liability accordingly.

- be for the sole purpose of promoting the listing applicant and not the securities to be listed; and

- comply with all applicable statutory requirements for publicity materials.

Forecasts, projections and valuations may be included in research reports if they are prepared independently, but they must not include specific valuation figures, save for valuation ranges, discussion of valuation technology and analyses of comparable stocks.

**Disclosure of Financial Interests and Business Relationships**

The research report should disclose the relevant particulars wherein the researching firm *(Paragraph 16.5 of the SFC Code of Conduct)*:

- has any financial interests in the listing applicant amounting to 1% of its market capitalization or more;
- has an employee or another person associated with the firm serving as officer of the listing applicant; or
- has had an investment banking relationship with the listing applicant within the preceding 12 months.

**SPONSORS’ OBLIGATIONS**

**Improper Dealing Ahead of Investment Research**

A sponsor should not improperly deal or trade ahead in securities related to any listed company which its investment research covers *(Paragraph 16.5(e) of the SFC Code of Conduct)*. Typically, Chinese walls are implemented as internal information barriers to restrict the flow of inside information on a need-to-know basis, to limit the risk of improper dealing.

**Quiet Period**

The SFC Code of Conduct does not establish any quiet period restricting the publication of a pre-deal research report before the making of an IPO offer, although there is a risk that too short a period could cause the report to become part of the offering and trigger liability accordingly. In the SFC’s “Consultation Conclusions on the Regulatory Framework for Pre-deal Research” dated June 2011, the SFC stated that it did not yet consider it appropriate to establish a pre-IPO quiet period. It also noted that many firms impose a quiet period of at least two weeks after they issue a pre-deal research report, and the length of a pre-IPO quiet period is a matter for firms to consider and implement in light of the nature, complexity and scale of their businesses.
However, sponsors and underwriters should not issue investment research covering a listing applicant or listed company at any time within: (i) 40 days after the shares are priced in an IPO; or (ii) 10 days after the shares are priced in a secondary public offering, unless the firm has been issuing investment research on the listing applicant or listed company with reasonable regularity in its normal course of business, or when major events occur that would affect the price of the securities, and the events are known to the public (paragraph 16.5(g) of the SFC Code of Conduct).

**Prohibition on Seeking Material Information from Listing Applicant**
An analyst preparing pre-deal research on a listing applicant should not seek from the applicant or its advisers, directly or indirectly, any material information, including forward-looking information, concerning the applicant that is not reasonably expected to be included in the prospectus or publicly available (paragraph 16.11(c) of the SFC Code of Conduct).

*Notes:* “Material information” means information “which enables a reasonable person to form as a result thereof a valid and justifiable opinion of the shares and the financial condition and profitability of the company at the time of the issue of the prospectus.”

“Forward-looking information” refers to “any forward-looking information, whether such information is quantitative or qualitative in nature.”

This prohibition enhances the integrity and objectivity of pre-deal research reports and prevents research reports from being used by listing applicants to disseminate information without formal prospectus liability.

**Information Flow**
Sponsors should take steps to ensure that all material information, including forward-looking information (whether quantitative or qualitative), that is disclosed or provided to analysts is contained in the relevant prospectus or other listing document (*Paragraph 5.10 of the CFA Code*). These steps involve carefully assessing any information proposed to be provided to analysts and not in the prospectus, to determine whether it might be prohibited “material information.”
As a result of this rule, key market participants have adopted standard measures and documentation for the pre-deal research process. The agreed key milestones relating to the issue of a pre-deal research report are as follows:

- **Kick-Off**
  - Sponsor and syndicate counsel to discuss whether extra control measures are required
  - Analysts and listing applicant to be trained on what information they cannot seek from listing applicant
  - Sponsor to send memo setting out the listing applicant’s responsibilities
  - Analysts to send the listing applicant a notice of the SFC Information Flow Requirements

- **Before Analyst Presentation**
  - Syndicate counsel to distribute Research Guidelines
  - Review presentation script
  - Internal Compliance to remind analysts before due diligence with listing applicant not to seek impermissible information
  - Analysts and Joint Book Runners: No joint due diligence

- **Analyst Presentation**
  - Analysts encouraged (but not obliged) to send written questions in advance
  - Each syndicate bank is deemed to have agreed to comply with the Research Guidelines
  - Syndicate counsel/listing applicant counsel to attend analysts’ presentations

- **Report Drafting**
  - Sponsor and syndicate counsel to review draft pre-deal research report
  - Analysts to confirm prior to publication that no receipt of impermissible information

### C. STRUCTURING AND PRICING THE OFFER

#### STRUCTURE OF A TYPICAL OFFER

As set out in Practice Note 18 (“PN18”) to the Listing Rules, the initial minimum allocation of shares to the public subscription tranche is 10%. The policy consideration underlying PN18 is to ensure a sufficient supply of shares to satisfy the demand of Hong Kong retail investors while otherwise allowing issuers and underwriters a sufficient degree of flexibility to determine their offer structures.

#### CLAWBACK MECHANISM

Where the Hong Kong public offer tranche is oversubscribed, PN18 prescribes certain clawback arrangements whereby given proportions of the shares will be transferred from the international placing
Tranche to the Hong Kong public offer tranche. However, the Exchange will accept lower clawback levels where the size of the offering is sufficiently large to warrant a modification of the standard PN18 requirements (*Listing Decision LD60-1*). The table below sets forth the standard clawback requirements under PN18, which range from 10% to 50% depending on the level of oversubscription, as well as the clawback requirements under a typical PN18 waiver granted by the Exchange.

<table>
<thead>
<tr>
<th>Offer Size (HK$ billions)</th>
<th>% Allocated to Hong Kong Public Offer Based on Number of Times (x) Hong Kong Public Offer is Oversubscribed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Initial</td>
</tr>
<tr>
<td>PN18 requirements</td>
<td>Not specified</td>
</tr>
<tr>
<td>Typical PN18 Waiver</td>
<td>10</td>
</tr>
</tbody>
</table>

The following chart illustrates the standard PN18 clawback mechanism, as well as a typical PN18 waiver, for a HK$10 billion offering.
When granting PN18 waivers, the Exchange will take the following factors into account:

- due regard must be given to the interest of local investors, particularly where it is anticipated that there will be significant public demand for the applicant’s securities;
- the trigger multiples for oversubscription clawback should be as low as possible;
- the number of shares that Hong Kong retail investors will obtain under the actual offering structure should not be less than the number of shares that they would have obtained under a typical PN18 waiver; and
- the trigger points for oversubscription clawback should be easy to implement and easy for an average retail investor to understand (Listing Decision LD60-1).

**ALLOCATION OF SHARES**

An investor is free to apply for shares in either the international placing tranche or the Hong Kong public offer tranche, but he may only receive shares in one tranche.

Multiple applications within either tranche or between tranches will be rejected. Issuers, their directors, sponsors and underwriters are required to take reasonable steps to identify and reject applications in the Hong Kong public offer tranche from investors that received shares in the international placing tranche, and to identify and reject indications of interest in the international placing tranche from investors that received shares in the Hong Kong public offer tranche.

**OFFER SIZE ADJUSTMENT**

For offers less than HK$100 million, changes in the size of an IPO during the subscription process are permitted through the inclusion of an offer size adjustment option, subject to a cap of 15% of the offer size (Listing Decision LD36-3). The offer size adjustment option must be exercised prior to listing. In contrast, the over-allotment option is exercised after listing. For details, see section E below.

**PRICING THE OFFER**

The offering price is typically negotiated by the company, the sponsor, the underwriters and the selling shareholders, if any. Generally speaking, the company will aim for the highest price that will facilitate the distribution of the offer shares. In contrast, the underwriters tend to seek a price that will assure that the offering will be oversubscribed to ensure a strong secondary market.

The offer price is normally disclosed as an indicative offer price range, instead of a fixed price, to allow greater flexibility in pricing the offer according to rapidly changing market conditions. The indicative offer price range is determined after a careful price discovery process, taking into account the valuation of the business and future development.

*Downward Revision of Offer Price Range*

The Exchange considers any downward revision of the offer price range after the issue of the prospectus but before close of the offer to be a material change of circumstances, as such a revision would affect other aspects of the listing, including the company’s market capitalization and use of proceeds. Hence, such a downward revision in the offer price requires the issue of a supplemental prospectus (Listing Decisions LD61-1 and LD86-1).
As a general rule, the Exchange will consequently require the issuer to extend the offer period and grant a right of withdrawal to applicants who have submitted applications under the original prospectus. Applicants who wish to proceed are required to opt-in by providing positive confirmations, failing which their applications are treated as lapsed.

**Transaction Costs for IPO Shares**

The amount payable for initial public offer shares comprises four elements, namely:

- **Application Money**: the offer price of the number of the shares applied for
- **Brokerage Fees**: 1% of the application money
- **SFC Transaction Levy**: currently 0.003% of the application money
- **Exchange Trading Fee**: currently 0.005% of the application money

**D. PLACEES AND PLACING GUIDELINES**

The Listing Rules include Placing Guidelines (*Appendix 6 to the Listing Rules*) designed to ensure that in a placing of shares, such as the international offering tranche of an IPO, the shares are placed to independent and genuine investors, rather than related parties or connected clients of the lead brokers or the distributors.

The Placing Guidelines apply only to securities of a class new to listing, such as IPO shares. For securities of a class already listed, the Placing Guidelines do not apply.

Before dealings commence, marketing statements in the form set out in Form D in Appendix 5 of the Listing Rules signed by each of the lead broker, any distributor(s) and the listing applicant must be lodged with the Exchange (*Paragraph 10 of Appendix 6*).

The lead broker must also provide the Exchange with a list of all placees and the amounts taken up by them, including their names, addresses and identity card/passport/business registration numbers and full beneficial owner details in the case of nominee companies (*Paragraph 11 of Appendix 6*). Dealings cannot commence until the Exchange has vetted and approved this list. The Exchange may also require further information on the placees for the purpose of establishing their independence (*Paragraph 11 of Appendix 6*).

The lead broker and each distributor and the listing applicant must keep a record of all placees for at least three years following the placing (*Paragraph 12 of Appendix 6*).
Under the Placing Guidelines, there are two main requirements:

1. **“GENERAL PUBLIC” REQUIREMENT**

Not more than 75% of the amount placed may be placed directly by the lead broker or through the other distributors, and the rest must be made available by the lead broker directly to the general public (Paragraph 3 of Appendix 6).

*Note:* “General public” means:
- investors other than clients of the lead broker; or
- clients of the lead broker who had not received any special notification or invitation in respect of the placing.

Where there is public demand, neither the lead broker nor any distributor may retain more than 5% of their respective shares of the total placing. Where there is insufficient demand from members of the “general public,” the amount not taken up in the placing tranche can be redistributed to clients of the lead broker (Paragraph 8 of Appendix 6).

Not more than 10% of the total placing may be offered to employees or past employees and not more than 25% of the total placing may be allocated to “discretionary managed portfolios” (Paragraphs 6 and 7 of Appendix 6).

*Note:* “Discretionary managed portfolio” means a fund of investments managed by an Exchange Participant or its group with power to enter into transactions for the fund at its discretion.

The securities placed must also have an adequate spread of holders depending on the size of the placing. For every HK$1 million of the placing, there should not be fewer than three holders, with a minimum of 100 holders.

Except for placings of securities by overseas listing applicants having their primary listing on another stock exchange, the expected initial market capitalization of the securities to be placed must not be less than HK$25 million or any other amount fixed from time to time by the Exchange (Paragraphs 1 and 2 of Appendix 6).
2. PROHIBITED PLACES

No allocations are permitted to the following without the prior written consent of the Exchange:

- “connected clients” of the lead broker or any distributors;
- directors or existing shareholders of the listing applicant or their associates, unless conditions under Listing Rule 10.03 are fulfilled; or
- nominee companies, unless the name of the ultimate beneficiary is disclosed.

*Note:* A “connected client” of an Exchange Participant means any client who is:

1. a partner, employee, substantial shareholder or director of the Exchange Participant;
2. the spouse or infant child or stepchild of any individual described in (1);
3. a person in his capacity as trustee of a private or family trust (other than a pension scheme) the beneficiaries of which include any person in (1) or (2);
4. a close relative of any person in (1) or (2) where his account is managed by the Exchange Participant under a discretionary managed portfolio agreement; or
5. a company in the same group as the Exchange Participant.

Availability of Consent from the Exchange

Consent will not normally be given for any allocation of shares to any connected client who intends to hold them for its own house account, but directors of the listing applicant and their associates may subscribe, in their own names or through nominees, provided that the shares are not offered to them on a preferential basis and no preferential treatment is given in the allocation, and the public float requirement (Listing Rule 8.08) is met.

Under Listing Decision LD44-2, consent was given to the allocation of IPO shares to a connected client of one of the distributors (who was also a shareholder of the listing applicant) on the following basis:

- the subscription was pursuant to an antidilution provision in the articles;
- the proposed placing would be at the IPO price;
- a three-year lockup would apply; and
- disclosure would be made in the prospectus and the allotment results announcement.
E. STABILIZATION AND OVER-ALLOTMENT

Price stabilization generally refers to transactions which support the market price of listed securities.

“The primary purpose of stabilization is to facilitate capital raising by corporations by addressing short-term fluctuations resulting from the sudden increase in supply in the secondary market (which would generally result in a decrease in the price of securities being offered).”

SFC, Legislative Council Brief (December 2002)

However, stock market manipulation is prohibited under section 278 of the SFO. Such manipulation takes place when, in Hong Kong or elsewhere, a person enters into or carries out two or more transactions in listed securities which increase, reduce, maintain or stabilize the price of any securities traded on a recognized market, or are likely to do so, with the intention of inducing another person to purchase or subscribe for, or refrain from selling, listed securities.

The Securities and Futures (Price Stabilization) Rules (the “Stabilization Rules”) prescribe a “safe harbor” for certain stabilizing actions by exempting them from constituting market misconduct (section 4 of the Stabilization Rules). Under the Stabilization Rules, only a single intermediary may be appointed by the listing applicant to act as its stabilizing manager, and such intermediary is the only person authorized to take any stabilizing action under the Stabilization Rules.

APPLICATION OF STABILIZATION RULES

Stabilization activities are allowed only in the following types of offerings (section 3 of the Stabilization Rules):

• public offerings that are the subject of a Hong Kong-registered prospectus; and
• placings in a public offering to institutional investors of securities that will be uniform in all respects with existing listed securities, where the offering is the subject of a public announcement containing the offer price and prescribed information on the stabilization (placings for sale by existing shareholders are eligible only if they are top-up placings).

To fall within the Stabilization Rules, the total value of the securities at their offer price should not be less than HK$100 million or its equivalent in any foreign currency.

Primary Stabilizing Actions

Under the Stabilizing Rules, the stabilizing manager may purchase or agree to purchase any of the relevant securities (or offer or attempt to do so) for the sole purpose of preventing or minimizing any reduction in the market price of the securities (section 6 of the Stabilization Rules). This is called primary stabilizing action. However, primary stabilizing action is allowed only during the stabilizing period, which begins on the day when trading of the securities commences on the Exchange (or another relevant stock exchange) and ends on the 30th day after the last date for lodging applications (or if earlier, the 30th day after the start of trading).
**Pricing Limitation**

In the course of any primary stabilizing action, the stabilizing manager may not make any bid or effect any transaction relating to the relevant securities at a price exceeding the maximum price for the relevant action set out below (section 11 and schedule 2 of the Stabilization Rules):

<table>
<thead>
<tr>
<th>Item</th>
<th>Time or circumstances of action</th>
<th>Maximum price</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Initial stabilizing action (i.e., first occasion)</td>
<td>The offer price</td>
</tr>
<tr>
<td>2</td>
<td>After the initial stabilizing action, where there has been a deal done or transaction effected at a price above the stabilizing price on the relevant market</td>
<td>The lower of (i) the offer price and (ii) the price at which that deal was done or at which that transaction was effected</td>
</tr>
<tr>
<td>3</td>
<td>After the initial stabilizing action, where there has been no deal or transaction described in item 2</td>
<td>The lower of (i) the offer price and (ii) the initial stabilizing price</td>
</tr>
</tbody>
</table>

**Ancillary Stabilizing Action**

In connection with any primary stabilizing action taken, the stabilizing manager may carry out the following ancillary stabilizing actions (section 7 of the Stabilization Rules):

- over-allocation of securities and short sales, in each case for the purpose of preventing or minimizing any reduction in the market price of the securities;
- the exercise of an over-allotment option to close out a position established in connection with the relevant primary stabilizing action (the pricing limitations above do not apply here); and
- sell shares acquired in the relevant primary stabilizing action to liquidate any position established by that action.
OVER-ALLOTMENT OR “GREEN SHOE” OPTIONS

In order to facilitate stabilization in connection with an IPO, the company or controlling shareholder may grant the underwriters an over-allotment option to buy additional shares at the IPO offer price, which can be exercised for up to 30 days from the last day for lodging of applications under the Hong Kong public offering. The Exchange would normally expect the number of additional shares which can be issued under an over-allotment option not to exceed in aggregate 15% of the total number of offer shares initially available under the offering. The purpose of setting a modest upper limit of 15% on the over-allotment option is to keep the uncertainty created by its potential dilution effect to within acceptable levels in the interests of maintaining an orderly market for new issuers (Listing Decision LD26-3).

When an IPO is priced, the underwriters typically will create a syndicate short position in the company’s shares by accepting orders for more shares than are to be sold (i.e., by over-allocating shares). The underwriters may then do one of two things to cover these over-allocations during the stabilization period:

• if the share price increases during after-market trading, the underwriters typically will cover their short position by exercising the over-allotment option and delivering to investors the additional securities purchased from the company or controlling shareholder at the lower IPO offer price; or

• if the share price decreases during after-market trading, the underwriters typically will cover their short position by purchasing shares from the secondary market following the commencement of trading, which helps create buying power and support the share price in the after-market.

The over-allotment option is often referred to as the “Green Shoe” option, as it was first used in connection with an offering of shares by The Green Shoe Manufacturing Company (the maker of Stride Rite shoes) in 1963.

Register of Stabilizing Action

The stabilizing manager must keep a register for each share offering, including the names of all appointed agents, the initial stabilizing price, details of each transaction effected during the stabilizing period and details of any allocations. The register must be kept for at least seven years and be made available for inspection by the SFC at any time and (as to certain transaction details) by the offeror of the relevant shares at any time within three months after the end of the stabilizing period (section 13 of the Stabilization Rules).

Disclosure Obligations

Disclosure of any over-allotment option to purchase the relevant securities from the offeror in the relevant offer document is a precondition of any stabilizing action. In addition, an announcement must be issued as soon as practicable after the exercise or partial exercise of an over-allotment option, stating...
the number of securities purchased and the number remaining available under any unexercised portion (section 9 of the Stabilization Rules).

Within seven days after the end of the stabilizing period, an announcement is required containing the following information, as applicable:

- the date on which the stabilizing period ended;
- whether or not any stabilization action was taken;
- the price range within which purchases were made;
- the date and price of the last purchase; and
- the extent to which any over-allotment option was exercised.

REGULATION M OF THE U.S. SECURITIES ACT

Regulation M of the U.S. Securities Act governs the activities of underwriters, issuers, selling security holders and other offering participants in connection with securities offerings and was adopted by the SEC to prevent manipulative conduct by persons with an interest in the outcomes of securities offerings. Rules 101 and 102 of Regulation M prohibit issuers, selling security holders, distribution participants and any of their affiliated purchasers from directly or indirectly bidding for, purchasing or attempting to induce another person to bid for or purchase the securities being distributed, or any security into which they may be converted, exchanged or exercised, or the terms of which may “in whole or significant part” determine their price. The restrictions of Regulation M apply globally if any element of a “distribution” occurs in the United States, even to activities conducted outside the United States by non-U.S. persons. However, securities distributed in reliance on the Rule 144A exemption are generally exempt from Regulation M requirements, so long as the securities meet the fungibility and other requirements under Rule 144A and are offered and sold in the United States only to QIBs, or if they are sold to persons in the United States who are not deemed to be “U.S. persons” for the purposes of Regulation S under the U.S. Securities Act. Regulation M also contains other exemptions for securities that are actively traded, for ordinary course transactions and for certain stabilization activities.
CHAPTER 8

THE PROSPECTUS

The prospectus is one of the most important documents that an issuer produces during the IPO process. It is the source of information for potential investors to understand, among other important information, the business operations, financial performance and corporate structure of the listing applicant. The prospectus should be produced in compliance with the regulatory regime, but in addition to its compliance function, the prospectus also serves as a marketing document for the listing applicant.

