Responsibilities of Directors Of Companies Listed on The Growth Enterprise Market of The Stock Exchange of Hong Kong Limited

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THE MAJOR SOURCES OF DIRECTOR's OBLIGATIONS

1. common law and applicable legislation, including the Companies Ordinance and the Securities and Futures Ordinance (**"SFO"**);

2. the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the **"GEM Rules"**);

3. the Code on Takeovers and Mergers and the Code on Share Buy-backs ("**Takeovers Code**");

4. the directors' Declaration and Undertaking to the Exchange; and

5. the Companies Registry's Guide on Directors' Duties.

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DIRECTORS'S OBLIGTION TO ENSURE ISSUER'S COMPLIANCE WITH LISTING RULES

- A listed issuer undertakes in its application for listing to comply with the Listing Rules once its securities are listed on the Exchange.
- Under GEM Rule 17.03, the directors of a listed issuer are collectively and individually responsible for ensuring that the listed issuer complies fully with the requirements of the GEM Rules.

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DIRECTORS'S DECLARATION AND UNDERTAKING

A director undertakes that he will:

- comply to the best of his ability with the GEM Rules and use his best endeavours to ensure that the listed issuer complies with the GEM Rules;
- comply to the best of his abilities with the requirements of the SFO, the Takeovers Code, the Code on Share Buy-backs, the Companies Ordinance and all other securities laws and regulations from time to time in force in Hong Kong and use his best endeavours to ensure that the listed issuer so complies; and
- cooperate in any investigation conducted by the Listing Division and/or the GEM Listing Committee of the Exchange.

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FIDUCIARY DUTIES OF DIRECTORS

1. Duty to act honestly and in good faith in the interests of the company as a whole
2. Duty to act for a proper purpose
3. Duty in relation to the assets of the listed issuer
4. Duty to avoid actual and potential conflicts of interest and duty
5. Duty to disclose fully and fairly his interests in contracts with the listed issuer
6. Duty to apply such degree of skill, care and diligence as may reasonably be expected of a person with his knowledge and experience and acting as a director of a listed issuer (GEM Rule 5.01)

Duties summarised in the Companies Registry's Guide on Directors' Duties (Attachment A)

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STATUTORY DUTY UNDER THE NEW COMPANIES ORDINANCE

Section 465(2) of the new Companies Ordinance (Cap. 622) adopts a mixed objective and subjective test for directors' duty of skill, care and diligence. The standard of care, skill and diligence required is that which would be exercised by a reasonably diligent person with:

- 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 (***the objective test***); and
- the general knowledge, skill and experience that the director has (***the subjective test***).

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

The directors of a non-Hong Kong company which is listed on the Exchange must comply with the statutory duty since they are required by GEM Rule 5.01 to exercise duties of skill, care and diligence to the standard set by Hong Kong law.

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CONSEQUENCES OF NON-COMPLIANCE WITH THE GEM RULES

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

- issue a private reprimand;
- issue a public statement which involves criticism;
- issue a public censure;
- report the offender's conduct to a regulatory authority (e.g. the SFC) or to an overseas regulatory authority;
- require a breach to be rectified or other remedial action taken within a stipulated period;
- state publicly that in the Exchange's opinion the retention of office by the director is prejudicial to the interest of investors; and
- take (or refrain from taking) such other action as the Exchange thinks fit. (GEM Rule 3.10)

If the Exchange considers the issuer failed in a material manner to comply with the GEM Rules, it can suspend dealings in, or cancel the listing of, the issuer's securities (GEM Rule 9.01).

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CONSEQUENCES OF NON-COMPLIANCE WITH THE GEM RULES (Cont'd)

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

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

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DIRECTORS' LIABILITIES FOR MISSTATEMENTS IN PROSPECTUS

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

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

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DIRECTORS' LIABILITIES FOR MISSTATEMENTS IN PROSPECTUS (Cont'd)

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

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

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DIRECTORS' LIABILITIES FOR MISSTATEMENTS IN PROSPECTUS (Cont'd)

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

- **Section 107 SFO** – imposes criminal liability for making any fraudulent or reckless misrepresentation to induce others to deal in securities

- **Section 298 SFO** – imposes criminal liability for disclosure of false or misleading information to induce dealings

- **Section 384 SFO** – imposes criminal liability for provision of false or misleading information in a prospectus or other document filed with the Exchange or the SFC

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

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

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RESTRICTION ON DISCLOSURE OF MATERIAL INFORMATION TO ANALYSTS

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

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

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

Breach of the prospectus laws is a criminal offence.