A. PROSPECTUS LIABILITY

Liability for the contents of a prospectus is governed under the CO, the SFO, common law and other legislation.

COMPANIES ORDINANCE

<table>
<thead>
<tr>
<th>Sections 38, 342 and the Third Schedule</th>
<th>These sections prescribe the compulsory information to be disclosed in the prospectus. If the prospectus fails to meet these requirements, any person who is knowingly responsible for the issue, circulation or distribution of the prospectus will be liable to a fine.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 40(1)</td>
<td>Where investors suffer losses in reliance upon misstatements in the prospectus, the following persons are liable to compensate the investors for the losses:</td>
</tr>
<tr>
<td></td>
<td>• directors of the company at the time of the issue of the prospectus;</td>
</tr>
<tr>
<td></td>
<td>• any person who has authorized himself to be named and is named in the prospectus as a director or as having agreed to become a director;</td>
</tr>
<tr>
<td></td>
<td>• promoter(s) of the company; and</td>
</tr>
<tr>
<td></td>
<td>• every person who has authorized the issue of the prospectus.</td>
</tr>
<tr>
<td>Section 40(2)</td>
<td>A person is not liable under section 40(1) if he:</td>
</tr>
<tr>
<td></td>
<td>• withdrew consent before the issue of the prospectus and it was issued without his authority or consent;</td>
</tr>
<tr>
<td></td>
<td>• did not know of or consent to the issue of the prospectus and, on becoming aware of its issue, he forthwith gave reasonable public notice that it was issued without his knowledge or consent;</td>
</tr>
<tr>
<td></td>
<td>• before allotment of the shares, became aware of an untrue statement in the prospectus, withdrew consent and gave reasonable public notice of the withdrawal of consent and the reason for it;</td>
</tr>
<tr>
<td></td>
<td>• had reasonable grounds to believe, and did until the time of allotment of shares believe, that the untrue statement was true (except where it was purportedly made on the authority of an expert or a public official document or statement);</td>
</tr>
</tbody>
</table>
### Section 40(2) continued
- reasonably believed, where the untrue statement was purportedly made by an expert (or fairly copied or extracted from an expert’s report), that the person making the statement was competent to make it and had given and not withdrawn consent to its inclusion prior to registration of the prospectus or (to the knowledge of the director) prior to allotment of the shares pursuant to the prospectus; or
- can prove that the untrue statement purported to have been made by an official person (or was contained in what purported to be a copy of or extract from a public official document) and was a correct and fair representation of the statement or extract.

### Sections 40A and 342F
Where a prospectus includes an untrue statement or omission of material information, any person who has authorized the prospectus will be liable to imprisonment and a fine, unless it can be shown that the statement was immaterial or that there were reasonable grounds to believe, and that the person did believe, that the statement was true.

### SECURITIES AND FUTURES ORDINANCE

#### Section 107
This section imposes criminal liability on a person who induces another person to enter into an agreement to acquire, dispose of, subscribe for, or underwrite securities by means of “fraudulent misrepresentation” or “reckless misrepresentation.”

**Fraudulent misrepresentation includes:**
- any statement known to its maker to be false, misleading, or deceptive, at the time when it is made;
- any promise which its maker intends not to fulfill or knows to be incapable of being fulfilled, at the time when it is made;
- any forecast which its maker knows is not justified on the facts known to him, at the time when it is made; or
- any statement or forecast from which its maker intentionally omits a material fact, at the time when it is made, with the result that the statement is rendered false, misleading, or deceptive or the forecast is rendered misleading or deceptive.

**Reckless misrepresentation includes** the same factual situations save that, instead of having such intention or knowledge, the person making the statement is reckless about, or lacks knowledge of, its truthfulness.

#### Section 108
This section imposes civil liability on a person who induces another person to enter into an agreement for the acquisition or subscription of shares by fraudulent, reckless or negligent misrepresentation. **Negligent misrepresentation includes** the same factual situations as the fraudulent and reckless varieties, save that the person making the statement has failed to exercise reasonable care to ensure the accuracy of the statement.
THE MOFO GUIDE TO HONG KONG IPOs

Chapter 8: The Prospectus

<table>
<thead>
<tr>
<th>Section</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 298</td>
<td>This section prohibits the disclosure, circulation or dissemination by any person of information likely to induce another person to enter into a securities transaction if such information is false or misleading and the first person knows that, or is reckless as to whether, the information is false or misleading.</td>
</tr>
<tr>
<td>Section 300</td>
<td>This section prohibits the use, in a securities transaction, of any deceptive or fraudulent conduct, or of any device or scheme intended to defraud or deceive.</td>
</tr>
<tr>
<td>Section 384</td>
<td>This section prohibits knowingly or recklessly giving false or misleading information to the Exchange and the SFC.</td>
</tr>
<tr>
<td>Section 390</td>
<td>Where a corporation commits an offense under the SFO, this section extends liability to any officer of the corporation who consented, connived, or was reckless as to the commission of that offense.</td>
</tr>
</tbody>
</table>

Theft Ordinance

The officers of a corporation may be subject to criminal liability under the Theft Ordinance with respect to the publication of various listing documents and announcements, such as the prospectus and financial accounts, if any disclosure was made with intent to deceive the shareholders or creditors and the officers knew that such information or disclosure was or may be misleading, false, or deceptive in a material respect.

Common Law

| Misrepresentation | The prospectus is a document issued by the listing applicant to the public for the primary purpose of inviting the public to invest in the securities of the company. Under common law, where representations are made by one person with the view of inducing another party to enter into a contract, if the representations are false, and the other party suffers losses in reliance upon the false representations, he may be entitled to rescind the contract and claim damages against the person who made the representations. |
| Negligent Misstatement | The directors of the listing applicant may be liable for negligent misstatement as a tort under common law, where the directors (i) make a misstatement in the prospectus with the intention that such statements be relied upon by the investors, (ii) the investors suffer a loss in reliance upon such statements and (iii) it was reasonable for the investors to have relied upon the misstatements. |
| Deceit | The listing applicant’s directors may be liable under the tort of deceit if the prospectus contains any misstatement that was fraudulently made, i.e., if it was made in any of the following circumstances:  
- with knowledge that the statement was false;  
- without belief in its truth; or  
- recklessly, without caring whether it was true or false. |
LISTING RULES

The Listing Rules (Listing Rule 11.12) require that a prospectus include a statement that the directors of the company collectively and individually accept full responsibility for the document and confirm, having made all reasonable inquiries, that to the best of their knowledge and belief the information contained in the prospectus is accurate and complete in all material respects and not misleading or deceptive, and that there are no other matters the omission of which would make any statement in the prospectus misleading. This statement can be relied upon by investors as the basis for legal action against the directors.

U.S. SECURITIES LAWS

Section 12 of the U.S. Securities Act imposes liability on any person who offers or sells a security in violation of Section 5 or by means of a prospectus or oral communication that includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading.

Section 12 does not require reliance on the misstatement or omission, or even the receipt of a prospectus. Liability under Section 12 may be for rescission, if the security is still owned by the purchaser, or otherwise for damages. A defense may be sustained under Section 12(a)(2) if the person selling the security can demonstrate that “he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission.” Though the statute does not explicitly require the defendant actually to exercise reasonable care, the “reasonable care” standard under Section 12(a)(2) appears to be the same as the “reasonable investigation” standard for the “due diligence” defense under Section 11. Therefore, the defendant must establish that he performed due diligence in order to sustain the defense.

Under Section 11 of the U.S. Securities Act, liability may arise from misstatements or omissions in a registration statement at the time it became effective. However, since Regulation S provides an exclusion from the registration requirements of Section 5, Regulation S offerings do not subject the issuer and underwriters to liability under Section 11. Nevertheless, underwriters often choose to conduct due diligence comparable to that conducted for a registered offering, particularly if the offering is a combined Rule 144A/Regulation S offering.

Finally, Rule 10b-5 under the U.S. Exchange Act provides purchasers of a security with a cause of action against any person who makes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made in connection with the purchase or sale of any security, in the light of the circumstances under which they were made, not misleading. Potential remedies under a Rule 10b-5 claim include rescission (cancelling the original transaction) and damages.

Rule 10b-5 was enacted by the U.S. SEC to buttress the liability provisions in the U.S. Securities Act. The reach of Rule 10b-5 is extremely broad, and U.S. courts have determined that all purchases and sales of securities fall under Rule 10b-5’s purview, regardless of whether these are exchange, private or over-the-counter transactions. This is in contrast to antifraud provisions of the U.S. Securities Act, which apply only to fraud perpetrated by the seller against purchasers. In addition to its substantive breadth, Rule 10b-5 also has broad procedural provisions; for example, process for a 10b-5 claim may be served anywhere in the world.
Private plaintiffs in Rule 10b-5 actions generally have the burden of proving the following elements:

- **Standing.** The plaintiff must be an actual purchaser or seller of the securities at issue.

- **Materiality.** The misrepresentation or omission must be of a material fact. The U.S. Supreme Court has held that a fact is material under Rule 10b-5 if there is a substantial likelihood that a reasonable investor would consider it as altering the total mix of information in deciding whether to purchase or sell the security. Generally speaking, if the disclosure of the information in question would impact the company’s stock price, the information is most likely considered material.

- **Scienter.** The defendant in question must have had scienter, or an intent to deceive, manipulate or defraud. U.S. courts have also held that scienter can be established not only by showing an actual intent to deceive, manipulate, or defraud, but also by showing that the defendant was reckless as to truth. Scienter can be refuted through showing that comprehensive due diligence was undertaken. This has given rise to the importance of “10b-5 letters” (see Chapter 11 of this Guide) in exempt transactions (such as Rule 144A and Regulation S transactions).

- **Reliance.** The plaintiff must have actually relied on the misrepresentation. However, if the undisclosed, omitted information was material, U.S. courts will generally presume reliance on the part of the plaintiff. In addition, in 10b-5 cases involving impersonal securities transactions on the open market (i.e., through a stock exchange or an over-the-counter market), U.S. courts will generally presume that the plaintiff relied on the alleged material misrepresentation and therefore dispense with the requirement that the plaintiff actually prove reliance.

- **Loss causation.** The plaintiff must have actually suffered losses proximately caused by the alleged misrepresentation or omission. Often, plaintiffs will show loss causation by pointing to a change in stock prices between the time when the alleged misrepresentations were made and the time when the alleged misrepresentations were rectified through disclosure of the correct information.

It should also be pointed out that in addition to private plaintiffs, the U.S. government itself can also bring a 10b-5 action against a defendant (although in a government action under Rule 10b-5, the government does not need to show standing, reliance or loss causation). Given its breadth and reach, Rule 10b-5 is one of the main lynchpins of the U.S. securities regulatory regime.

**CONSULTATION ON PROSPECTUS LIABILITY**

In May 2012, the SFC published a consultation paper on the regulation of sponsors. The SFC’s proposals are an effort to improve the quality of listings in Hong Kong, and they focus on the conduct of sponsors in meeting their responsibilities in connection with new listings, aiming to provide a regulatory basis for defining the expected quality of sponsor work. Prospectus liability of sponsors is one of the key proposals in the consultation paper.
B. PROSPECTUS CONTENTS

GENERAL

The prospectus should be drafted in accordance with the following major principles:

- Hong Kong legal and regulatory requirements on the form and content of prospectuses, including the disclosure of all material information to investors so as to present an accurate, complete and non-misleading picture;
- market practice regarding the structure, contents and style of the prospectuses of companies in the same industry;
- investor expectations regarding disclosure of information; and
- the characteristics of the listing applicant’s structure and business.

PRACTICAL TIP: REVIEW EARLY FOR THIRD-PARTY CONSENTS

Prior to an IPO, a company may have entered into agreements that impose restrictions on its ability to complete the IPO, including shareholder agreements that require consents to share issues, loan agreements that restrict shareholding changes, or agreements with significant business partners that contain broad “change of control” provisions that may be triggered by the IPO.

A company, with the help of its counsel, should review all of its agreements to identify these provisions and negotiate for necessary consents or waivers with the other parties involved so that they do not jeopardize the timing of the IPO. Companies will want to avoid any last minute hold-up by a shareholder, creditor, supplier or customer that could delay the offering or require the issuer to pay a consent fee or make other concessions.

The CO and the Listing Rules (Part A of Appendix 1) collectively operate to set out the minimum level of disclosure required in a prospectus. The following information pertaining to the applicant should be included, as appropriate:

- information on its general business trend and financial and trading prospects;
- details of its intended use of proceeds;
- accountants’ report covering three financial years (unless otherwise agreed by the Exchange);
- management’s discussion and analysis of the financial condition;
- property valuation;
- information about the listing applicant’s management, directors and their respective interests in the shares of the listing applicant;
• details of the substantial shareholders; and
• the various material contracts and other documents which must be made available for public inspection.

A mineral and natural resources company ("Mineral Company") is subject to additional disclosure obligations under Chapter 18 of the Listing Rules and must include the following information in its prospectus:
• a technical report prepared by a qualified independent expert as to the mining resources and/or reserves of the listing applicant. Such technical report must be prepared in accordance with the acceptable standards prescribed under the Listing Rules;
• a statement confirming no material changes since the effective date of the technical report, or where applicable, descriptions of any material changes;
• details of all prospecting, exploration, exploitation, land use and mining rights, and details of material rights to be obtained. Also, a statement of any legal claims or proceedings that may have an influence on its rights to explore or mine;
• specific and general risks with reference to Guidance Note 7 to the Listing Rules;
• disclosure on social and environmental considerations, if relevant and material; and
• for a Mineral Company not yet in production, plans for production with indicative dates and costs supported as least by a scoping study, sustained by the opinion of a qualified independent expert.

See Chapter 9 of this Guide for the conditions for listing Mineral Companies.

Typically a prospectus would include, among others, the following sections:

<table>
<thead>
<tr>
<th>Main Sections</th>
<th>Appendices</th>
</tr>
</thead>
<tbody>
<tr>
<td>Summary</td>
<td>Accountants’ Report</td>
</tr>
<tr>
<td>Risk Factors</td>
<td>Unaudited Pro Forma Financial Information</td>
</tr>
<tr>
<td>Waivers</td>
<td>Profit Forecast</td>
</tr>
<tr>
<td>Industry Overview</td>
<td>Property Valuation</td>
</tr>
<tr>
<td>Regulatory Overview</td>
<td>Summary of Articles of Association</td>
</tr>
<tr>
<td>History and Development</td>
<td>Summary of Principal Legal and Regulatory Provisions</td>
</tr>
<tr>
<td>Business</td>
<td>Statutory and General Information</td>
</tr>
<tr>
<td>Directors and Senior Management</td>
<td>Documents Delivered to the Companies Registry and Available for Inspection</td>
</tr>
<tr>
<td>Relationship with Controlling Shareholder and Directors</td>
<td></td>
</tr>
<tr>
<td>Connected Transactions</td>
<td></td>
</tr>
<tr>
<td>Financial Information</td>
<td></td>
</tr>
<tr>
<td>Future Plans and Use of Proceeds</td>
<td></td>
</tr>
<tr>
<td>Underwriting</td>
<td></td>
</tr>
</tbody>
</table>
The following briefly details certain sections set out above:

<table>
<thead>
<tr>
<th>Section</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Summary</strong></td>
<td>A summary which provides the investors with a high-level overview of the most important information in the prospectus. See Guidance Letter GL27-12 (January 2012) for guidance on the disclosure in this section.</td>
</tr>
<tr>
<td><strong>Risk Factors</strong></td>
<td>A discussion of the principal risks relating to the listing applicant's business, the industry in which it operates, the location or other context of its business and the IPO itself, that render an investment in the shares of the listing applicant risky (in order to provide maximum protection for the listing applicant, the discussion should be tailored to the specific listing applicant and not merely “boiler plate”).</td>
</tr>
<tr>
<td><strong>Industry Overview</strong></td>
<td>An introduction of the industry in which the listing applicant operates. See Guidance Letter GL8-09 (July 2009) for discussions on the use of cautionary language when including statistics, data or extracts sourced from commissioned or non-commissioned research reports in prospectuses.</td>
</tr>
<tr>
<td><strong>Regulatory Overview</strong></td>
<td>The major laws and regulations of the industry in which the listing applicant operates.</td>
</tr>
<tr>
<td><strong>History and Development</strong></td>
<td>A description of the historical developments and changes in the corporate structure of the listing applicant’s group.</td>
</tr>
<tr>
<td><strong>Business</strong></td>
<td>A description of the competitive advantages, strategies and principal businesses of the listing applicant (including but not limited to the following, as applicable: products, production facilities, production processes, sales arrangements, procurement management, quality and safety control, research and development capability, market promotion and advertising, client and pricing policies, inventory control, information technology, intellectual property rights, material litigation, personnel, properties and environmental protection issues).</td>
</tr>
<tr>
<td><strong>Directors and Senior Management</strong></td>
<td>A description of the management personnel’s qualifications and professional experience and the remuneration policies, incentive schemes and corporate governance structure of the company.</td>
</tr>
<tr>
<td><strong>Relationship with Controlling Shareholder and Connected Transactions</strong></td>
<td>A description of the controlling shareholder and its relationship with the listing applicant (e.g., potential competition) and the connected transactions of the listing applicant. See Chapter 9 of this Guide for the relevant guidance.</td>
</tr>
</tbody>
</table>
### Financial Information

The management’s discussion and analysis of historical financial information and major accounting policies. This section is the equivalent of the management’s discussion and analysis of financial condition commonly included in Rule 144A offering circulars.

This section will reflect the views of the management in relation to the listing applicant’s financial condition and operating results for the past three financial years. The discussion will comprise the group’s performance and financial trends, major reasons and influencing factors, future trends, comparisons of the operating results between the financial years, critical accounting policies and judgments, qualitative analysis of market risks, dividend policies and any other information which is material to the investors.

Also see Guidance Letter GL37-12 (June 2012), which addresses the prospectus disclosure requirements regarding indebtedness, liquidity, financial resources and capital structure.

### Future Plans and Use of Proceeds

A description of the business strategies of the listing applicant and the intended use of the IPO proceeds. See Guidance Letter GL34-12 (April 2012) for guidance on disclosure of the intended use of proceeds by listing applicants in prospectuses.

### Underwriting

A description of the underwriting arrangements and the undertakings by the underwriters with respect to the offering. See Guidance Letter GL33-12 (April 2012) for guidance on disclosure in relation to “hard underwriting” arrangements in prospectuses.

### Appendices

The prospectus will also include other important information in the form of appendices, such as an audited financial report, a property valuation report issued by a property valuation agency and any profit forecast report. See Guidance Letter GL30-12 (February 2012) for the recommended disclosure of intellectual property rights in prospectuses.

Also, see Guidance Letter GL13-09 (October 2009) for guidance on the preparation of prospectus covers.
LATEST PRACTICABLE DATE

Sufficient information must be provided to potential investors in relation to, *inter alia*, the listing applicant’s indebtedness, liquidity, financial resources, capital structure and working capital sufficiency. The Exchange expects directors and sponsors to have performed sufficient due diligence to ensure accuracy and completeness of information in a listing document and to include up-to-date information.

Guidance Letter GL38-12 (June 2012) states that the Exchange will usually accept the following:

- as the latest practicable date for inclusion of information in the prospectus – no more than 10 calendar days before the prospectus date; and
- as the latest date for the liquidity disclosure\(^1\) – no more than two calendar months before the prospectus date.

However, the Exchange requires confirmation of no adverse change in the “Summary” and “Financial Information” sections to be up to the date of the prospectus (instead of the latest practicable date).

MATERIAL CHANGES POST-TRACK RECORD PERIOD

The Exchange considers that as a minimum, sponsors and listing applicants should consider whether there is any adverse change that has taken place or is expected to take place in the near future, in the technological, market, economic, legal or operating environment in which the applicant operates.

Guidance Letter GL41-12 (August 2012) provides guidance on the prospectus disclosure of material changes in the applicant’s financial, operational and/or trading position after the trading record period. The guidance letter also lists various non-exhaustive examples of adverse changes which will require disclosure if material. Note that mitigating factors which reduce the potential impact of financial or operational loss do not negate the need to disclose the adverse changes.

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1. Paragraph 32 of Part A of Appendix 1 to the Listing Rules requires the listing document to include a statement as at the most recent practicable date (which must be stated) of the new applicant’s indebtedness (or an appropriate negative statement), liquidity, financial resources and capital structure, if material.
ACCOUNTANTS’ REPORT AND FINANCIAL STATEMENTS

The listing applicant must include an accountants’ report in the prospectus. The report must be prepared by independent certified public accountants qualified under the Professional Accountants Ordinance (Listing Rule 4.03). The Listing Rules prescribe the following requirements on the contents and standards of the accountants’ report and financial statements:

<table>
<thead>
<tr>
<th>Listing Rules</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>4.04 and 4.05</td>
<td>The accountants’ report must include the income statements and cash flow statements for the last three financial years (or any shorter period accepted by the Exchange) and balance sheets as at the end of each of the three previous financial years.</td>
</tr>
<tr>
<td>4.05A</td>
<td>If the listing applicant has completed an acquisition of any material subsidiary or business during the previous three years, which would have been classified as a major transaction (Listing Rule 14.06(3)) or very substantial acquisition (Listing Rule 14.06(5)) under the Listing Rules, then certain financial information regarding the subsidiary or business must be disclosed.</td>
</tr>
<tr>
<td>4.09</td>
<td>The accountants’ report must disclose the consolidated or combined results and the consolidated or combined balance sheet of the listing applicant and its subsidiaries and any business or subsidiary acquired or proposed to be acquired since the date of the latest audited accounts of the listing applicant.</td>
</tr>
<tr>
<td>4.11 and 4.13</td>
<td>The financial history of results and balance sheets included in the accountants’ report must be prepared in accordance with either Hong Kong Financial Reporting Standards or International Financial Reporting Standards.</td>
</tr>
<tr>
<td>4.14</td>
<td>If adjustments need to be made in preparing the accountants’ report, the reporting accountants are required to produce a written statement (the statement of adjustments), which will be made available for public inspection and which must be signed by the reporting accountants.</td>
</tr>
<tr>
<td>4.17</td>
<td>Where the reporting accountants refer to reports, confirmations or opinions of valuers, accountants or other experts, their names, addresses, and professional qualifications must be stated in the report.</td>
</tr>
<tr>
<td>4.18</td>
<td>Where the reporting accountants qualify or modify their accountants’ report, they must refer to all material matters about which they have reservations. All reasons for the qualification or modification must be given and its effect quantified if this is both relevant and practical.</td>
</tr>
<tr>
<td>8.06</td>
<td>The latest financial period reported on by the reporting accountants must not have ended more than six months before the date of the prospectus.</td>
</tr>
<tr>
<td>19.14 and 19.39</td>
<td>In certain circumstances (e.g., secondary listings), the Exchange may allow the accountants’ report to be prepared in accordance with generally accepted accounting principles in the United States of America (U.S. GAAP) or other accounting standards acceptable to the Exchange.</td>
</tr>
</tbody>
</table>
**Acquisition of Subsidiaries or Businesses During and After the Track Record Period**

In Guidance Letter GL32-12 (March 2012), the Exchange clarified the accounting and disclosure requirements with respect to the acquisition of subsidiaries or businesses by a listing applicant during or after the track record period which its accountants’ report covers. The chart below summarizes the key elements of the issues addressed in the guidance letter:

<table>
<thead>
<tr>
<th></th>
<th>During the Track Record Period</th>
<th>After the Track Record Period</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Listing Rules</strong></td>
<td>• Listing Rule 4.05A</td>
<td>• Listing Rules 4.04(2) and 4.04(4)</td>
</tr>
<tr>
<td><strong>Scope</strong></td>
<td>• Acquisitions of a material subsidiary or business (including any equity interest in another company) during the track record period</td>
<td>• Acquisitions (including any acquisition agreements and intention to acquire) of any subsidiary or business (including any equity interest in another company) after the track record period</td>
</tr>
<tr>
<td><strong>Size Test</strong></td>
<td>• 25% or more (major transaction or very substantial acquisition)</td>
<td>• No size test</td>
</tr>
<tr>
<td></td>
<td>• By comparing the assets, profits, or revenue of the subsidiary or business for the most recent financial year of the trading record period with the total assets, profits, or revenue of the applicant for the same financial year</td>
<td></td>
</tr>
<tr>
<td><strong>Disclosure Requirements</strong></td>
<td>• Pre-acquisition financial information (from commencement of the trading record period to the date of acquisition)</td>
<td>• Financial information during the trading record period</td>
</tr>
<tr>
<td></td>
<td>• In a note to accounts or separate accountants’ report</td>
<td>• In a note to accounts or separate accountants’ report</td>
</tr>
<tr>
<td></td>
<td>• Full financial statements (including information required by Listing Rules 4.04 and 4.05)</td>
<td>• Full financial statements preferred but at least include income statement and balance sheet (including information required by Listing Rule 4.05)</td>
</tr>
</tbody>
</table>
FORECASTS
The Listing Rules do not require the inclusion of a profit forecast in the prospectus. However, a listing applicant’s future profitability is one of the most important factors that a potential investor will consider in making his investment decision, and accordingly issuers may want to include a profit forecast after consultation with the sponsor. The contents and presentation of any profit forecast are subject to the following requirements under the Listing Rules:

<table>
<thead>
<tr>
<th>Listing Rule 11.16</th>
<th>Any forecast of future profits or dividend based on an assumed future level of profits must be supported by a formal profit forecast.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Listing Rule 11.17²</td>
<td>Where a profit forecast is included in the prospectus, it must be clear, unambiguous and presented in an explicit manner, and the principal assumptions, including commercial assumptions, upon which it is based must be stated. The accounting policies and calculations for the forecast must be reviewed, reported on and set out by the reporting accountants. In addition, “profit forecast” is defined widely to include:</td>
</tr>
<tr>
<td></td>
<td>• any forecast of profits or losses, however worded;</td>
</tr>
<tr>
<td></td>
<td>• any statement that explicitly or implicitly quantifies the anticipated level of future profits or losses, either expressly or by reference to previous profits or losses or any other benchmark or point of reference; and</td>
</tr>
<tr>
<td></td>
<td>• any profit estimate, being any estimate of profits or losses for a financial period which has expired but for which the results have not yet been audited or published.</td>
</tr>
<tr>
<td>Listing Rule 11.18</td>
<td>The profit forecast should normally cover a period which corresponds to the issuer’s financial year-end. If the profit forecast period ends at a half year-end, the Exchange will require an undertaking from the issuer that the interim report for that half year will be audited.</td>
</tr>
<tr>
<td>Listing Rule 11.19</td>
<td>The underlying assumptions of the profit forecast must provide useful information to the investors to help them form a view as to the reasonableness and reliability of the forecast. Such assumptions should draw the investors’ attention to, and where possible quantify, those uncertain factors which could materially disturb the ultimate achievement of the forecast. The assumptions should be specific rather than general and definite rather than vague.</td>
</tr>
</tbody>
</table>

If the issuer’s actual results of operation deviate from the profit forecast following its listing, the issuer must consult with its compliance adviser and issue an announcement to clarify the differences. Also, it must include an explanation for the deviation in the annual report.

² Listing Rule 11.17 requires principal assumptions on which a profit forecast is based to be stated in a listing document. However, the requirement to state assumptions is not applicable to a profit estimate, as it relates to a financial period which has ended (Guidance Letter GL35-12 (May 2012)).
PROPERTY VALUATION REPORTS

Pursuant to a general disclosure obligation under the CO and the Listing Rules, listing applicants and listed issuers must disclose in any prospectus relevant and meaningful information regarding any material properties. The Exchange expects applicants, issuers and sponsors to consider all facts and circumstances to determine if a property is material and, if it is, to disclose property valuation and/or other relevant information.

However, certain property valuation exemptions apply to property interests in (i) business activities involving holding/developing properties for subsequent sale or as investments (“property activities”); and (ii) other business activities such as own use (“non-property activities”). See Chapter 5 of the Listing Rules for details.

Below is a summary of property interests exempted from valuation requirements:

<table>
<thead>
<tr>
<th>Exempt Property Interests (No Property Valuation Required)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Listing Applicants</strong></td>
</tr>
<tr>
<td>For property activities: property interests with an individual carrying amount below 1% of the applicant’s total assets are exempted, provided that the total carrying amount of property interests not valued must not exceed 10% of its total assets.</td>
</tr>
<tr>
<td>For non-property activities: property interests with individual carrying amount below 15% of the applicant’s total assets are exempted.</td>
</tr>
<tr>
<td>Property interests held under operating leases are exempted.</td>
</tr>
<tr>
<td>Property interests ancillary to mining activities are exempted if the mining activities and ancillary property interests have been valued as a business or an operating entity.</td>
</tr>
<tr>
<td>Not applicable</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>
SPECIFIC LISTING ISSUES

A. LISTING APPLICANTS FROM OVERSEAS JURISDICTIONS

ACCEPTABLE JURISDICTIONS

In addition to the four jurisdictions recognized under the Listing Rules (i.e., Hong Kong, the PRC, Bermuda and the Cayman Islands), the following jurisdictions have been accepted by the Exchange as suitable for listing in Hong Kong, and the list is expected to continue growing:

<table>
<thead>
<tr>
<th>Australia</th>
<th>ACCEPTABLE OVERSEAS JURISDICTIONS</th>
<th>Brazil</th>
</tr>
</thead>
<tbody>
<tr>
<td>British Virgin Islands</td>
<td>Canada’s Alberta, British Columbia and Ontario</td>
<td>Cyprus</td>
</tr>
<tr>
<td>Guernsey</td>
<td>Isle of Man</td>
<td>Italy</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Singapore</td>
<td>South Korea</td>
</tr>
<tr>
<td>USA’s California, Delaware and Maryland</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

GENERAL FRAMEWORK

The general framework for determining the suitability for listing of an overseas listing applicant is set out in Chapter 19 of the Listing Rules. In particular, Listing Rule 19.05(1) provides that the Exchange may refuse a listing of securities of an overseas issuer if:

- the Exchange believes that it is not in the public interest to list it; or
- the Exchange is not satisfied that the overseas issuer is incorporated or otherwise established in a jurisdiction in which the standards of shareholder protection are at least equivalent to those provided in Hong Kong.

The Exchange and the SFC issued a Joint Policy Statement in 2007 to facilitate the listing of overseas issuers by clarifying the requirements under the Listing Rules and setting out the principal shareholder protection requirements to be satisfied by an overseas incorporated issuer. These requirements include:

- a corporate structure that clearly protects principal shareholder rights;
- fair proceedings for general meetings to enable shareholders to utilize their rights in full;
• corporate governance measures that ensure that the powers of the directors are reasonably contained and subject to reasonable scrutiny;
• the capital maintenance concept is enshrined in the applicant’s corporate structure and with respect to all its corporate actions; and
• the overseas jurisdiction has sufficient arrangements in place to ensure reasonable regulatory cooperation between the statutory securities regulators there and in Hong Kong.

STREAMLINED VETTING

To streamline the procedures for listing of overseas companies, the Exchange published Guidance Letter GL12-09 (September 2009), which allows a listing applicant to ride on a first issuer’s arrangements, as well as benchmark the shareholder protection standards in its home jurisdiction against any one of the recognized or accepted jurisdictions. Therefore, it is not necessary for a listing applicant to demonstrate parallel shareholder protection mechanisms with Hong Kong, provided that its standards are not lower than those indicated in the relevant listing decisions. However, the applicant must also demonstrate that there is a reasonable nexus between its business operations and the relevant jurisdiction.

The Exchange emphasized in the guidance letter that potential overseas issuers and their advisers should consult the Exchange early to determine whether a particular jurisdiction is acceptable for listing before submitting a formal listing application. The Exchange will then accept listing applications after consulting the Listing Committee on the acceptability of the relevant jurisdiction.

In considering whether a new jurisdiction is acceptable, the Exchange adopts a purposive interpretation of shareholder protection equivalence requirements. It is not necessary for the shareholder protection regime in an overseas jurisdiction to show textual resemblance. For example, Hong Kong law requires a three-quarters majority vote by shareholders to pass certain resolutions, whereas the corresponding law of an overseas jurisdiction may require only a two-thirds majority vote of shareholders. The Exchange still considers the latter regime as acceptable, although it is not strictly equivalent to the Hong Kong requirement. The issuer, however, must disclose the differences in its prospectus.

Further, the Exchange does not rigidly require an overseas issuer to amend its constitutional documents to ensure equivalent standards of shareholder protection. Instead, the Exchange allows a listing applicant to demonstrate comparable shareholder protection by alternative means, for example, by demonstrating that compliance with rules of the local exchange on which it is listed would result in the same investor protection.

B. PRC BUSINESSES

PRC businesses may seek a listing by offering H shares or by way of a red-chip offering. In each case, the listing applicant may need to obtain approval from PRC government or regulatory authorities. A PRC-incorporated listing applicant is typically required to submit a copy of the CSRC approval before the Listing Committee hearing. Also, the listing applicant is required to submit a PRC legal opinion covering various aspects of PRC laws and regulations. Further, the Exchange requires that the sponsor(s) must have obtained and reviewed documentation from the relevant PRC tax bureau, confirming the tax rate to
which the listing applicant is subject and confirming that the listing applicant has paid the relevant tax. In practice, the process of obtaining such confirming documentation is often time consuming.

Chapter 19A of the Listing Rules specifically governs the listing of companies incorporated in the PRC by setting out additional requirements and modifications of the Listing Rules. It prescribes, among other things, the following requirements with respect to a PRC-incorporated listing applicant:

<table>
<thead>
<tr>
<th>Due Incorporation (Listing Rule 19A.03)</th>
<th>A PRC issuer must be duly incorporated as a joint stock limited company in the PRC and must be in compliance with PRC laws and regulations and its articles of association.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sufficient Shareholder Protection (Listing Rule 19A.03)</td>
<td>The Exchange must be satisfied that applicable PRC laws and the PRC issuer’s articles of association provide a sufficient level of shareholder protection to H shareholders.</td>
</tr>
<tr>
<td>Articles of Association (Listing Rule 19A.01)</td>
<td>A PRC issuer’s articles of association must contain provisions that reflect the different nature of H shares and domestic shares (and the different rights of these shareholders) and that disputes arising between shareholders and the PRC issuer should be resolved by arbitration.</td>
</tr>
<tr>
<td>Compliance Adviser (Listing Rules 19A.05 and 19A.06)</td>
<td>A PRC issuer is required to retain a compliance adviser from the date of listing until it distributes its annual report with respect to the financial results for the first full financial year. The compliance adviser must be a corporation licensed by the SFC to act as a sponsor and is required to act impartially. Often an issuer will appoint the IPO sponsor as its compliance adviser. A PRC issuer may not terminate its compliance adviser until it has appointed a replacement. If the Exchange is not satisfied that the compliance adviser is fulfilling its responsibilities, it may require the PRC issuer to terminate the appointment.</td>
</tr>
<tr>
<td>Accountants’ Report (Listing Rule 4.11)</td>
<td>A PRC issuer may present its accounts in conformity with the CASBE (instead of HKFRS or IFRS) if it has adopted the CASBE for the preparation of its annual financial statements.</td>
</tr>
</tbody>
</table>

C. MINERAL AND NATURAL RESOURCES COMPANIES

To promote the Exchange as a listing platform for overseas mining and natural resources companies, the Exchange updated Chapter 18 of the Listing Rules in June 2010. The revisions clarified and updated the Listing Rules and synchronized them in certain important respects with globally recognized standards. In addition to listing applicants, the revised Chapter 18 also affects existing listed mineral companies, as well as other listed entities that acquire or dispose of mineral or petroleum assets as part of a transaction that is a major transaction, very substantial acquisition/disposal or reverse takeover.
Conditions for listing mineral and natural resources companies are as follows:

| Rights to Exploration and/or Extraction and Control of Assets | The applicant must have the right to participate actively in the exploration for and/or extraction of natural resources:  
- through control of a majority (>50% by value) of the assets in which it has invested, together with adequate rights over such exploration and/or extraction; or  
- through adequate rights that give it sufficient influence in decisions over such exploration and/or extraction.  
“Adequate rights” include exploration and extraction rights held by third parties under joint, product sharing or other valid arrangements, if the applicant can demonstrate enough influence over the exploration and extraction. Rights granted under specific government mandates will be recognized. If a company has not yet started production and cannot show it has extraction rights until later, the risks relevant to obtaining such rights must be disclosed. |
| --- | --- |
| Portfolio | The applicant must at least have a sufficiently substantial portfolio of Indicated Resources of minerals (as defined in the Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves (the “JORC Code”), or Contingent Resources of petroleum (as defined in the Petroleum Resources Management System ("PRMS")). Preproduction mineral companies must also:  
- outline their plans to proceed to production, with indicative dates and costs; and  
- be supported by a scoping study evaluating the mineral project (including economic viability), to be substantiated by the opinion of a competent person. |
| Competent Person’s Report | The resources must be substantiated by an independent technical report under recognized reporting standards (see below). The report must be prepared by a competent person, being a person who:  
- has appropriate professional qualifications and is in good standing;  
- has at least five years’ relevant experience; and  
- is independent of the applicant and its directors, senior management and advisers. |
| Cash Operating Costs | If production has begun, an estimate of cash operating costs is required for items including costs associated with workforce employment, consumables, non-income taxes and royalties, as well as other governmental charges and contingency allowances. |
| Working Capital Requirements | Working capital must be at least 125% of budgeted working capital needs for the 12 months following the date of the listing document. |
The reporting standards acceptable to the Exchange are currently:

- for petroleum resources and reserves – PRMS; and
- for valuations – Canada’s CIMVAL Code, South Africa’s SAMVAL Code and Australasia’s VALMIN Code.

If a mineral company cannot satisfy the usual requirements under Listing Rule 8.05, it may nevertheless be eligible for listing under the following alternative listing requirements:

The financial track record requirements in Listing Rule 8.05 can be waived if the mineral company can satisfy the Exchange that its directors and senior managers, taken together, have sufficient experience relevant to the exploration and/or extraction activity that it is pursuing. Individuals relied on must have a minimum of five years’ relevant industry experience.

Applicants that are already in production will usually need a demonstrable path to profitability. For example, a mineral company incurring expenditures for further exploration or development activities, which have contributed to its inability to meet the profit requirements, is likely to be considered favorably for a waiver.

However, a mineral company unable to meet the profit requirements with all of its mining assets in operation and no development activity on hand will not be able to seek a waiver.

D. COMPETING BUSINESS OF CONTROLLING SHAREHOLDER AND INDEPENDENCE FROM PARENT COMPANY

It is a fundamental requirement under Part A of Appendix 1 of the Listing Rules that the prospectus disclose how the issuer is satisfied that it is capable of carrying on its business independently of the controlling shareholder (including any associate of such controlling shareholder) after listing, as well as particulars of the matters that it relied on in making the statement.

It is common for a listing applicant to have a controlling shareholder (i.e., a shareholder who holds at least 30% of the voting rights or controls the composition of its board). In assessing a listing applicant's independence, the Exchange will consider the applicant's financial aspects, operational aspects (such as independent access to supplies/raw materials for production, independent access to customers and independence of production/operation capabilities) and management aspects.
Financial Independence

A common way to demonstrate the listing applicant’s financial independence is by repaying or capitalizing all outstanding loans due to, and releasing guarantees provided by, its parent before listing.

While the Exchange accepts the release method to demonstrate an applicant’s financial independence of its parent, it is not a mandatory requirement. The Exchange has accepted other methods to demonstrate an applicant’s financial independence, such as using the IPO proceeds to repay shareholder loans.