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RESTRICTION ON DISCLOSURE OF MATERIAL INFORMATION TO ANALYSTS (Cont'd)

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

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

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

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RESTRICTION ON DISCLOSURE OF MATERIAL INFORMATION TO ANALYSTS (Cont'd)

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

- In case of disclosure (whether intentional or not) to analysts, the Company may be compelled to disclose the same information in the prospectus;

- Such information may not be appropriate for a prospectus and may not be verifiable.

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RESTRICTION ON DISCLOSURE OF MATERIAL INFORMATION TO ANALYSTS (Cont'd)

Consequences of putting such a statement in the prospectus

- any untrue statement (including any statement that is false, misleading or deceptive) in a prospectus may give rise to criminal and civil liability, including personal liabilities of each director and any other person who authorised the issue of the prospectus; and

- the directors must likewise take personal liability for the truthfulness, accuracy and completeness of any information the Company may be compelled under the SFC rules to insert into the prospectus under the above circumstances.

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

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

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RESTRICTION ON FUNDAMENTAL CHANGE IN THE NATURE OF THE BUSINESS IN 12 MONTHS AFTER LISTING

In the first 12 months after dealings in an issuer's securities commence on GEM, an issuer is prohibited from entering into any transaction or arrangement which would result in a fundamental change to its principal business activities or those of its group.

The Exchange may grant a waiver of this prohibition if the circumstances are exceptional and the transaction or arrangement is approved by the shareholders in general meeting by a resolution on which any controlling shareholder (or if there are no controlling shareholders, any chief executive or directors (other than INEDs) of the listed issuer) and their respective associates are required to abstain from voting in favour. Shareholders with a material interest in the transaction and their associates are also required to abstain from voting on the transaction.

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RESTRICTION ON DISPOSALS BY CONTROLLING SHAREHOLDERS FOLLOWING LISTING

The Listing Rules impose restrictions on the disposal of securities by a controlling shareholder following a company's new listing. Any person shown by the listing document to be a controlling shareholder of the issuer at the time of listing must not:

i. dispose of, or enter into any agreement to dispose of, or create any options, rights, interests or encumbrances in respect of, any shares which the listing document shows to be beneficially owned by him in the period commencing on the date on which disclosure of the shareholding is made in the listing document and ending 6 months from the date on which dealings in the securities of the new applicant commence on the Exchange; or

ii. dispose of, or enter into any agreement to dispose of, or create any options, rights, interests or encumbrances in respect of, any shares which the listing document shows to be beneficially owned by him if such disposal would result in him ceasing to be a controlling shareholder in the period of 6 months commencing on the date on which the period referred to in (i) above expires

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RESTRICTION ON DISPOSALS BY CONTROLLING SHAREHOLDERS FOLLOWING LISTING (Cont'd)

There are exceptions to the above prohibitions on disposals by controlling shareholders for:

i. pledges or charges of shares created in favour of an authorised financial institution (as defined in the Banking Ordinance) as security for a bona fide commercial loan;

ii. disposals made pursuant to a power of sale under a pledge or charge referred to at (i) above;

iii. disposals on the death of a controlling shareholder or in other exceptional circumstances approved by the Exchange.

Controlling shareholders must however immediately inform the issuer if they pledge or charge any of their shares in favour of an authorised institution or pursuant to a waiver granted by the Exchange during the period commencing on the date by reference to which the shareholding is disclosed in the listing document and ending 12 months from the date on which dealings commence on the Exchange.