In Listing Decision LD69-1, the Exchange determined that the listing applicant could operate financially independently of its controlling shareholder, taking into account the following:

- it had a record of fund-raising on a stand-alone basis without any credit support from the controlling shareholder;
- it had received firm offers from a number of independent financial institutions to provide generally equivalent finance facilities, on a stand-alone basis, to refinance the loans secured by the controlling shareholder’s guarantees; and
- it had a strong financial position.

Satisfied that the listing applicant was financially independent of its controlling shareholder, the Exchange determined that:

- the controlling shareholder’s guarantees of the listing applicant’s banking facility need not be released before or at the time of listing; and
- the listing applicant would be permitted to ask its controlling shareholder for a secured loan facility to refinance the existing loans, if the terms offered by independent third parties were considered by the directors to be less favorable.

Operational Independence

In Listing Decision LD46-1, the Exchange noted that the level of reliance that the listing applicant placed on its controlling shareholder for sales and procurement functions gave rise to concerns such as transfer pricing, conflicts of interest, substantial reliance on the protection mechanisms offered by the connected transaction requirements under the Listing Rules and how performance of the listed part of the company may be independently evaluated.

The Exchange thus determined that the applicant should take concrete steps to address the issue of reliance before it would consider any further review of the listing application.

In Listing Decision LD46-2, the Exchange determined that the level of reliance that the listing applicant had placed on its controlling shareholder could be addressed by prospectus disclosure, including a description of the associated risks, provided that adequate mechanisms were put in place to protect minority shareholders.
The test of management independence is similar to the principle set out under Paragraph 3(d) of Practice Note 15, in which the Exchange requires that it be satisfied that the listing applicant would operate independently and in the interests of its shareholders as a general body, and not in the interests of the controlling shareholder only, when the interests of the applicant and its controlling shareholder are actually or potentially in conflict.

In Listing Decision LD52-2, the Exchange considered factors including the number of common directors between the listing applicant and its controlling shareholder, the respective roles of the common directors, the extent of the delineation between the two operations, the number and amount of continuing connected transactions, and the independence of the senior management of the listing applicant and the controlling shareholder.

If a controlling shareholder of the listing applicant has an interest in another business that competes with that of the applicant, certain disclosure and compliance requirements must be satisfied by the issuer (Listing Rule 8.10). The common approach to resolving the competition issue is for the issuer to enter into a noncompetition undertaking with the controlling shareholder, in which the controlling shareholder undertakes not to compete with the issuer in the manner specified in the undertaking. If such an undertaking is entered into, the Exchange would require that details of the undertaking be disclosed in the listing document. While competition is normally a disclosure issue, in extreme cases in which there are inadequate arrangements to manage conflicts of interest and delineation of businesses between the applicant and other businesses under common control, the Exchange would consider the impact on the applicant’s suitability for listing.

E. CONNECTED TRANSACTIONS

Connected transactions may be either one-off transactions (in the case of listed issuers) or continuing transactions (in the case of both listed issuers and new applicants). The connected transactions rules are intended (i) to ensure that the interests of shareholders as a whole are taken into account by a listed issuer when the listed issuer enters into connected transactions and (ii) to provide certain safeguards against listed issuers’ directors, chief executives or substantial shareholders (or their associates) taking advantage of their positions.

Generally speaking, connected transactions are required to be disclosed after listing of an issuer’s securities and are subject to independent shareholders’ approval. Accordingly, when a connected transaction is proposed, in general the transaction must be announced publicly by means of an announcement and a circular must be sent to shareholders giving information about the transaction. Prior approval by the shareholders in a general meeting is often required before the transaction can proceed.

However, certain categories of transaction are exempt from the disclosure and independent shareholders’ approval requirements, and certain transactions are subject only to disclosure requirements. See the “Plain Language Guide on Connected Transaction Rules” published by the Exchange for further details.
### What are Connected Transactions?

Connected transactions include transactions between a group and connected persons.

Connected transactions also include transactions between a group and third parties that may confer benefits on connected persons. Such transactions relate to investments in, or financing arrangements with, companies in which the group and its directors, chief executives or controlling shareholders are, or will as a result of the transactions become, shareholders.

Connected transactions include both capital and revenue transactions. They may be one-off transactions or continuing transactions.

### Who are Connected Persons?

Connected persons of an issuer are persons who can control or exercise significant influence over the group or who stand to benefit from transactions with the group.

They include chief executives and substantial shareholders of the issuer or its subsidiaries, and any persons closely associated with them.

The scope of connected persons also includes an issuer’s non-wholly owned subsidiary if it is substantially held by chief executives and/or substantial shareholders at the level of the issuer (and/or their associates).

### Requirements for Connected Transactions

The general requirements for connected transactions include disclosures in announcements and annual reports, and shareholders’ approval. Persons with material interests cannot vote on the resolution approving the transaction. Continuing connected transactions also require annual reviews by independent non-executive directors and the auditors.

### Exemptions and Waivers

To reduce issuers’ compliance burden, exemptions and waivers from all or some of the connected transaction requirements are available during the new listing application process for specific categories of connected transactions. These apply to connected transactions that are immaterial to the group, or specific circumstances in which the risk of abuse by connected persons is low.

A connected person is:

1. a director, chief executive or substantial shareholder of the issuer or any of its subsidiaries;
2. a person who was a director of the issuer or any of its subsidiaries in the past 12 months;
3. a supervisor of a PRC issuer or any of its subsidiaries;
4. an associate of any of the above persons;
5. a connected subsidiary of the issuer (i.e., a subsidiary of which 10% or more of the voting power is controlled by persons in categories (1) to (4) above); or
6. a person deemed by the Exchange to be connected, based on certain extended family relationships, or on the person’s proposed or actual arrangement with a person in categories (1) to (3) above regarding the relevant transaction.
An associate of an individual includes:

1. a spouse, his/her (or his/her spouse’s) child (natural or adopted) or stepchild under the age of 18 years (each an “immediate family member”);
2. 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 “trustee”);
3. a 30%-controlled company held by the individual, his immediate family members and/or the trustees (individually or together), or any of its subsidiaries;
4. a person cohabiting with him/her as a spouse, or his/her child, stepchild, parent, step-parent, brother, stepbrother, sister or stepsister (each a “family member”); or
5. a majority-controlled company held by his family members (individually or together), or of which his family members control the composition of a majority of the board of directors.

An associate of a corporation includes:

1. its subsidiary or holding company, or a fellow subsidiary of the holding company (together the “group companies”);
2. the trustees, acting in their capacity as trustees of any trust of which the company is a beneficiary or, in the case of a discretionary trust, is (to its knowledge) a discretionary object (the “trustees”); or
3. a 30%-controlled company held by the company, the group companies and/or the trustees (individually or together), or any of its subsidiaries.

EXEMPTIONS

Connected transactions are classified by a combination of their nature and size. They can be broadly divided into three categories:

- Wholly exempted – exempt from all reporting, announcement and independent shareholders’ approval (Listing Rules 14A.31 and 14A.33);
- Partially exempted – exempt from independent shareholders’ approval but subject to certain reporting and announcement requirements (Listing Rules 14A.32 and 14A.34); or
- Non-exempt – subject to reporting, announcement and independent shareholders’ approval requirements (Listing Rule 14A.17).

The percentage ratios below (collectively referred to as the “percentage ratios”) are applicable for determining whether a connected transaction/continuing connected transaction qualifies as a wholly exempt or partially exempt connected transaction:

1. Assets ratio – the total assets that are the subject of the transaction, divided by the total assets of the listed issuer;

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1. For ease of presentation, certain types of associate are set out in the preceding list of the categories of connected persons.
(2) Revenue ratio – the revenue attributable to the assets that are the subject of the transaction, divided by the revenue of the listed issuer;

(3) Consideration ratio – the consideration divided by the total market capitalization of the listed issuer. The total market capitalization 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

(4) 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.

If the amount of a relevant connected transaction/continuing connected transaction is lower than the designated threshold according to the appropriate percentage ratio, that transaction may qualify as a wholly exempt or partially exempt connected transaction. The following table summarizes the relevant thresholds:

<table>
<thead>
<tr>
<th>Category</th>
<th>Exemption</th>
<th>Thresholds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wholly Exempted</td>
<td>Exempted from all the reporting, announcement and independent shareholders’ approval requirements</td>
<td>Each or all of the percentage ratios is/are:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(a) less than 0.1%; or</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(b) less than 1% and the transaction is a connected transaction only because it involves a person who is a connected person of the listed issuer by virtue of his relationship(s) with the issuer’s subsidiary or subsidiaries; or</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(c) less than 5% and the total consideration is less than HK$1 million.</td>
</tr>
<tr>
<td>Partially Exempted</td>
<td>Exempted from independent shareholders’ approval requirements</td>
<td>Each or all of the percentage ratios (other than the profits ratio) is/are:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(a) less than 5%; or</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(b) less than 25% and the total consideration is less than HK$10 million.</td>
</tr>
</tbody>
</table>
CONTINUING CONNECTED TRANSACTIONS OF NEW APPLICANTS

A listing applicant may apply to the Exchange for waiver of the announcement, circular and shareholders’ approval requirements for continuing connected transactions entered into by it or its subsidiaries. The listing applicant must disclose in the listing document its sponsor’s opinion on whether the transactions are in the group’s ordinary and usual course of business, on normal commercial terms, are fair and reasonable and are in the interests of the shareholders as a whole. The sponsor is also typically required to opine on the fairness and reasonableness of the proposed annual caps of the continuing connected transactions.

F. PRE-IPO AND POST-IPO SHARE OPTION SCHEMES

PRE-IPO SHARE OPTION SCHEMES

To attract and retain key employees and incentivize management performance, listing applicants often establish share option schemes. A share option scheme created before the IPO (a “Pre-IPO Share Option Scheme”) will generally be structured to comply with the Listing Rules to the extent possible, although there is no requirement for compliance.

If a Pre-IPO Share Option Scheme does not comply with the Listing Rules, options granted prior to listing remain valid after listing (subject to approval for listing of the underlying shares), but no further options may be granted under the scheme after listing. Such schemes typically provide that the option exercise price will represent a limited discount to the IPO price.

Further, the listing applicant is required to disclose in the prospectus full details of all outstanding options, as well as the grantees and the potential dilution effect and impact on earnings per share upon exercise of the options. However, the SFC and the Exchange would normally grant waivers from disclosing the names and addresses of certain grantees if the applicant can demonstrate that such disclosures would be irrelevant or unduly burdensome.

POST-IPO SHARE OPTION SCHEMES

The terms of a share option scheme created after listing (a “Post-IPO Share Option Scheme”) must comply with Chapter 17 of the Listing Rules, which includes the following provisions:

<table>
<thead>
<tr>
<th>Eligible Grantees</th>
<th>Directors and employees of the group and other persons who have or will contribute to the group are generally eligible grantees.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Shares to be Issued</td>
<td>The total number of shares that may be issued upon exercise of all options to be granted under all share option schemes must not in aggregate exceed 10% of the issued shares on the date the scheme was approved.</td>
</tr>
<tr>
<td>The 10% Limit</td>
<td>The scheme will require shareholders’ approval, and the “refreshed” limit must not exceed 10% of the issued shares as of the date of approval. Options previously granted under the scheme will not be counted for the purpose of calculating the “refreshed” limit.</td>
</tr>
</tbody>
</table>
The total number of shares that may be issued upon exercise of all outstanding options granted and yet to be exercised under all schemes must not exceed 30% of the issued shares from time to time. No options can be granted if this would result in the limit being exceeded.

Unless approved by shareholders, the maximum number of shares issued and to be issued on exercise of the options granted to any grantee in any 12-month period must not exceed 1% of the issued shares.

The exercise price must be the higher of (i) the closing price on the date of grant and (ii) the average closing price for the five business days preceding the date of grant (or the IPO price when the company has been listed for less than five days).

The period within which the shares must be taken up under the option must not be more than 10 years from the date of the grant.

The life of the scheme must not be more than 10 years from the date of its adoption.

Options granted are personal to the grantee and may not be transferred or assigned.

When an option is to be granted to a director, chief executive or substantial shareholder (or their respective associates), the grant must be approved by the INEDs (excluding any INED who is the grantee). Similarly, an option granted to a substantial shareholder or INED (or their respective associates) would require approval from shareholders, if such a grant will result in the grantee holding options representing in aggregate over 0.1% of the issued shares or if the aggregate value of the options granted is greater than HK$5 million (based on closing price at date of grant).

**G. HONG KONG DEPOSITARY RECEIPTS (“HDRs”)**

Depositary receipts (“DRs”) are securities issued by a depositary representing underlying shares of the issuer, which have been placed with the depositary or its nominated custodian. The actual securities listed are the underlying shares represented by DRs. The depositary acts as the agent for the issuer in dealing with the DR holders.

The HDR framework is an alternative facility for issuers to list on the Exchange. Chapter 19B provides that an issuer may list its securities as HDRs, and the Listing Rules apply in the same manner as to the listing of other equity securities. An issuer seeking to list in Hong Kong through HDRs generally will have to comply with the same requirements as an issuer of shares. The requirements of the Listing Rules for admission to listing and the relevant guidance material such as the Joint Policy Statement Regarding the Listing of Overseas Companies, as well as the continuing obligations and relevant statutes, will apply to an HDR issuer in the same manner as to an issuer of shares.
A DR will represent a number of underlying shares (or a fraction of a single share), according to the DR ratio. The depositary converts dividends into the host market currency and pays the amounts (net of its own fees) to the DR holders. The depositary also transmits other entitlements and corporate communications from the issuer to the DR holder and transmits the DR holder’s instructions back to the issuer. The rights and obligations of the issuer, the depositary and the DR holders are set out in the deposit agreement.

Most important, the trading, clearing and settlement arrangements for HDRs will be the same as the arrangements for shares.

Listing in HDR form may provide the following advantages for issuers and investors:

<table>
<thead>
<tr>
<th>For Issuers</th>
<th>For Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>• A practical method for overseas issuers to list in Hong Kong if there are regulations or policies in their domestic jurisdictions that:</td>
<td>• Delegation of foreign tax administration to the depositary</td>
</tr>
<tr>
<td>(i) prevent them from listing overseas in the form of ordinary shares;</td>
<td>• Dividend payments in the investor’s local currency</td>
</tr>
<tr>
<td>(ii) prevent the holding of ordinary shares overseas;</td>
<td>• Better information flow from issuer in the investor’s language (with the assistance of the depositary)</td>
</tr>
<tr>
<td>(iii) prohibit the establishment of a branch register overseas, or splitting of the share register; or</td>
<td></td>
</tr>
<tr>
<td>(iv) require direct holders of the issuer’s shares to be licensed as foreign investors.</td>
<td></td>
</tr>
<tr>
<td>• A convenient means to “resize” the issue when the issuer’s shares are of a very different price per board lot from that customarily used in Hong Kong</td>
<td></td>
</tr>
<tr>
<td>• Reduced time for transfer with the operation of pre-release</td>
<td></td>
</tr>
<tr>
<td>• Reduced potential legal risks with dematerialized shares in their home market</td>
<td></td>
</tr>
<tr>
<td>• Flexibility in deciding the amount of DRs with respect to which listing is sought, to reflect actual trading needs</td>
<td></td>
</tr>
</tbody>
</table>
The listing and operation of HDRs are generally subject to the following rules of Chapter 19B.

<table>
<thead>
<tr>
<th>HDR Characteristics (Listing Rule 19B.09)</th>
<th>The DRs must be freely transferable, and the underlying shares must be fully paid and free from all liens and any restriction on the right of transfer to the depositary.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Issuer’s Register (Listing Rule 19B.13)</td>
<td>The issuer is not required to keep a register in Hong Kong of holders of the shares represented by depositary receipts. However, the issuer must ensure that the depositary maintains, through an approved Hong Kong share registrar, a register of DR holders and the transfers of the depositary receipts in Hong Kong.</td>
</tr>
<tr>
<td>The Depositary (Listing Rules 19B.14 and 19B.15)</td>
<td>The depositary is required to (a) be duly incorporated and operate in conformity with its constitutional documents, (b) be a suitably authorized and regulated financial institution acceptable to the Exchange and (c) have adequate experience in issuing and managing DR programs in Hong Kong or overseas.</td>
</tr>
</tbody>
</table>
| Deposit Agreement (Listing Rule 19B.16) | The deposit agreement must be in a form acceptable to the Exchange. It must be executed by the depositary and the issuer and must provide that the depositary holds on trust (or equivalent arrangements) for the sole benefit of the DR holders. The agreement must also provide, among others:  
• the appointment of the depositary by the issuer;  
• the status of the DRs as instruments representing ownership with respect to the underlying shares;  
• the status of a registered holder of depositary receipts as the legal owner;  
• the role of the depositary to issue depositary receipts as agent of the issuer; and  
• the duties of the depositary. |
| Continuing Obligations (Listing Rule 19B.17) | The issuer is responsible for ensuring the continued suitability of the depositary. It should notify the DR holders of any change of depositary by announcement that identifies the incoming depositary and seeks the consent of the DR holders for any material changes to the deposit agreement, including changes to the rights and obligations of holders of depositary receipts and any changes to the fees and charges payable to the depositary. |
| Listing of HDRs | The methods of listing for HDRs are the same as for issuers of shares: Chapter 7 of the Listing Rules applies to HDR issuers in the same way as it applies to equity offerings. Accordingly, HDR issuers may list by way of introduction if the requirements of Listing Rules 7.13 to 7.17 are met, and a placing of HDRs will not normally be permitted if there is expected to be significant public interest in an issue. |
| Listing Documents Disclosure | Parts E and F of Appendix 1 to the Listing Rules have stipulated additional disclosure requirements for the listing documents of an HDR. |
H. BUSINESS TRUSTS

The Exchange, in conjunction with the SFC, began in early 2011 to explore ways to list active businesses by way of a business trust under the existing Hong Kong regulatory framework. Much of the impetus for this exploration came from competition from jurisdictions such as Singapore, which has permitted the listing of business trusts since 2004. Very generally, business trusts are established by a trust deed and are managed by a trustee manager, which operates the business and holds legal title to assets for beneficiaries. These beneficiaries do not have day-to-day control over the management of these assets, but they will be able to receive profits or returns from the business trust. Given that business trusts effectively operate as business enterprises, the Exchange considers their listing applications and regulates them by applying the same principles in the Listing Rules as those applied to companies.

Guidance Letter GL40-12 (August 2012) sets out the applicable principles and key issues that a business trust should address when preparing a listing. The overriding principle set forth in the guidance letter is to ensure that holders of units in business trusts are subject to comparable investor protection standards as shareholders of Hong Kong corporate issuers, and key relevant SFO provisions must apply. The guidance letter also suggests possible approaches listing applicants may consider in addressing particular issues.

HKT Trust, a business trust spin-off of PCCW Limited, was the first business trust listed in Hong Kong in November 2011, after it obtained listing approval from the Exchange in June 2011. The offering was structured as a “stapled security” (a method adopted from Australia’s framework for stapled securities) by which a HKT Trust unit was stapled to a specifically identified preference share of HKT Limited (i.e., the underlying, listed corporation) and linked to a beneficial interest in a specifically identified ordinary share of HKT Limited, with the ordinary shares legally held by the trustee manager of HKT Trust.

A subscriber for HKT Trust would subscribe for a “share stapled unit,” which comprises the above HKT Trust unit, the beneficial interest in the specifically identified ordinary share and the specifically identified preference share. There is a single price quotation on the Exchange for the share stapled unit, which can be traded only as a whole.

I. STRUCTURED CONTRACTS

Listing applicants have, since 2004, adopted various contract-based arrangements (typically known as structured contracts or variable interest entity (“VIE”) arrangements) to give the applicants contractual rights to gain control over and receive all economic benefits derived from businesses in industries where foreign ownership is restricted, despite their not holding any equity interest in these businesses. Industries in the PRC that typically limit foreign investment are publishing, shipbuilding, pawn businesses and Internet content providers.

The suitability of listing applicants with structured contracts was discussed by the Listing Committee in 2004 as a policy issue. The Listing Committee decided that such applicants are suitable for listing as long as they can demonstrate that their adoption of structured contracts is in compliance with all relevant laws and regulations and that the structured contract arrangements are binding and enforceable. However, this was reviewed in 2011, and the Listing Committee decided that it was not appropriate to allow the use of structured contracts generally in all businesses and circumstances. The Listing Committee endorsed the
Exchange’s established practice that the use of structured contracts would be considered on a case-by-case basis.

**TYPICAL STRUCTURED CONTRACT/VIE ARRANGEMENT**

THE EXCHANGE’S STANDARD OF REVIEW

Listing Decision LD43-3 provides guidance on the Exchange’s standard of review in relation to structured contracts, including:

- Structured contracts must be narrowly tailored to achieve business purposes and minimize potential for conflict with the relevant laws and regulations.
- Applications will be considered on a case-by-case basis after considering the reasons for adopting the arrangements.
- If non-restricted businesses are involved, the cases will be referred to the Listing Committee.
- The listing applicant and its sponsor should:
  - provide reasons for using the structured contracts in the listing applicant’s business operations;
  - unwind the structured contracts as soon as possible once the law allows operation of the business without them;
  - include a power of attorney in the structured contracts by which the listing applicant’s directors and their successors are empowered by the operating company’s shareholders to exercise all the rights of the operating company’s shareholders;
– include appropriate dispute resolution clauses in the structured contracts; and
– ensure that the structured contracts encompass dealing with the operating company’s assets and not only the right to manage its business and the right to revenue.

• The Exchange will conduct a broad review of the facts and circumstances of the listing applicant, including its compliance history, financial resources, corporate governance practices, record in protecting shareholder interests and its financial resources to ensure compliance with the applicable laws and regulations. If material uncertainties are identified in areas of the applicant’s business, a higher level of assurance with respect to the arrangements will be required.

• Appropriate regulatory assurance must be obtained.

REQUIRED DISCLOSURES

An applicant using structured contracts for all or part of its business is required to disclose the following information concerning the structured contracts in its prospectus:

<table>
<thead>
<tr>
<th>Risk Factors</th>
<th>As a minimum, the risk factors should include the following:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>• the PRC government may determine that the structured contracts do not comply with applicable regulations;</td>
</tr>
<tr>
<td></td>
<td>• the structured contracts may not provide control as effective as direct ownership;</td>
</tr>
<tr>
<td></td>
<td>• the domestic shareholders may have potential conflicts of interest with the applicant; and</td>
</tr>
<tr>
<td></td>
<td>• structured contracts may be subject to scrutiny of the PRC tax authorities and additional tax may be imposed.</td>
</tr>
<tr>
<td>All related risk factors should be disclosed under a heading such as “Risks Relating to Corporate Structure.”</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>The Operating Company’s Registered Shareholders</th>
<th>A detailed discussion about the operating company’s registered shareholders and a confirmation that appropriate arrangements have been made to protect the applicant’s interests in the event of death, bankruptcy or divorce of the operating company’s registered shareholders, to avoid any practical difficulties in enforcing the structured contracts.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potential Conflicts of Interest</td>
<td>The extent to which the applicant has arrangements in place to address the potential conflicts of interest between the applicant and the operating company’s registered shareholders, particularly when these shareholders are officers and directors of the applicant.</td>
</tr>
<tr>
<td>Directors’ Belief</td>
<td>Bases for the directors’ belief that each of the agreements passing significant control and economic benefits from the operating company to the applicant is enforceable under the PRC and local law.</td>
</tr>
<tr>
<td>Economic Risks</td>
<td>The economic risks the applicant bears as the primary beneficiary of the operating company, in what way the applicant shares the losses of the operating company, the circumstances that could require the applicant to provide financial support to the operating company, or other events or circumstances that could expose the applicant to losses.</td>
</tr>
<tr>
<td>Any Interference or Encumbrance from PRC Governing Bodies</td>
<td>A discussion about whether the applicant has, to date, encountered any interference or encumbrance from any PRC governing bodies in operating its business through the operating company under the structured contracts.</td>
</tr>
<tr>
<td>Option to Acquire OPCO Ownership</td>
<td>The limitations in exercising the option to acquire ownership in the operating company, including a separate risk factor explaining these limitations and a clarification that ownership transfer may still be subject to substantial costs.</td>
</tr>
<tr>
<td>Material Contracts</td>
<td>The structured contracts should be disclosed as material contracts in the “Statutory and General Information” section and also made available on the applicant’s website.</td>
</tr>
<tr>
<td>Corporate Structure Table</td>
<td>A corporate structure table in the “Summary” section for the purpose of illustrating the structured contracts and facilitating investors’ review and understanding of the arrangements.</td>
</tr>
</tbody>
</table>
CHAPTER 10

CORPORATE GOVERNANCE

A. SOURCES

LISTING RULES

In addition to any corporate governance requirements arising under the laws of an issuer’s place of incorporation, the Listing Rules require the directors to fulfill fiduciary duties and duties of care, skill and diligence to the standard established under Hong Kong Law. The Listing Rules contain their own specific requirements for not only directors but also authorized representatives (through whom the Exchange principally communicates with the issuer), board committees and the company secretary.

CORPORATE GOVERNANCE CODE

The Listing Rules also contain a Corporate Governance Code (Appendix 14 to the Listing Rules) providing further requirements and guidance. The Corporate Governance Code sets forth the principles of good corporate governance for a listed issuer to comply with, followed by code provisions and recommended best practices. The code provisions and recommended best practices are not mandatory rules. Deviations from code provisions are acceptable if the issuer considers there are more suitable ways for it to comply with the principles, but it must state in each interim report and annual report whether it has complied with the code provisions for the relevant accounting period and must explain any deviations (this is known as “comply or explain”).

The subject matter of the Corporate Governance Code includes directors, remuneration and evaluation, accountability and audit, board delegation and communication with shareholders and the company secretary.

Issuers must include in their summary financial reports (if any) and in their annual reports a Corporate Governance Report prepared by the board of directors. There are certain mandatory disclosure requirements (contained in Appendix 14 to the Listing Rules), and any breach of these is regarded as a breach of the Listing Rules.
### B. DIRECTORS

#### DUTIES

The Listing Rules set out the duties that directors owe to their company *(Listing Rule 3.08)*, which are in line with those applicable under Hong Kong Law and may be summarized as follows:

<table>
<thead>
<tr>
<th><strong>Duty of Skill, Care and Diligence</strong></th>
<th><strong>Description</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>• This means the skill, care and diligence that would be exercised by a reasonably diligent person with:</td>
<td></td>
</tr>
<tr>
<td>• the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company; and</td>
<td></td>
</tr>
<tr>
<td>• the general knowledge, skill and experience that the director in fact has.</td>
<td></td>
</tr>
<tr>
<td><strong>Note:</strong> For clarity, this duty is codified in the new CO, expected to come into force in 2014.</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>To Act Honestly, Bona Fide for the Benefit of the Company</strong></th>
<th><strong>Description</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Directors owe a duty to act in the interests of all of the company’s shareholders, present and future;</td>
<td></td>
</tr>
<tr>
<td>• Directors are answerable to the company for the application or misapplication of its assets; and</td>
<td></td>
</tr>
<tr>
<td>• Full and fair disclosure of a director’s interests in contracts with the company must be provided.</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>To Exercise Their Powers for a Proper Purpose</strong></th>
<th><strong>Description</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Directors must not use their powers under the company’s articles for a purpose for which they were not intended.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Not to Allow any Actual or Potential Conflict Between Their Duties as Directors and Their Personal Interests</strong></th>
<th><strong>Description</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Directors must not take personal advantage of the company’s opportunities, allow their personal interests to conflict with those of the company or misapply the company’s assets.</td>
<td></td>
</tr>
<tr>
<td>• Secret profits are not permitted.</td>
<td></td>
</tr>
<tr>
<td><strong>Note:</strong> If the director has a material interest in a transaction, he should abstain from voting, even if he has no beneficial interest in the shares of the other company (Listing Rule 13.44). “Material interest” is not defined in the Listing Rules: materiality should be assessed considering all relevant facts and circumstances.</td>
<td></td>
</tr>
<tr>
<td>But if the director’s interest is the same as all shareholders, such as in approving dividend payments, then he need not abstain from voting.</td>
<td></td>
</tr>
</tbody>
</table>
Though directors may delegate their functions, Listing Rule 3.08 clarifies that this does not absolve them from the required levels of skill, care and diligence. Directors do not satisfy these required levels if they pay attention to the issuer’s affairs only at formal meetings. At a minimum, they must take an active interest in the issuer’s affairs and obtain a general understanding of its business, including following up anything untoward that comes to their attention.

EVALUATION

The Listing Rules require directors to satisfy the Exchange regarding their character, integrity, experience and competence (Listing Rule 3.09). Directors’ conduct at predecessor companies will be taken into account by the Exchange in determining if the directors have met the required standard of competence (Listing Decision LD34-12).

THE CORPORATE GOVERNANCE CODE

The Corporate Governance Code contains principles, code provisions and recommended best practices regarding the role, leadership and composition of the board, as well as directors’ appointment, responsibilities, information and remuneration.

INDEPENDENT NON-EXECUTIVE DIRECTORS

From December 31, 2012, an issuer must appoint INEDs representing at least one-third of the board (Listing Rule 3.10A). Until then, the board must have at least three INEDs. At least one of the INEDs must have appropriate professional qualifications or accounting or related financial management expertise (Listing Rule 3.10).

Appropriate Professional Qualifications

“Appropriate professional qualifications” normally refers to professional accounting qualifications, including those obtained from a recognized body in an overseas jurisdiction, such as the PRC. In determining whether a certain INED has the “appropriate accounting or related financial management expertise,” the Exchange expects the INED to have “experience with internal controls and in preparing or auditing comparable financial statements or experience reviewing or analyzing audited financial statements of public companies” gained through experience as a public accountant or auditor or as a chief financial officer, controller or principal accounting officer of a public company, or through performance of similar functions. It is the responsibility of the board to determine on a case-by-case basis whether the candidate is suitable for the position. In making its decision, the board must evaluate the totality of the individual’s education and experience.

Assessing Independence

In assessing the independence of an INED, the Exchange will take into account the following factors, none of which is necessarily conclusive. Independence is more likely to be questioned if the director:

- holds more than 1% of the total issued share capital of the listed issuer;
- has received an interest in any securities of the listed issuer as a gift, or by means of other financial assistance, from a connected person or the listed issuer itself;
• is a director, partner or principal of a professional adviser that currently provides or has within one year immediately prior to the date of his proposed appointment provided services, or is an employee of such a professional adviser who is or has during the same period been involved in providing services, to (i) the listed issuer, its holding company or any of their respective subsidiaries or connected persons or (ii) any person who was a controlling shareholder of the listed issuer within one year immediately prior to the date of the proposed appointment, or any of their associates;
• has a material interest in any principal business activity of or is involved in any material business dealings with the listed issuer, its holding company or their respective subsidiaries or with any connected persons of the listed issuer;
• is on the board specifically to protect the interests of an entity whose interests are not the same as those of the shareholders as a whole;
• is or was connected with a director, the chief executive officer or a substantial shareholder of the listed issuer within two years immediately prior to the date of his proposed appointment;
• is, or has at any time during the two years immediately prior to the date of his proposed appointment been, an executive or director (other than an INED) of the listed issuer, its holding company or any of their respective subsidiaries, or of any connected persons of the listed issuer; or
• is financially dependent on the listed issuer, its holding company, or any of their respective subsidiaries or connected persons of the listed issuer.

Serving More than Nine Years
If an INED serves more than nine years, his further appointment should be subject to a separate resolution to be approved by shareholders. The papers to shareholders accompanying that resolution should include the reasons why the board believes the INED is still independent and should be reelected.

Nomination of INED for Election
An issuer should include an explanation of its reasons for proposing an INED’s election, and the reasons it considers the INED independent, in a circular nominating the INED for election.

BOARD DIVERSITY
In September 2012, the Exchange published a consultation paper on proposed amendments to the Corporate Governance Code and Corporate Governance Report in relation to board diversity. The proposals include a new code provision stating that the nomination committee (or the board) should have a policy concerning diversity in the boardroom, which should be disclosed in the issuer’s Corporate Governance Report. The consultation paper clarified that diversity of board members can be achieved through consideration of a number of factors, including but not limited to, gender, age, cultural and educational background and professional experience.
C. AUDIT, REMUNERATION AND NOMINATION COMMITTEES

The Listing Rules and the Corporate Governance Code contain requirements for and guidance on the composition and terms of reference of three committees of the listed issuer’s board of directors, as follows:

<table>
<thead>
<tr>
<th>Committee</th>
<th>Composition</th>
<th>Key Terms of Reference (Corporate Governance Code)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit Committee</td>
<td>Non-executive directors only with a majority of INEDs</td>
<td>• Review and monitor the company’s relationship with auditors, including the auditors’ independence;</td>
</tr>
<tr>
<td></td>
<td>Chaired by an INED</td>
<td>• Monitor the integrity of the company’s financial information and review significant reporting judgments in them;</td>
</tr>
<tr>
<td></td>
<td>Minimum of three members, at least one being an INED with appropriate professional qualifications or accounting or financial management expertise</td>
<td>• Oversee the company’s financial reporting and internal control procedures; and</td>
</tr>
<tr>
<td></td>
<td><em>(Listing Rule 3.21)</em></td>
<td>• Consider major investigation findings on internal control matters and management’s response to these findings.</td>
</tr>
<tr>
<td>Remuneration Committee</td>
<td>Majority of INEDs</td>
<td>• Make recommendations to the board on policy and structure for all director and senior management remuneration;</td>
</tr>
<tr>
<td></td>
<td>Chaired by INED</td>
<td>• Review and approve management remuneration proposals;</td>
</tr>
<tr>
<td></td>
<td><em>(Listing Rule 3.25)</em></td>
<td>• Review and approve compensation payable for loss or termination of office, or dismissal or removal for misconduct; and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Ensure that no director (nor any of his associates) is involved in deciding his own remuneration.</td>
</tr>
<tr>
<td></td>
<td></td>
<td><em>Note: The Listing Rules do not restrict issuers from appointing their staff or executive directors to act as members of the Remuneration Committee, as long as a majority of the Remuneration Committee is INEDs and it is chaired by an INED.</em></td>
</tr>
<tr>
<td>Nomination Committee</td>
<td>Majority of INEDs</td>
<td>• Review structure, size and composition of the board at least annually;</td>
</tr>
<tr>
<td></td>
<td>Chaired by chairman of the board or an INED</td>
<td>• Identify and recommend potential board members; and</td>
</tr>
<tr>
<td></td>
<td><em>(Code Provision A.5)</em></td>
<td>• Assess independence of INEDs.</td>
</tr>
</tbody>
</table>
**D. COMPANY SECRETARY**

The company secretary supports the board by ensuring good information flow within the board and that board policy and procedures are followed. The company secretary is responsible for advising the board through the chairman and/or the chief executive on governance matters and should also facilitate induction and professional development of directors.

**EVALUATION**

The company secretary must be an individual who, by virtue of his academic or professional qualifications or relevant experience, is, in the opinion of the Exchange, capable of discharging the functions of the position *(Listing Rule 3.28).*

**ACCEPTABLE QUALIFICATIONS**

The Exchange considers the following academic or professional qualifications to be acceptable:

- member of The Hong Kong Institute of Chartered Secretaries;
- solicitor or barrister (as defined in the Legal Practitioners Ordinance); and
- certified public accountant (as defined in the Professional Accountants Ordinance).

**RELEVANT EXPERIENCE**

In assessing “relevant experience,” the Exchange will consider the individual’s:

- length of employment with the issuer and other issuers and the roles he played;
- familiarity with the Listing Rules and other relevant laws and regulations, including the SFO, the CO and the Takeovers Code;
- relevant training that has or will be completed; and
- professional qualifications in other jurisdictions.
CHAPTER 10  CORPORATE GOVERNANCE

Some examples of “relevant experience” that the Exchange has taken into account include:

- directorship in a Hong Kong-listed subsidiary and active involvement in the subsidiary’s compliance with the Listing Rules and corporate governance for a considerable period of time;
- more than seven years of experience working closely with the retiring company secretary and professional advisers in the company’s secretarial and administrative matters; and
- approximately 70 hours of training courses on Listing Rule compliance, corporate governance and other related laws and regulations.

TRAINING

Company secretaries are required to have 15 hours of professional training in each financial year (Listing Rule 3.29). The compliance dates are staggered according to the date when a person became the company secretary of a listed issuer:

<table>
<thead>
<tr>
<th>Date of Appointment</th>
<th>Latest Compliance Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 January 2000 to 31 December 2004</td>
<td>1 January 2013</td>
</tr>
<tr>
<td>1 January 1995 to 31 December 1999</td>
<td>1 January 2015</td>
</tr>
<tr>
<td>On or before 31 December 1994</td>
<td>1 January 2017</td>
</tr>
</tbody>
</table>

E. MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

A director must ensure that when he is (or is deemed to be) interested in any dealing in securities of his listed issuer, that dealing is conducted in accordance with the Model Code (Appendix 10 to the Listing Rules). Any breach of the Model Code is regarded as a breach of the Listing Rules.

The main point in the Model Code is that directors who are aware of any negotiations or agreements related to intended acquisitions or disposals that are notifiable or connected transactions under Chapter 14 or 14A of the Listing Rules, or any price-sensitive information, must refrain from dealing in the listed issuer’s securities as soon as they become aware of them until proper disclosure of the information in accordance with the Listing Rules.

Directors who are privy to relevant negotiations, agreements or price-sensitive information should warn any other directors who are not so privy that there may be unpublished, price-sensitive information and that they must not deal in the listed issuer’s securities for the same period.

The Model Code’s restrictions on dealings by a director apply equally to any dealings by the director’s spouse or by or on behalf of any minor child (natural or adopted), and any other dealings in which he is interested for the purposes of Part XV of the SFO. The director must therefore seek to avoid any such dealings at a time when he himself is not free to deal.

When a director places securities of the listed issuer under professional management, discretionary or otherwise, the managers must be made subject to the same restrictions and procedures as the director himself with respect to any proposed dealings in the listed issuer’s securities.
The requirements to be observed by a director of a listed issuer under the Model Code include the following:

**ABSOLUTE PROHIBITIONS**

- Dealing in the securities of the listed issuer is not permitted at any time when he is in possession of unpublished price-sensitive information.
- Dealing in the securities of any listed issuer is not permitted when he is in possession of unpublished price-sensitive information in relation to those securities through his position as a director of another listed issuer.

**BLACKOUT PERIODS FOR DIRECTORS**

Dealing in securities of the listed issuer is not permitted on the day on which its audited financial results are published and is also not permitted:

- during the period of 60 days immediately 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 immediately preceding the publication date of the quarterly results (if any) and 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.

*Note: An issuer must notify the Exchange in advance of the start of each blackout period. It may choose to do so at the same time that it notifies the Exchange of the board meeting under Listing Rule 13.43.*

**REQUIRED NOTIFICATIONS**

- Dealing in any securities of the listed issuer is not permitted without first notifying the chairman or a designated director (other than himself) in writing and receiving a dated, written acknowledgment.
- A response to a request for such a clearance to deal must be given within five business days of the request being made, and the clearance to deal must be valid for not longer than five business days after the clearance is received.

**F. ENVIRONMENTAL, SOCIAL AND GOVERNANCE (“ESG”) REPORTING**

ESG reporting is a recommended practice for all issuers in financial years ending after December 31, 2012, and is guided by an Environmental, Social and Governance Reporting Guide *(Appendix 27 to the Listing Rules)*, which covers four subject areas: Workplace Quality, Environmental Protection, Operating Practices and Community Involvement. However, the Exchange does not expect issuers to report on all recommended disclosures from the start. Subject to further consultation, the Exchange plans to raise the level of obligation of some recommended disclosures to “comply or explain” by 2015.

An issuer may disclose the ESG information in its annual report regarding the relevant period, or in a separate report published in print or on its website.
INTERNATIONAL OFFERINGS

A. REGULATION S AND RULE 144A SAFE HARBORS

Listings on the Main Board of the Exchange above a certain offer size typically will include a sale of securities to institutional investors in major international financial markets, such as Singapore, London or New York. Such international offerings are required to comply with the legal requirements of the relevant jurisdictions in which they are offered and sold, including the securities laws of the United States. All securities to be offered or sold in the United States must either be registered under the U.S. Securities Act or rely on an exemption from registration. Regulation S and Rule 144A under the U.S. Securities Act are two such commonly used exemptions.