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STATUTORY REGIME FOR INSIDE INFORMATION DISCLOSURE – KEY FEATURES

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

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STATUTORY REGIME FOR INSIDE INFORMATION DISCLOSURE – KEY FEATURES (Cont'd)

- The application of an **objective test** in determining whether information is inside information: whether a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.
- Statutory obligation to disclose inside information **as soon as reasonably practicable** upon knowledge.
- An obligation on directors and officers to take reasonable measures to ensure **proper safeguards** exist to prevent corporations' breach of statutory requirements.
- Individual liability on directors/officers for corporation's breach of the requirement if such breach is a result of their intentional, reckless or negligent conduct or failure to ensure proper safeguards.
- The provision of "**safe harbours**" for legitimate circumstances where non-disclosure or late disclosure is permitted.
- The SFC can **investigate** suspected breached and to **institute proceedings** before the MMT.
- Civil sanctions: a **fine** up to **HKD 8 million** or **disqualification** order up to **5 years**.
- Liability to pay compensation to persons who suffer financial loss as a result of the breach.

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DEFINITION OF "INSIDE INFORMATION"

Section 307A SFO

Specific information that is about:

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

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DEFINITION OF "INSIDE INFORMATION" (Cont'd)

Key elements of the definition

The three key elements of the definition are that:

- the information must be **specific;**
- the information **must not be generally known** to that segment of the market which deals or which would likely deal in the corporation's securities; and
- the information would, if generally known, be **likely to have a material effect on the price of the corporation's securities;**
- SFC guidelines provide guidance on interpretation.

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"DEFINITION OF INSIDE INFORMATION" (cont'd)

Specificity of Information

- The information must be capable of being identified, defined and unequivocally expressed
- The information need not be precise; information may be specific even though the particulars or details are not precisely known
- Information on a transaction that is only contemplated or under negotiation, while not yet subject to a final agreement, can be specific information
- Mere rumours, vague hopes, or worries, wishful thinking and unsubstantiated conjecture are not specific information

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"DEFINITION OF INSIDE INFORMATION" (cont'd)

Generally known to the market

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

"DEFINITION OF INSIDE INFORMATION" (cont'd)

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

- Test: whether the inside information would influence persons who are accustomed to or would be likely to deal in the corporation's shares, in deciding whether to buy or sell the securities

- The test is necessarily a hypothetical one since it must be applied at the time the information becomes available.

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TIMING OF DISCLOSURE

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

a) the inside information has, or ought reasonably to have, come to the knowledge of an officer of the corporation in the course of performing functions as an officer of the corporation; **and**

b) a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation (section 307B(2) SFO).

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

MEANING OF "AS SOON AS REASONABLY PRACTICABLE"

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

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

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

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

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WHO IS AN "OFFICER"?

- Officer: a director, manager or company secretary of a corporation or any other person involved in its management (Part 1 of Schedule 1 to the SFO).
- For the purpose of the inside information regime, "manager" generally connotes a person who, under the immediate authority of the board, is charged with management responsibility affecting the whole or a substantial part of the corporation.
- The formulation "in course of performing functions as an officer of the corporation" implies that only information being known in situations **where the officer is acting in capacity as an officer** is subject to the new PSI disclosure requirement.

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MANNER OF DISCLOSURE

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

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THE SAFE HARBOURS

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

Safe Harbour A

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

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THE SAFE HARBOURS (Cont'd)

Safe Harbour B

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

Examples:

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

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THE SAFE HARBOURS (Cont'd)

Safe Harbour C

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

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

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

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THE SAFE HARBOURS (Cont'd)

Safe Harbour D

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

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

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THE SAFE HARBOURS (Cont'd)

Safe harbour condition of confidentiality:

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

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

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

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

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

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SFC's POWER TO GRANT WAIVER

- The SFC can grant waivers where the disclosure of inside information in Hong Kong would be prohibited under a court order or legislation of another jurisdiction or would contravene a restriction imposed by a law enforcement agency or government authority in another jurisdiction (section 307E(1)SFO). The SFC will grant waivers on a case-by-case basis and may attach conditions.

- During an application for a waiver, confidentiality must be maintained. Should an information leakage occur, the corporation would be obliged to suspend trading prior to making a disclosure. The waiver application fee will be HK$24,000.

- A corporation must copy to the Exchange any application to the SFC for a waiver from the disclosure obligation and the SFC's decision when received.

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LIABILITY OF OFFICERS UNDER THE NEW REGIME

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

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

- the breach resulted from the officer's intentional, reckless or negligent conduct; or

- the officer has not taken all reasonable measures to ensure that proper safeguards exist to prevent the breach (section 307G(2) SFO).