Both Regulation S and Rule 144A are nonexclusive safe harbors. Accordingly, an offering targeted at investors outside the United States in reliance on Regulation S often is conducted side by side with an offering targeted at qualified institutional buyers in the United States in reliance on Rule 144A.

**REGULATION S OFFERINGS**

Regulation S provides safe harbor guidelines for determining when an offering of securities will be deemed to have occurred outside the United States and is therefore exempt from registration under the U.S. Securities Act. The availability of the Regulation S safe harbor is contingent on two general conditions:

- the offer or sale must be made in an offshore transaction; and
- no “directed selling efforts” may be made by the issuer, a distributor, any of their respective affiliates or any person acting on their behalf.

**Offshore Transactions**

Generally speaking, offers or sales of securities are considered offshore transactions when two conditions are satisfied: (i) the offer must be made to a person outside the United States and (ii) at the time the buy order is originated, the buyer must be outside the United States or the seller and any person acting on the seller’s behalf must reasonably believe that the buyer is outside the United States.

**Directed Selling Efforts**

“Directed selling efforts” are any activities undertaken for the purpose of, or that could be reasonably expected to result in, conditioning the U.S. market for the securities being offered. They include mailing printed material to U.S. investors, conducting promotional seminars in the United States or placing advertising in publications with a general circulation in the United States. In general, however, Regulation S is not intended to interfere with any lawful and customary activities that are conducted outside the United States, such as offshore press activities conducted in accordance with Rule 135e of the U.S. Securities Act. See part A of Chapter 7, “Marketing, Sales and Stabilization,” for a further discussion on publicity concerns in the context of a Regulation S offering.
Other Requirements

In addition to the offshore transaction requirement and the prohibition on “directed selling efforts,” other requirements may be applicable depending on the “category” of securities being offered under Regulation S, which are calibrated to the level of risk that securities in a particular type of transaction will flow back into the United States. Rule 903 of Regulation S distinguishes among three categories of transactions based on: (i) the type of securities being offered and sold; (ii) whether the issuer is domestic or foreign; (iii) whether the issuer is a reporting issuer under the U.S. Exchange Act; and (iv) whether there is “substantial U.S. market interest” (or “SUSMI”) in the securities.

- “Category 1” transactions are those in which the securities are least likely to flow back into the United States. Therefore, the only restrictions are that the transaction must be an “offshore transaction” and there must be no “directed selling efforts” in the United States.

- “Category 2” and “Category 3” transactions are subject to an increasing number of offering and transactional restrictions for the duration of the applicable “distribution compliance period.” “Distribution compliance period” is defined in Regulation S generally as the period following the offering when any offer or sale of Category 2 or Category 3 securities must be made in compliance with the requirements of Regulation S in order to prevent the flowback of the offered securities into the United States. The period ranges from 40 days to six months for reporting issuers or one year for equity securities of non-reporting issuers.

Disclosure

Because Regulation S offerings are exempt from the U.S. registration requirements, such offerings need not comply with the U.S. SEC’s detailed prospectus disclosure requirements. In addition, the risk of triggering liabilities under Rule 10b-5 is low if the offering is done in strict compliance with the requirements of the Regulation S safe harbor and the securities sold are unlikely to flow back into the United States. As a result, the offering document for a listing with a Regulation S offering tranche, but not a Rule 144A tranche, will have greater flexibility in the style and substance of disclosure. Nevertheless, the underwriters may still choose to adopt a disclosure approach that is substantially similar to that of a Rule 144A offering for marketing and/or reputational reasons.

RULE 144A PLACINGS

Rule 144A is a safe harbor exemption from the registration requirements of the U.S. Securities Act for certain offers and sales of qualifying securities by certain persons other than the issuer of the securities. The exemption applies to resales of securities to qualified institutional buyers, who are commonly referred to as QIBs. QIBs must be institutions and cannot be individuals—no matter how wealthy or sophisticated. The securities eligible for resale under Rule 144A are securities of U.S. and foreign issuers that are not listed on a U.S. securities exchange or quoted on a U.S. automated inter-dealer quotation system.
QIBs

Rule 144A identifies certain institutions that are considered to be QIBs, including insurance companies, registered investment companies, licensed small business investment companies, certain pension plans, registered investment advisers and certain banks, savings and loan associations and trust funds. Furthermore, QIBs may be domestic or foreign entities. Generally, QIBs must meet specific financial thresholds. Any entity that owns and invests on a discretionary basis at least US$100 million in securities of nonaffiliates, even if the entity was formed to acquire restricted securities, is considered a QIB. Banks and thrifts must also have an audited net worth of at least US$25 million. Registered securities dealers need only own and invest on a discretionary basis US$10 million in securities of nonaffiliates, and they may also execute no-risk principal transactions for QIBs without regard to the amount owned and invested. Additionally, any entity of which all of the equity owners are QIBs is deemed to be a QIB itself.

Conditions for Relying on Rule 144A

There are four conditions to fulfill when relying on Rule 144A:

- the reoffer or resale must be made only to a QIB or to an offeree or purchaser that the reseller (or any person acting on its behalf) reasonably believes is a QIB;
- the securities reoffered or resold: (a) when issued were not of the same class as securities listed on a U.S. national securities exchange or quoted on a U.S.-automated inter-dealer quotation system and (b) are not securities of an open-end investment company, unit investment trust or face-amount certificate company that is, or is required to be, registered under the Investment Company Act;
- the reseller (or any person acting on its behalf) must take reasonable steps to ensure that the buyer is aware that the reseller may rely on Rule 144A in connection with the resale; and
- when the issuer of the securities being reoffered or resold is not: (i) a reporting company under the U.S. Exchange Act; (ii) a foreign issuer exempt from reporting pursuant to Rule 12g3-2(b) of the U.S. Exchange Act or (iii) a foreign government, the holder of the securities and a prospective buyer of the securities designated by the holder must have the right to obtain from the issuer and must receive, upon request, certain reasonably current information about the issuer.

Disclosure

Because Rule 144A offerings are exempt from the U.S. registration requirements, such offerings need not comply with the U.S. SEC’s detailed prospectus disclosure requirements. However, as the securities are sold within the United States, potential liabilities under Rule 10b-5 of the U.S. Exchange Act still apply. As a result, issuers and underwriters typically engage in U.S.-style due diligence to establish a defense to potential liabilities under Rule 10b-5, and the level of disclosure in the offering document used in a Rule 144A offering is generally substantially similar to that used for a U.S. SEC-registered offering.

In practice, the prospectus for the listing in Hong Kong can be used in the United States, so long as it is in English and meets U.S. standards with respect to material disclosure, i.e., the offering document does not contain an untrue statement of a material fact or omit to state a material fact necessary in order to make the statements therein not misleading in light of the circumstances under which they were made. The offering document used in a Regulation S and/or Rule 144A offering is often adapted by adding a
supplement to the prospectus used for the listing. As noted above, under Rule 144A, a seller and anyone acting on its behalf must take “reasonable steps” to ensure that the purchaser is aware that the seller may rely on the Rule 144A exemption. This requirement is typically satisfied by placing a legend on the security and including appropriate statements in the supplement to the prospectus. The supplement also contains other legends and statements that are appropriate for U.S. private placements, such as restrictions on resale, descriptions of the U.S. tax consequences of purchasing, holding and disposing of the securities and of the differences between GAAP in the United States and in the issuer’s jurisdiction. This supplement is known in practice as an “international wrap,” which will usually be placed in front of the Hong Kong prospectus.

Publicity Concerns

A Rule 144A exemption is a type of “private offering” exemption. Accordingly, there can be no “general solicitation” or “general advertising” of the offering in the United States. A press announcement in or directed into the United States regarding a private offering, made prior to completion of the offering, may constitute a general solicitation or general advertisement of the offer and could jeopardize the availability of Rule 144A. The prohibitions on general solicitation and general advertising also include the distribution of research reports by initial purchasers participating in the offering, subject to limited exceptions. See part A of Chapter 7, “Marketing, Sales and Stabilization,” for a further discussion on publicity concerns in the context of a Rule 144A offering.

B. H- AND A-SHARE DUAL LISTINGS

TYPES OF DUAL LISTINGS

There are three major types of dual listings undertaken by PRC companies on the Exchange and a domestic Chinese stock exchange: (i) simultaneous A- and H-share listings (i.e., listing A-shares and H-shares at the same time—the most notable example is Industrial and Commercial Bank of China’s landmark IPO in October 2006 in both Hong Kong and Shanghai, the largest IPO in history at the time); (ii) listing A-shares first and then H-shares; or (iii) listing H-shares first and then A-shares (most dual-listed PRC companies in Hong Kong fall into this category). H- and A-share dual listings have become popular for a number of reasons—they allow issuers a wider access to capital, a greater shareholder base and increased liquidity. Additionally, H- and A-share dual listings have been actively supported and encouraged by the PRC authorities, as these listings are believed to promote the reform and development of China’s domestic capital markets and to deepen the economic relationship between Hong Kong and the PRC. The PRC has also encouraged dual listings to raise the international profile and corporate governance standards of domestic PRC companies, especially state-owned enterprises.

GENERAL ISSUES AND DIFFERENCES

As the scope of this Guide does not cover the mechanics of listing A-shares on a domestic Chinese stock exchange, this section will only point out a few general issues and, more specifically, differences between an A-share offering and an H-share listing in Hong Kong.
Lack of Fungibility

It is important to note that A-shares listed on a domestic Chinese stock exchange (such as the Shanghai Stock Exchange or the Shenzhen Stock Exchange) are not fungible with H-shares listed in Hong Kong. Due to PRC regulations, only PRC residents and qualified financial institutional investors ("QFIs") may acquire A-shares.

Disclosure and Timing Issues

There are important differences between A- and H-share offerings in terms of disclosure and timing, as the disclosure requirements in the PRC and Hong Kong may differ. Specific differing areas include disclosure of price-sensitive information, periodic financial reporting, disclosure of notifiable transactions and disclosure of connected transactions. For example, with regards to notifiable transactions, Hong Kong and the PRC have different requirements for shareholder approval—the Hong Kong Listing Rules allow shareholders to express their approval through general meeting resolutions and also, in some cases, written circulation, whereas written circulation is prohibited for A-share companies.

Furthermore, due to differences in terms of timing, issuers must take care to comply with each jurisdiction’s rules on pre-deal publicity. For example, A-share offerings generally involve posting the A-share prospectus on the CSRC’s website before the CSRC hearing, with a subsequent publication of a final prospectus on the same website after the CSRC has granted approval. However, especially for simultaneous A- and H-share offers, this A-share publication schedule would run counter to publicity regulations and practices in Hong Kong, where the H-share prospectus is not published until registration is complete. Potential H-share investors would have information about the issuer from the CSRC website before the H-share prospectus was disseminated by the Exchange. To reconcile these timing differences, the Exchange allows, and expects, the publication of an information pack (or WPIP) on the Exchange’s website after the Listing Committee hearing. The WPIP is essentially a late-stage draft of the Hong Kong prospectus, which does not include information about the offering. See part A of Chapter 7, “Marketing, Sales and Stabilization,” for a further discussion on the publication of a WPIP.

Disclosure of Additional Information

Where a PRC company is issuing securities other than H-shares simultaneously with its H-share issue in Hong Kong pursuant to a share issue plan that has been approved in a meeting of its shareholders (or a proposed share issue plan), Listing Rule 19A.42 requires the disclosure of additional information in the H-share prospectus. Such additional information includes:

- a description of the effect of the listing on the PRC issuer’s future plans, prospects and financial condition if the issue of shares is not completed in accordance with the share issue plan or share issue plan proposal;
- a breakdown of the PRC issuer’s shares issued or proposed to be issued; and
- a statement confirming whether the share issue plan has been approved by the PRC State Council Securities Policy Committee.
Once a company is listed on the Exchange, it will need to meet the continuing obligations set out under the Listing Rules, in addition to the statutory obligations under the SFO and the laws of its place of incorporation. These continuing obligations are primarily designed to ensure the maintenance of a fair and orderly market in securities and that all users of the market have simultaneous access to the same information. Failure by an issuer to comply with any applicable continuing obligation may result in the Exchange taking disciplinary action, in addition to its power to suspend or cancel a listing.

A. STATUTORY DISCLOSURE REGIME

From January 1, 2013, listed issuers have a statutory obligation under new Part XIVA of the SFO to disclose price-sensitive information (defined as “inside information”) to the public, as soon as reasonably practicable after the inside information has come to their “knowledge.”

In conjunction with the statutory disclosure regime, the SFC has also published Guidelines on Disclosure of Inside Information (the “Guidelines”) to illustrate how the statutory disclosure requirements operate in practice and relevant compliance issues, though the Guidelines do not have the force of law. Please refer to the illustrative flowchart below.

CONCEPT OF “INSIDE INFORMATION”

The key elements comprising the concept of inside information are:

- specific information about a particular listed corporation, a shareholder or officer of the corporation or the listed securities of the corporation or their derivatives;
- the information is not generally known to those who are accustomed or would be likely to deal in the corporation’s securities; and
- if known, the information would be likely to have a material effect on the price of the listed securities.

WHAT CONSTITUTES “KNOWLEDGE”?

A listed corporation will be regarded as having knowledge of inside information if:

- information has, or ought reasonably to have, come to the knowledge of an officer of the corporation in the course of performing functions as its officer; and
- a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.
“OFFICER”

An “officer” is “a director, manager or secretary of, or any other person involved in the management of, the corporation.” The intention of the proposed legislation is to include directors and high-level individuals responsible for managing listed companies.

“OUGHT REASONABLY TO HAVE COME TO THE KNOWLEDGE”

The concept of “ought reasonably to have come to the knowledge” is an element that triggers the disclosure obligation for a listed company and does not by itself result in liability on “officers.” The intention is to prevent listed companies evading the disclosure obligation by arguing that inside information has been channeled to its officers, but has not been read, or deliberately keeping inside information from being accessed by the officers.

Based on section 307G, an “officer” would be held liable only if the breach of a disclosure requirement is the result of the officer’s intentional, reckless or negligent conduct, or his failure to take all reasonable measures from time to time to ensure that proper safeguards existed to prevent a breach of a disclosure requirement.

The SFC sets out clearly in the Guidelines that assuming a listed corporation has implemented reasonable measures to prevent a breach, an officer (including a NED) who acts in good faith and in accordance with all his fiduciary duties without actual knowledge of the information or involvement in the corporation’s breach is unlikely to be personally liable on grounds of intentional, reckless or negligent conduct.

For a list of examples of such reasonable measures and additional guidance on officers’ liability and obligations of NEDs, please refer to the Guidelines.

“REASONABLE PERSON” TEST

If an “officer” acted reasonably in deciding that information is not inside information, and therefore did not disclose the information, it will not cause the officer or the company to be treated as having knowledge of inside information.

TIMING OF DISCLOSURE

A listed corporation should disclose inside information as soon as reasonably practicable, unless the information falls within any of the safe harbors provided in the SFO. The Guidelines clarify that “as soon as reasonably practicable” means that the corporation should immediately take all steps that are necessary in the circumstances to disclose the information to the public, such as ascertaining sufficient details, internally assessing the matter and its likely impact, seeking professional advice and verifying the facts.

CONFIDENTIALITY PRIOR TO DISCLOSURE

A listed corporation must ensure that inside information is kept strictly confidential before the information is fully disclosed to the public. If confidentiality cannot be maintained or may have been breached, the corporation should immediately disclose the information to the public.
The Guidelines state that a listed corporation could consider issuing a “holding announcement” if it needs time to clarify the details of, and the impact arising from, an event or a set of circumstances. However, a listed corporation should consider applying for a suspension of trading where confidentiality has not been maintained, and it is not able to make a full or holding announcement.

SAFE HARBORS
There are five safe harbors within which listed companies can withhold or delay disclosure of inside information. Please refer to the flowchart below for further details.

DEALING WITH SPECULATION, MARKET RUMORS AND ANALYSTS’ REPORTS
As clarified in the Guidelines, no analyst, investor or journalist should receive a selective release of inside information.

Generally, companies are not obliged to respond to press speculation or market rumors. However, where press speculation or market rumors are largely accurate and the information underlying the speculation or rumors constitutes inside information, the company should disclose the information as soon as reasonably practicable.

In relation to incorrect analysts’ reports, the company is not obliged to make corrections or provide clarification under the SFO, unless it knows inside information which has not been disclosed but requires disclosure. The SFC has commented that, for good practice, it may be appropriate for a corporation to clarify historical information and correct any factual errors in analysts’ assumptions which are significant to the extent that they may mislead the market, provided any clarification is confined to drawing the analyst’s attention to information that has already been made available to the market. However, on the other hand, companies may wish to avoid routinely correcting errors published by others, as this would then be widely interpreted as implying confirmation of any reports or data which they do not correct.

Note that the obligations to disclose inside information under Part XIVA of the SFO are distinct from the disclosure requirements under the Listing Rules and the Takeovers Code. For general guidance on handling particular situations and issues pursuant to the Listing Rules, see the Exchange’s letter “Recent economic developments and the disclosure obligations of listed issuers,” dated October 31, 2008, which can be found at the Exchange’s website at: http://www.hkex.com.hk/eng/rulesreg/listrules/listletter/documents/20081031.pdf.

With a view to ensuring compliance with their continuing obligations, it is important for issuers to establish procedures to monitor actively their share price and any news, comments or reports relating to them circulated in the market. Directors should ensure that they have a proper understanding of the issuer’s business, financial position and prospects and that there is an effective system for them to monitor developments continuously so they can promptly and accurately respond to any enquiries from regulators concerning the issuer’s affairs and, where necessary, publish announcements to correct or prevent a false market.
ENFORCEMENT AND SANCTIONS

Breaches of the statutory disclosure requirement are dealt with by the MMT, which is able to impose a number of civil sanctions including a regulatory fine up to HK$8 million on the listed company, each of the directors and/or its chief executive, respectively. Those who suffer pecuniary loss as a result of others breaching the disclosure requirements will also be able to rely on the findings of the MMT to launch civil claims for compensation.

In addition, the SFC is now able to institute proceedings directly before the MMT (previously only instituted by the Financial Secretary) to enforce the statutory disclosure requirement, as well as to deal with various market misconduct under Part XIII of the SFO.
CHAPTER 12 ➔ POST-LISTING CONTINUING OBLIGATIONS

WHEN IS THE INFORMATION “INSIDE INFORMATION”¹ REQUIRING DISCLOSURE?

Specific information²
- Capable of being identified, defined and unequivocally expressed
- Applies to negotiations that have a substantial commercial reality with a realistic view to achieving an identifiable goal

Not generally known to market³
Examples of generally known information:
- General external developments, such as changes in commodity prices or outbreak of pandemic diseases
- Disclosure of interests under Part XV of the SFO

Knowledge of a listed corporation:
- Officer⁵ has actual knowledge or “ought reasonably” to know; and
- Reasonable person test⁶

Within safe harbors?
- Disclosure prohibited under HK law/court order⁷
- Incomplete proposal or negotiation⁸,⁹
- Trade secret¹⁰

No disclosure obligation under Part XIVA of the SFO
Inside information must be disclosed as soon as reasonably practicable
**Likely material effect on price**

Standard by which materiality is to be judged: the information would influence persons who are accustomed or would be likely to deal in the listed shares of the corporation in deciding whether or not to buy/sell.

- **NO**
  - No disclosure obligation under Part XIVA of the SFO

- **NO**
  - No disclosure obligation under Part XIVA of the SFO

**or**

- **Provision of liquidity support for the listed group**

- **Disclosure is waived by the SFC**

  - **YES**
    - Reasonable precautions for preserving confidentiality of information; and
    - Confidentiality of information is preserved

  - **NO**
    - Disclose as soon as reasonably practicable once corporation becomes aware of leakage

  - **NO**
    - No disclosure obligation under Part XIVA of the SFO

  - **YES**
    - No disclosure obligation under Part XIVA of the SFO
Notes:

1. Note the distinct disclosure requirements under the Listing Rules and Takeovers Code.

2. Specific information that is about the corporation, a shareholder/officer or the listed shares or their derivatives. The information need not be precise—it may still be “specific” even though it has a vague quality, and may be broad, allowing room for further particulars. For example, information about a corporation’s financial crisis or contemplation of share placing would be regarded as specific, even if details are unknown.

3. The market is defined as those persons who are accustomed or likely to deal in the listed securities of the corporation. Where the information known to the market (i) is incomplete; (ii) contains material omissions; or (iii) is of doubtful bona fides, such information cannot be regarded as generally known, and full disclosure is necessary.

4. The following factors should be taken into consideration in determining whether a material effect on price is likely to occur:

   (a) the anticipated magnitude of the event or circumstances in the context of the corporation’s overall activities;

   (b) the relevance of the information as regards the main factors that determine the price;

   (c) the reliability of the source; and

   (d) market variables that affect the price (such as prices, returns, volatilities, liquidity, price relationships among securities, volume, supply, demand, etc.).

In relation to volatility, the Guidelines state that while a certain percentage movement for a small company’s stock might be seen as immaterial, the same (or even a lower) percentage movement in a large company’s stock might be considered material by virtue of the stock’s nature and size.

5. Defined as “a director, manager or secretary of, or any other person involved in the management of, the corporation.”

6. Whether a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.

7. This safe harbor does not apply to information the disclosure of which is prevented by a contractual duty.

8. Examples include (i) when a contract is being negotiated but has not been finalized; (ii) when a corporation decides to sell a major holding in another corporation; (iii) when a corporation is negotiating a share placing with a financial institution; or (iv) when a corporation is negotiating the provision of financing with a creditor.

9. This safe harbor does not allow withholding disclosure of any material change in financial position or performance to the extent that this is inside information.

10. Commercial terms and conditions of a contract or financial information of a corporation cannot be regarded as trade secrets, as these are not proprietary information or rights owned by the corporation.

11. Where the liquidity support is from the Exchange Fund of the Government of Hong Kong or from an institution which performs the functions of a central bank, including such an institution located outside Hong Kong.

12. A listed corporation may apply for a waiver from the SFC if there are circumstances where disclosure of the information is prohibited under or would constitute a contravention of a restriction imposed by (a) foreign legislation; (b) an order of a court exercising jurisdiction under foreign law; (c) a foreign law enforcement agency; or (d) a governmental authority in the exercise of a power conferred by foreign legislation, especially where the corporation or certain of its subsidiaries are incorporated or operate outside Hong Kong.
B. ANNOUNCEMENT, CIRCULAR AND DISCLOSURE OBLIGATIONS

The Listing Rules also impose certain continuing publicity requirements, identifying specific circumstances in which an issuer is obliged to disclose information to the holders of its securities and the public. This section highlights the key continuing disclosure obligations of listed issuers under the Listing Rules.

POST-VETTING REGIME

In 2009, the Exchange introduced a post-vetting regime, in a shift of its regulatory focus from pre-vetting towards post-vetting, monitoring and enforcement. Under Listing Rule 13.52B(2), issuers are encouraged to consult the Exchange on rule compliance issues.

The following documents continue to require pre-vetting by the Exchange prior to publication (*Listing Rule 13.52*):

- listing document (including prospectus);
- circular relating to:
  1. cancellation or withdrawal of listing;
  2. notifiable transaction;
  3. connected transaction (including continuing-connected transaction);
  4. any proposal to explore for natural resources as an extension to or change from the issuer’s existing activities under Listing Rule 18.07;
  5. any warrant proposal under paragraph 4(c) of Practice Note 4 of the Listing Rules;
- circular or offer document relating to a takeover, merger, or offer; and
- announcement for:
  1. very substantial disposal, very substantial acquisition, or reverse takeover;
  2. any transaction or arrangement which would result in a fundamental change in the principal business activities of the listed issuer within 12 months after listing under Listing Rules 14.89 to 14.91; or
  3. any matter relating to a cash company under Listing Rules 14.82 and 14.83.

In addition, the Exchange has the right to request to review any announcements, circulars and other relevant documents before publication. In such cases, the issuer should submit a draft to the Exchange for review and until the Exchange has cleared the document, it may not be issued to the public (*Listing Rule 13.52A*).
**ANNOUNCEMENT**

Once a decision has been made by the shareholders of the issuer at a general meeting on any substantive matter, an announcement must be issued notifying the Exchange and its shareholders. A listed issuer should also issue an announcement in the following circumstances:

| General Corporate Change | • Change of company name  
|                          | • Change in memorandum and articles of association *(Listing Rule 13.51(1))* |
| Share Capital            | • Issue of securities for cash *(Listing Rule 13.28)*  
|                          | • Issue of securities for cash at a 20% (or more) discounted issue price *(Listing Rule 13.29)*  
|                          | • Adoption of share option scheme *(Listing Rule 17.02(1)(a))*  
|                          | • Rights issue or open offer *(Listing Rule 13.09)*  
|                          | • Changes in rights attaching to any class of listed securities and changes in rights attaching to any shares into which any listed debt securities are convertible or exchangeable *(Listing Rule 13.51(3))* |
| Directors, Supervisors and Chief Executives | • Appointment, resignation, re-designation, retirement, or removal of any director, supervisor or chief executive *(Listing Rule 13.51(2))*  
|                          | • Changes in information of a director or supervisor (includes any public or regulatory sanctions, bankruptcy orders, or judgments made against him) during term of office *(Listing Rule 13.51B(2))*  
|                          | • If notice from a shareholder to propose a person for election as director at a general meeting is received by the issuer after publication of the notice of meeting *(Listing Rule 13.70)*  
|                          | • Number of independent non-executive directors falls below the minimum number required under Listing Rule 3.10(1) or their qualifications fail to meet the requirement under Listing Rule 3.10(2) *(Listing Rules 3.11 and 3.14)*  
|                          | • Failing to set up an audit or remuneration committee or appoint appropriate members to such committees *(Listing Rules 3.23, 3.27)* |
| Auditors, Compliance Adviser and Others | • Changes in auditor or financial year end *(Listing Rule 13.51(4))*  
|                          | • Resignation or termination of engagement of compliance adviser *(Listing Rule 3A.29)*  
|                          | • Changes in company secretary, share registrar (including any change in overseas branch share registrar), registered address or agent for the service of process in Hong Kong *(Listing Rule 13.51(5))* |
### Specific Transactions

- Advance to an entity exceeding certain asset ratio (Listing Rules 13.13 and 13.14)
- Financial assistance and guarantee to affiliated company of the issuer (Listing Rule 13.16)
- Controlling shareholder pledging its shares in support of the issuer (Listing Rule 13.17)
- Entering into loan agreements which impose performance obligation on a controlling shareholder (Listing Rule 13.18)
- Issuer’s breach of loan agreement (Listing Rule 13.19)
- Notifiable transactions
- Connected transactions not exempt from the announcement requirement
- Other transactions involving price-sensitive information which would fall to be disclosed under the general disclosure obligation (Listing Rule 13.09)

### Financial Information

- Preliminary announcement of results for each full or first half of the financial year (Listing Rule 13.49)
- Preliminary announcement of profits/losses for any year, half-year, or other period (Listing Rule 13.45(3))
- Seven business days in advance of any board meeting at which declaration, recommendation or payment of dividend is expected to be decided, and upon any such approval after the board meeting (Listing Rules 13.43, 13.45(2))
- Seven business days in advance of any board meeting at which an announcement of profits/losses for any year, half-year, or other period is to be approved for publication, and upon any such approval after the board meeting (Listing Rules 13.43, 13.45(3))

### Shareholders’ Meeting

- Notice of annual general meeting (Listing Rule 13.37)
- Poll results of any general meeting (Listing Rule 13.39(5))

### Closure of Books and Record Date

- At least 10 business days before closure of transfer books or register of members (in the case of a rights issue, at least six business days) (Listing Rule 13.66(1))

### Overseas Regulatory Announcements (Listing Rule 13.09)

A listed issuer must also release all overseas regulatory information in Hong Kong at the same time the information is required to be disclosed on other stock exchanges. This includes any information disclosable under Chapter 13 of the Listing Rules, which is released by its subsidiary to another stock exchange on which that subsidiary is listed.
CIRCULAR

When an issuer needs to seek approval from its shareholders on certain matters, a circular must be issued containing a recommendation from the board of directors and a notice of the general meeting. Where a matter does not require shareholders’ approval, issue of a circular is generally not required.

A listed issuer should issue a circular in the following circumstances:

| General Corporate Change | • Proposed change in memorandum and articles of association (Listing Rule 13.51(1))
|                         | • Proposed change of company name
| Share Capital           | • Proposed issue of shares, convertible securities, options, warrants or similar rights to subscribe for any shares (Listing Rule 13.36)
|                         | • Proposed increase in authorized share capital (Listing Rule 13.57)
|                         | • Share repurchase by the issuer (Listing Rule 10.06)
|                         | • Rights issue and open offer (Listing Rules 7.22 and 7.27)
|                         | • Adoption of share option scheme (Listing Rule 17.02(1)(a))
| Directors and Others    | • Approval of directors’ service contracts (Listing Rule 13.68)
|                         | • Appointment of auditor or removal prior to expiration of his term of office (Listing Rule 13.88)
| Specific Transactions   | • Major transaction, very substantial disposal, very substantial acquisition, and reverse takeover
|                         | • Connected transaction not exempt from the independent shareholders’ approval requirements
| Shareholders’ Meeting   | • Annual general meeting
| Other                   | • Withdrawal of listing (Listing Rules 6.11 and 6.12)

ANNUAL REPORT AND INTERIM REPORT

In addition to publishing an announcement of its financial results for the full financial year and first half of the financial year, a listed issuer should issue an annual report not later than three months, and an interim report not later than two months, after the end of the relevant period. It is a recommended best practice under the Corporate Governance Code for the issuer to publish quarterly financial results.

Chapter 14 and Appendix 16 of the Listing Rules set out the minimum financial information which a listed issuer should include in its preliminary results announcements, interim reports, annual reports and other listing documents. In addition to financial performance of the issuer, an annual report should include the following information:

• details of directors’ emoluments;
• change in any information required to be disclosed under paragraphs (a) to (e) of Listing Rule 13.51(2) during the course of the term of office of a director or supervisor (Listing Rule 13.51B(1));
• certain types of connected transactions (Listing Rules 14A.28 and 14A.45);
• certain types of continuing-connected transactions \((\text{Listing Rules 14A.29 and 14A.37})\);
• a corporate governance report; and
• whether the issuer has complied with the code provisions under the Corporate Governance Code and an explanation where it deviates from any of them. For further details on the Code, please refer to Chapter 10 of this Guide.

RESPONSE TO EXCHANGE’S INQUIRIES

Where there are unusual movements in the price or trading volume of securities of the listed issuer, the Exchange may raise inquiries with the issuer. The issuer should respond to these inquiries promptly and, where appropriate, issue an announcement containing a statement in the prescribed form to the effect that it is not aware of any matter or development relevant to the unusual price movement or trading volume \((\text{Listing Rule 13.10})\).

OTHER DISCLOSURES

As a continuing obligation of a listed issuer, the following documents should be posted in English and Chinese on the websites indicated below:

<table>
<thead>
<tr>
<th>Website of Exchange</th>
<th>Website of Exchange and Issuer</th>
<th>Website of Issuer</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Monthly return in relation to movements in the issuer’s securities ((\text{Listing Rule 13.25B}))</td>
<td>• Constitutional documents ((\text{Listing Rule 13.90}))</td>
<td>• Procedures for shareholders to propose a person for election as director ((\text{Listing Rule 13.51D}))</td>
</tr>
<tr>
<td>• Next day disclosure return in relation to certain corporate events ((\text{Listing Rule 13.25A}))</td>
<td>• Updated list of directors identifying their role and function ((\text{Code Provision A.3.2}))</td>
<td>• Communication policy with shareholders ((\text{Code Provision E.1.4}))</td>
</tr>
<tr>
<td>• Terms of reference of the nomination, remuneration and audit committees ((\text{Code Provisions A.5.3, B.1.3, C.3.4}))</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

C. BOARD AND SHAREHOLDERS MEETINGS

BOARD MEETING

A listed issuer should hold at least four board meetings each year \((\text{Code Provision A.1.1})\). Prior to and after a board meeting, an announcement must be issued in respect of any decision on certain prescribed matters, such as the payment of a dividend (see also the subsection above on issuance of announcements). A listed issuer should also observe the provisions of its articles of association or bylaws with respect to the proceedings of a board meeting.
CHAPTER 12  ➤ POST-LISTING CONTINUING OBLIGATIONS

Director’s Interest in Contracts
Subject to exceptions, a director of a listed issuer may not vote on any board resolution approving any contract or other proposal in which he or any of his associates has a material interest, and he may not be counted in the quorum present at the board meeting (Listing Rule 13.44). Where a director is interested in a contract, he should disclose his interest at the board meeting.

SHAREHOLDERS MEETING
A listed issuer should hold annual general meetings and extraordinary or special general meetings where appropriate pursuant to its articles of association. General meetings are important in allowing shareholders, directors and members of senior management to examine and make decisions on important affairs of the company. Under the Corporate Governance Code, the chairman of the board, the chairmen of the audit, remuneration, nomination and any other committees (as appropriate) should attend the annual general meeting (Code Provision E.1.2). The external auditor of the issuer should also attend the annual general meeting to answer questions about the audit, accounting policies and content of the auditor’s report.

Any vote of shareholders at general meetings must be taken by poll, except where the chairman decides to allow a resolution in relation to administrative matters (Listing Rule 13.39(4)). Where parties are required to abstain from voting in favor of a resolution at a general meeting, they may vote against the resolution at the general meeting provided that their intention has been stated in the relevant circular or listing document to the shareholders (Listing Rule 13.40).

Notice of Meeting and Poll Results
Notice of an annual general meeting must be published on the website of the Exchange (Listing Rule 13.37) and sent to all shareholders at least 20 clear business days before the meeting. For all other general meetings, the required period is at least 10 clear business days before such meeting (Code Provision E.1.3).

Notice of any general meeting must be sent with a proxy form offering two-way voting on all resolutions and must also be published on the website of the Exchange (Listing Rule 13.38).

As soon as poll results are available, they must be published at least 30 minutes before the start of the morning trading session (including any pre-opening session) on the business day after the meeting (Listing Rule 13.39(5)).
D. DISCLOSURE OF SHARE INTERESTS

Part XV of the SFO requires directors and others to disclose certain interests in listed securities, and changes therein, by notice to the Exchange and the listed issuer.

“The overriding objective of the disclosure regime is to provide investors in listed corporations with more complete and better quality information on a timely basis to enable them to make informed investment decisions.”

SFC’s Outline of Part XV of the SFO – Disclosure of Interests

DISCLOSURE DUTIES OF SUBSTANTIAL SHAREHOLDERS (Divisions 2-6 of Part XV of the SFO)

Substantial shareholders, being for these purposes individuals and corporations who are interested in 5% or more of any class of voting shares in the listed issuer, must disclose their interests and short positions in voting shares of the issuer.

When Does the Duty Arise?

Circumstances in which the duty of disclosure of a substantial shareholder arises include:

• when an individual or corporation first becomes, or ceases to be interested in, 5% or more of the shares of a listed issuer;
• when there is an increase or decrease in the percentage figure of the shareholding, which is above 5%, resulting in the interest crossing over a whole percentage number;
• when an entity has a notifiable interest and the nature of its interest in the shares changes (e.g., on exercise of an option);
• when an entity has a notifiable interest and it comes to, or ceases to, have a short position of more than 1%; and
• when an entity has a notifiable interest and there is an increase or decrease in the percentage figure of its short position that results in its short position crossing over a whole percentage number which is above 1%.

Note: A person has a notifiable interest at any time when he is interested in 5% or more of the issued share capital of a listed issuer (section 311(5) of the SFO).

De minimis Exemption

Where a person acquires an interest in shares, or ceases to be interested in shares, of the issuer and, as a result, his interest crosses over a whole percentage number, the person will not need to disclose the new interest if:
the percentage level of his interest is the same as, or less than, the percentage level of his interest given in his last notification to the Exchange and the issuer; and

- the difference between the percentage figure of his interest disclosed in his last notification and the percentage figure of his interest at all times thereafter is less than 0.5% of the issued share capital (of the same class) of the listed issuer (section 313(7) of the SFO).

**Other Exemptions**

**Wholly owned group exemption:** in certain circumstances where a parent company makes a disclosure in respect of an interest, its wholly owned subsidiary does not need to make a separate disclosure.

**Securities borrowing and lending exemption:** securities borrowing and lending are exempt from the duty of disclosure by virtue of the Securities and Futures (Disclosure of Interests—Securities Borrowing and Lending) Rules, in prescribed circumstances.

**DISCLOSURE DUTIES OF DIRECTORS AND CHIEF EXECUTIVES (Divisions 7-10 of Part XV of the SFO)**

Directors and chief executives of a listed issuer must disclose their interests and short positions in any shares in or debentures of the listed issuer (or any of its associated corporations).

**When Does the Duty Arise?**

Circumstances in which duty of disclosure of a director or chief executive arises (section 341(1) of the SFO) include:

- when he becomes, or ceases to be, interested in shares in or debentures of the listed issuer or its associated corporation;
- when he contracts to sell any shares in or debentures of the listed issuer or its associated corporation;
- when he assigns a right granted to him by the listed issuer or its associated corporation to subscribe for its shares or debentures;
- when the nature of his previously notified interests changes; and
- when he comes to have or ceases to have a short position in shares of the listed issuer or its associated corporation.

**Note:** An associated corporation means:

(a) a subsidiary or holding company of the issuer;
(b) a subsidiary of the issuer’s holding company (i.e., a fellow subsidiary); or
(c) a corporation in which the issuer has an interest exceeding 20% of any class of its issued share capital (section 308 of the SFO).

Debentures include debenture stocks, bonds and other securities of a corporation, whether constituting a charge on the assets of the corporation or not (schedule 1 of the SFO).
INTERESTS IN SHARES

For the purposes of part XV of the SFO, a person has an “interest” in shares if:

- his name is on the register of members of the issuer;
- the shares are held for him by another person, such as his stockbroker, custodian, trustee or nominee, including the Central Clearing and Settlement System;
- he is entitled to exercise rights attaching to the shares or to control their exercise; or
- he is deemed interested (see further below).

Deemed Interests

The following related persons’ interests in the shares of the issuer are attributed to (i.e., deemed held by) a substantial shareholder, director or chief executive of the listed issuer (the “Relevant Person”):

<table>
<thead>
<tr>
<th>Family Interest</th>
<th>Spouse and any child under the age of 18 of the Relevant Person</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate Interest</td>
<td>A corporation if the Relevant Person controls, directly or indirectly, one-third or more of the voting power at its general meetings, or if the corporation or its directors are accustomed to act in accordance with the Relevant Person’s directions</td>
</tr>
</tbody>
</table>
| Trust Interest           | • A trust, if the Relevant Person is a trustee or beneficiary of the trust, except in the case of a bare trust  
                          | • A discretionary trust, if the Relevant Person is the founder of the trust |
| Interest Held by Parties Acting in Concert | All persons who have agreed to act in concert to acquire interests in the shares of the issuer by an agreement to which the Relevant Person is a party |

In calculating the total number of shares in which the Relevant Person is interested, his deemed interests through the above parties are to be included.

TIMING OF NOTIFICATION

For most relevant events, notifications must be given within three business days (excluding Saturdays) of the day the Relevant Person becomes aware of the relevant event which triggered the duty of disclosure. However, for an initial notification, such as when a director first comes under a duty of disclosure by reason of holding shares in the issuer at the time it becomes a listed corporation, or by reason of holding shares in an associated corporation when the director becomes a director of the issuer, notification must be given within 10 business days (excluding Saturdays) of the date of the relevant event.
E. INSIDER DEALING

Insider dealing is both a criminal offense and a form of civil market misconduct governed by Part XIII of the SFO. As noted in the Model Code in Appendix 10 to the Listing Rules, directors of an issuer wishing to deal in any of its securities must first have regard to the insider dealing provisions.

Listed issuers must adopt rules governing directors’ dealings on terms no less exacting than those of the Model Code. Any breach of the required standard will be treated as a breach of the Listing Rules (Listing Rule 13.67). For more details on the Model Code, see Chapter 10 of this Guide.

OVERVIEW OF INSIDER DEALING REGIME

Under the insider dealing provisions, where a person (i) has information which he knows is relevant information in relation to that listed corporation and (ii) is connected with that listed corporation, or received the information (directly or indirectly) from a person whom he knows is so connected and whom he knows (or has reasonable cause to believe) held the information as a result of being so connected, that person should not deal, or counsel or procure another to deal, or disclose information to another person knowing or having reasonable cause to believe that such other person will make use of the information for the purpose of dealing, or of counseling or procuring another person to deal, in the securities of the Hong Kong listed corporation (or a related corporation) or their derivatives.

The key elements of these restrictions and their implications are:

1. Relevant Information

Inside information, defined in the SFO as “relevant information,” is information that is not generally known and is material and specific. The term means specific information about:

- a corporation or a shareholder or officer of the corporation; or
- the listed securities of the corporation or their derivatives.

It only applies where such information is not generally known to those persons who are accustomed or would be likely to deal in the listed securities of that corporation. What is “material” information is a question of fact to be assessed on the basis of how general investors would have acted on the date when the dealing took place, if they had known the relevant information.

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1. In the 2009 case regarding Chaoda Modern Agriculture, the MMT stated that “it is not necessary that all the particulars or details of the transaction, event or matter be precisely known,” but that there is “substantial commercial reality” to the event occurring.
2. Connected

The SFO defines persons who are “connected” with a corporation in very broad terms, including among others (broadly, and in addition to group companies’ directors, employees and substantial shareholders) any person who has access to relevant information concerning the corporation by reason of his being “connected” with another corporation, where the information relates to any actual or contemplated transaction involving both those corporations, or involving one of them and the listed securities of the other or their derivatives, or to the fact that such a transaction is no longer contemplated. Those who are wall crossed in relation to a prospective transaction involving a listed corporation will typically be “connected” with it by virtue of receiving information from a person falling within this definition.

3. Dealing, Counseling or Procuring

The SFO’s scope extends to a wide range of dealings in listed securities or their derivatives. A person “deals” in securities or their derivatives if (whether as principal or agent and whether on or off market) he buys, sells, exchanges or subscribes for listed securities or their derivatives or agrees to do so, or acquires or disposes of, or agrees to acquire or dispose of, the right to buy, sell, exchange or subscribe for any listed securities or their derivatives (section 289 of the SFO).

Insider dealing also takes place when a person with relevant information counsels or procures another to deal in listed securities or their derivatives (section 291(1)(b) of the SFO).

SFC ENFORCEMENT ACTIONS

Under the civil regime of the SFO, the MMT is empowered to impose various sanctions, including:

- disqualification orders (disqualification as director, liquidator, receiver or manager of listed companies, etc.);
- cold-shoulder orders (bar on banned individuals having access to assistance from SFC licensees in acquiring, disposing of or dealing in securities or financial products for a period not exceeding five years); and
- disciplinary referrals.

Under the criminal regime of the SFO, a person who commits an insider dealing offense may be liable to a fine of up to HK$10 million and to a maximum of 10 years’ imprisonment.
F. ISSUE OF SHARES

CONSENT FOR ISSUE OF NEW SHARES/SUBSCRIPTION RIGHTS \((\text{Listing Rule 13.36}(1)(a))\)

In order to protect the shareholders of listed issuers from dilution, the Listing Rules require an issuer to obtain its shareholders’ consent (subject to exceptions noted below) for any allotment, issue or grant by it of any:

- shares;
- convertible securities; or
- options, warrants or similar rights to subscribe for any shares or convertible securities.

EXCEPTIONS TO SHAREHOLDERS’ CONSENT

However, no such consent is required in the following circumstances:

- Rights issue/open offer: where a listed issuer offers new shares to its existing shareholders on a pro rata basis \((\text{Listing Rule 13.36}(2)(a))\) (see section G below for further details); or
- General mandate: where the existing shareholders have by ordinary resolution in a general meeting given a general mandate to the directors to allot or issue such shares or to grant any offers or options which would require the issue, allotment or disposal of shares during the continuance of such mandate \((\text{Listing Rule 13.36}(2)(b))\).

Such a general mandate is subject to a restriction that the number of securities allotted or agreed to be allotted must not exceed the aggregate of 20% of the existing issued share capital of the issuer and, if so resolved separately by the shareholders, the number of such securities repurchased by the issuer since the granting of the general mandate (up to 10% of the existing issued share capital).

A general mandate may only continue in force until:

- the end of the first annual general meeting after it has been granted, at which time it lapses unless renewed; or
- it is revoked or varied by ordinary resolution in general meeting.

NO SHARE ISSUE WITHIN SIX MONTHS OF LISTING \((\text{Listing Rule 10.08})\)

The Exchange does not permit further issues of shares or securities convertible into equity securities of a listed issuer within six months of listing except for:

- the issue of shares pursuant to a share option scheme under Chapter 17 of the Listing Rules or Chapter 23 of the GEM Listing Rules;
- the exercise of conversion rights attaching to warrants issued as part of the initial public offering;
- any capitalization issue, capital reduction, consolidation or subdivision of shares;
- the issue of shares or securities pursuant to an agreement entered into before the commencement of dealing and disclosed in the issuer’s listing document; and
• 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 under Chapter 9A.

SUBSEQUENT LISTINGS (Listing Rule 13.26)

Prior to any share issue, an issuer must apply for the listing of any securities of the same class as securities already listed, and may not issue such securities until the Exchange has granted approval for their listing.

The Exchange issued a “Guide on Practices and Procedures for Post-vetting Announcements of Listed Issuers and Handling Matters Involving Trading Arrangements prior to Publication of Announcements” (the “Trading Arrangement Guide”) in January 2009 (updated in January 2010), which sets out specific information required in relation to subsequent listings.

PLACINGS

No placing for cash may be made by a listed issuer pursuant to a general mandate at an issue price representing a discount of 20% or more to the benchmarked price (Listing Rule 13.36(5)). The benchmarked price is the higher of the closing price on the date of the placing agreement and a five-day trailing average.

Appendix 6 of the Listing Rules sets out the requirements for a placing by an issuer. For further details, see Chapter 7 of this Guide.

G. RIGHTS ISSUES AND OPEN OFFERS

Rights issues and open offers are offers of shares by the issuer to its shareholders on a pro rata basis. They fall within one of the exceptions under which shareholders’ consent is not required by the Listing Rules for the issue of shares (Listing Rule 13.36(2)(b)).

DIFFERENCES BETWEEN RIGHTS ISSUES AND OPEN OFFERS

A rights issue is an offer by way of rights to existing shareholders which enables them to subscribe securities in proportion to their existing shareholdings, or to renounce and sell the subscription rights (Listing Rule 7.18).

An open offer is an offer to existing shareholders to subscribe for securities on the basis that, although their subscription rights are proportionate to their existing shareholdings, others may take up any unsubscribed securities. In an open offer, securities offered to shareholders are not allotted to them as renounceable documents as in the case of a rights issue. An open offer may be combined with a placing, made subject to the rights of existing shareholders to subscribe part or all of the placed securities on a pro rata basis (Listing Rule 7.23).
CHAPTER 12  POST-LISTING CONTINUING OBLIGATIONS

REQUIREMENTS FOR RIGHTS ISSUES AND OPEN OFFERS

1. **Offer Period (Listing Rules 7.20 and 7.25)**

   Rights issues and open offers must remain open for acceptance for a period of not less than 10 business days. Where an issuer proposes an offer period of more than 15 business days, such as where there is a large number of overseas shareholders, the Exchange must be consulted.

2. **Fully Underwritten (Listing Rules 7.19(1) and 7.24(1))**

   Underwriting provides a degree of certainty to the issuer through commitment of sound financial institutions. In normal circumstances, a rights issue or an open offer must be fully underwritten. However, there may be circumstances where it is appropriate to proceed without underwriting, subject to additional disclosure requirements (Listing Rules 7.19(3) and 7.24(4)) and prior notification to the Exchange (e.g., where the issuer has specific intended uses for the proceeds and additional underwriting costs are not justified).

3. **Shareholders’ Approval (Listing Rules 7.19(6) and 7.24(5))**

   The general rule under Listing Rule 13.36(2)(b) is that the shareholders’ consent is not required for any offering to shareholders on a pro rata basis. But a proposed rights issue or open offer must be approved by shareholders in general meeting if it would increase the issued share capital or market capitalization of the issuer by more than 50%, either on its own or when aggregated with any rights issues or open offers announced by the issuer:
   - within 12 months before announcement of the proposed rights issue or open offer or
   - before that 12-month period, where dealing in the new shares started within the 12-month period.

   In such case, a circular must be issued setting out required information such as the purpose of the proposed rights issue or open offer and the total funds to be raised (Listing Rules 7.19(6)(b) and 7.24(5)(b)).

H. **SUSPENSION AND RESUMPTION OF TRADING**

The suspension and resumption of trading of listed securities are regulated by Chapter 6 of the Listing Rules.

**Suspension of Trading**

Where necessary in the interests of all parties, a request for suspension must be made by the issuer or issuer’s authorized representative or financial adviser with specific supporting reasons (Listing Rule 6.02); although in many cases, the issue of an announcement is preferable to the fettering of the proper functioning of the market by suspension.
Whether or not a request has been made to the Exchange, it may also suspend dealing in the issuer’s securities (Listing Rule 6.01) where:

- the issuer has failed to comply with the Listing Rules in a material manner;
- there are insufficient securities in public hands;
- the issuer does not have a sufficient level of operations or sufficient assets to warrant the continued listing;
- the issuer or its business is no longer suitable for listing; or
- the issuer has failed to publish timely financial information (Listing Rule 13.50).

RESUMPTION OF TRADING

The Exchange has power to direct the resumption of trading of suspended securities, and the issuer may be required to issue an announcement in respect of the terms of the resumption (Listing Rule 6.07).

The Exchange considers that the continuation of any suspension for longer than absolutely necessary denies reasonable access to the market and prevents its proper functioning. The Exchange’s power to direct resumption may only be exercised after giving the issuer the opportunity to be heard, and at the hearing the burden is on the issuer opposing the resumption of trading to satisfy the Exchange that a continued suspension would be appropriate (Listing Rule 6.08).

WITHDRAWAL OF LISTING

An issuer may voluntarily withdraw its listing on the Exchange if:

- after a general offer, a right to compulsory acquisition is exercised resulting in the acquisition of all the listed securities of the issuer or
- the issuer is privatized by way of a scheme of arrangement or capital reorganization, which is governed by and in compliance with the Takeovers Code,

and notice of the withdrawal has been given to shareholders by way of an announcement (and the intention not to retain its listing on the Exchange has been set out in a shareholder circular) (Listing Rule 6.15). In other cases, additional restrictions apply.
I. SHARE REPURCHASES

In Hong Kong, a share repurchase by a listed issuer can be achieved by:

• a repurchase by a general offer to all shareholders,
• an on-market repurchase (an offer made through the Exchange), or
• an off-market repurchase.

Each of these methods is subject to restrictions in the Listing Rules and the Share Repurchase Code, in addition to requirements under the laws of the place of incorporation.

REPURCHASE BY GENERAL OFFER

A repurchase by general offer has to be authorized by the independent shareholders of the listed issuer at a general meeting in accordance with the requirements of the Share Repurchase Code. The notice of meeting must be accompanied by the offer document.

Share repurchases by general offer must be made to all shareholders of the class, and arrangements must be made for those shareholders who wish to do so to accept in full for the relevant percentage of their holdings. Shares tendered in excess of this percentage must be accepted by the offeror from each shareholder in the same proportion as the number tendered to the extent necessary to enable the offeror to obtain the total number of shares for which the offer has been made.

ON-MARKET REPURCHASE

On-market share repurchases by listed issuers are subject to restrictions under the Listing Rules. An issuer whose primary listing is on the Exchange may only repurchase shares on the Exchange if:

• the shares proposed to be repurchased are fully paid up;
• the issuer has previously sent its shareholders an explanatory statement in compliance with the Listing Rules; and
• the shareholders of the issuer have given specific approval or a general mandate to the directors of the issuer to make such repurchases by way of an ordinary resolution, and a copy of such resolution has been delivered to the Exchange (Listing Rule 10.06(1)(a)).

The total number and description of the shares which the issuer is authorized to repurchase may not exceed 10% of the issued share capital of the issuer as at the date of the resolution granting the mandate (Listing Rule 10.06(1)(c)(iii)). In addition, the issuer must also submit a confirmation to the Exchange that the explanatory statement fulfills the contents requirements and that the share repurchase and explanatory statement contain no unusual features, and submit a compliance undertaking from the directors (Listing Rule 10.06(1)(b)).
Dealing Restrictions
The following dealing restrictions apply to repurchases of shares on the Exchange (Listing Rule 10.06(2)):

- no purchase of shares if the purchase price is higher by 5% or more than the average closing market price for the five trading days preceding the day on which the shares were traded on the Exchange;
- no purchase of shares for a consideration other than cash or for settlement other than in accordance with the trading rules of the Exchange from time to time;
- no purchase of shares from a connected person, and a connected person shall not knowingly sell shares to the issuer, on the Exchange;
- the issuer must procure that any broker it appoints to effect the repurchases will disclose to the Exchange any information on the repurchases as the Exchange may request;
- the issuer must not purchase its shares on the Exchange at any time after a price-sensitive development has occurred or has been the subject of a decision until the price-sensitive information is publicly available. In particular, the issuer should not repurchase any shares in the period starting one month before the earlier of:
  - the date of the board meeting for the approval of the issuer's results for any year, half-year, quarter or other interim period and
  - the deadline for the issuer to publish an announcement of its results for any year, half-year, quarter or other interim period,
  and ending on the date of the results announcement; and
- the repurchase must not result in the public float falling below 25% (or any lower level determined by the Exchange for the relevant issuer upon its listing).

The Exchange may waive all or part of the above restrictions if, in its opinion, there are exceptional circumstances justifying the waiver (Listing Rule 10.06(2)(g)).

STATUS OF REPURCHASED SHARES
The listing of all shares which are repurchased by an issuer (on the Exchange or otherwise) must be automatically cancelled, and the issuer must apply for listing of any further issues of that type of shares in the normal way (Listing Rule 10.06(5)). The issuer must ensure that the documents of title of repurchased shares are cancelled and destroyed as soon as reasonably practicable following the settlement of any such purchase.

SUBSEQUENT ISSUES
Without the prior approval of the Exchange, an issuer may not issue new shares or announce a proposed new issue of shares within 30 days after any share repurchase, whether on the Exchange or otherwise (other than an issue of securities pursuant to the exercise of warrants, share options or similar instruments requiring the issuer to issue securities, which were outstanding prior to that repurchase) (Listing Rule 10.06(3)).
OFF-MARKET REPURCHASES

The Share Repurchase Code provides that off-market repurchases must be approved by the SFC and by at least three-fourths of the votes cast on a poll by disinterested shareholders at a general meeting (Rule 2 of Share Repurchase Code). The notice of the meeting must comply with certain minimum content requirements, and the directors must have made diligent inquiries of the members who will be affected by the proposal. In addition, the purchase agreement has to be disclosed.

J. PUBLIC FLOAT

At least 25% of a listed issuer’s total issued share capital must be held in public hands at all times (Listing Rule 8.08), save that at the time of listing (but not later) the Exchange may at its discretion grant to eligible issuers (of sufficient size) a lower required percentage (Listing Rule 8.08(1)(d)).² Compliance with the required level must be disclosed in the issuer’s annual report (Listing Rule 13.35).

NOTIFICATION TO EXCHANGE

Once a listed issuer becomes aware that its public float has fallen below 25% (or any lower minimum applicable to it), or if any part of the securities of the issuer or its subsidiary becomes listed or traded on any other stock exchange, it must inform the Exchange immediately (Listing Rule 13.32(1)).

SUSPENSION OF TRADING

Where a listed issuer’s percentage of a public float falls below the required level, the Exchange will normally require suspension of trading in its securities (Listing Rule 13.32(3)), and reserves the right to continue suspension until appropriate steps have been taken to restore the required level.

PUBLIC FLOAT WAIVER AFTER GENERAL OFFER

In the case of an issuer which is the subject of a general offer under the Takeovers Code, the Exchange may grant a temporary waiver of the public float requirement for a reasonable period after the close of the general offer (Listing Rule 13.33).

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² Having conducted a public consultation in 2008, the Exchange has in some cases granted waivers substituting a required public float of not less than 10% where the market capitalization of the issuer exceeds HK$40 billion (approximately US$5.1 billion).
CHAPTER 12  POST-LISTING CONTINUING OBLIGATIONS

K. NOTIFIABLE AND CONNECTED TRANSACTIONS

NOTIFIABLE TRANSACTIONS
The classification of notifiable transactions is based on the calculation of the following percentage ratios:

<table>
<thead>
<tr>
<th>Ratio</th>
<th>Formula</th>
</tr>
</thead>
</table>
| Asset ratio            | \[
|                        | \frac{\text{Total assets which are the subject of the transaction}}{\text{Total assets of the listed issuer}} \] |
| Profits ratio          | \[
|                        | \frac{\text{Profits attributable to the assets which are the subject of the transaction}}{\text{Profits of the listed issuer}} \] |
| Revenue ratio          | \[
|                        | \frac{\text{Revenue attributable to the assets which are the subject of the transaction}}{\text{Revenue of the listed issuer}} \] |
| Consideration ratio    | \[
|                        | \frac{\text{Consideration}}{\text{Total market capitalization of the listed issuer}} \] |
| Equity Capital ratio*  | \[
|                        | \frac{\text{Nominal value of the issuer's equity capital issued as consideration}}{\text{Nominal value of the issuer’s issued equity capital before the transaction}} \] |

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

Transactions are classified in the following types based on their percentage ratios (Listing Rule 14.08):

- **Share transaction**: less than 5% in all percentage ratios and involving an acquisition of assets (other than cash) by a listed issuer where the consideration includes securities for which listing will be sought;
- **Disclosable transaction**: 5% or more but less than 25% in any percentage ratio;
- **Major transaction (disposal)**: 25% or more but less than 75% in any percentage ratio, except for equity capital ratio;
- **Major transaction (acquisition)**: 25% or more but less than 100% in any percentage ratio;
- **Very substantial disposal**: 75% or more in any percentage ratio; and
- **Very substantial acquisition**: 100% or more in any percentage ratio.
Different types of notifiable transaction are subject to the following different disclosure requirements. Chapter 14 of the Listing Rules explains the specific requirements in more detail.

<table>
<thead>
<tr>
<th>Disclosure Requirements</th>
<th>Notification to Exchange</th>
<th>Publication of Announcement</th>
<th>Circular to Shareholders</th>
<th>Shareholders’ Approval</th>
<th>Accountants’ Report</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Transaction</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>No(^{(1)})</td>
<td>No</td>
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<tr>
<td>Disclosable Transaction</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
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<tr>
<td>Major Transaction</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes(^{(2)})</td>
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<td>Very Substantial Disposal</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Very Substantial Acquisition</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes(^{(2)})</td>
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<tr>
<td>Reverse Takeover</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes(^{(3)})</td>
<td>Yes(^{(2)})</td>
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</tbody>
</table>

Notes:  
(1) No shareholders’ approval is necessary if the consideration shares are issued under a general mandate.  
(2) An accountants’ report on the business, company or companies being acquired is required.  
(3) Approval from the Exchange is necessary.

**CONNECTED TRANSACTIONS**


See Chapter 9 of this Guide for more details.

**WHERE A CONNECTED TRANSACTION IS ALSO A NOTIFIABLE TRANSACTION**

A connected transaction may also be a notifiable transaction under Chapter 14 of the Listing Rules, and accordingly, subject to the relevant disclosure requirements. In such cases, additional disclosures should be made in the circular as required for that type of notifiable transaction (*Listing Rule 14A.60*).
<table>
<thead>
<tr>
<th><strong>GLOSSARY</strong></th>
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<tr>
<td><strong>A1</strong></td>
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<td><strong>carrying amount</strong></td>
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</tbody>
</table>
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