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

SANCTIONS

Possible penalties imposed by the MMT:

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

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

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

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CIVIL LIABILITY – PRIVATE RIGHT OF ACTION

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

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

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

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LISTING RULE DISCLOSURE OBLIGATIONS

The role and duties of the SFC and the Exchange

The SFC is responsible for the enforcement of the statutory disclosure regime, but the Exchange will remain responsible for maintaining an orderly, informed and fair market.

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

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

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

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

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LISTING RULE OBLIGATIONS (Cont'd)

Obligation to avoid false market (GEM Rule 17.10(1))

- If it is the Exchange's view that there is, or is likely to be, a false market in a listed issuer's securities, the issuer must announce the information necessary to avoid a false market as soon as reasonably practicable after consultation with the Exchange.

- An issuer is also required to contact the Exchange as soon as reasonably practicable if it believes that there is likely to be a false market in its securities.

- Under GEM Rule 17.10(2), where an issuer is required to disclose inside information under the SFO, it must simultaneously announce the information. An issuer is also required to simultaneously copy to the Exchange any application to the SFC for a waiver from the requirement to disclose PSI and to promptly copy to the Exchange the SFC's decision whether to grant such a waiver.

LISTING RULE OBLIGATIONS (Cont'd)

Obligation to respond to the Exchange's enquiry

- GEM Rule 17.11 requires an issuer that receives an enquiry concerning unusual movements in the price or trading volume of an issuer's listed securities, the possible development of a false market in its securities, or any other matters from the Exchange, must respond promptly in one of two ways:
  - provide (and announce, if so required by the Exchange) any information it has that is relevant to the subject matter of the enquiry, so as to inform the market or to clarify the situation; or
  - if appropriate and if requested by the Exchange, issue a standard announcement confirming that the directors, **having made such enquiry with respect to the issuer as may be reasonable in the circumstances**, are not aware of any information that is or may be relevant to the subject matter of the enquiry or of any inside information that needs to be disclosed under the SFO.
- The latter response should be made in a standard form that is set out in Note 1 to the revised GEM Rule 17.11.

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LISTING RULE OBLIGATIONS (Cont'd)

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

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

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

- A note to GEM Rule 17.11 – an issuer does not need to disclose inside information under the Rules if the information is exempted from disclosure under the statutory regime as set out in Part XIVA SFO.

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TRADING HALTS OR SUSPENSION

GEM Rule 17.11A requires an issuer to request a trading halt or trading suspension if an announcement cannot be made promptly in any of the following circumstances:

a) where an issuer has information which must be disclosed under the GEM Rule 17.10;

b) an issuer reasonably believes that there is inside information which must be disclosed under the statutory disclosure obligation under Part XIVA of the SFO; or

c) circumstances exist where it reasonably believes or it is reasonably likely that confidentiality may have been lost in respect of inside information which is: (i) the subject of an application to the SFC for a waiver; or (ii) exempt from the statutory disclosure obligation (except if the exemption concerns disclosure prohibited by Hong Kong law/court order).

"Trading halts" are defined as an interruption of trading in an issuer's securities requested or directed pending disclosure of information under the Rules

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TRADING HALTS OR SUSPENSION (Cont'd)

Under GEM Rule 9.04, the Exchange also has the right to direct a trading halt or suspend dealings in an issuer's securities in a number of circumstances including where:

a) there are unexplained movements in the price or trading volume of the issuer's listed securities or where a false market for the trading of such securities has developed and the issuer's authorised representative cannot immediately be contacted to confirm that the issuer is not aware of any matter that is relevant to the unusual price movement or trading volume or the development of a false market;

b) the issuer delays in issuing an announcement in response to enquiries from the Exchange under GEM Rule 17.11; or

c) there is uneven dissemination or leakage of inside information in the market giving rise to an unusual movement in the price or trading volume of the issuer's listed securities.

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ANNOUNCEMENTS

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

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

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ANNOUNCEMENTS (Cont'd)

- **Price-sensitive information** – any price-sensitive information which is discloseable as inside information under Part XIVA SFO must be announced and kept strictly confidential until a formal announcement is made.
- **Notifiable transactions** – any notifiable transaction within Chapter 19 of the GEM Rules.
- **Connected transactions** – any connected transaction (unless an exemption is available) within Chapter 20 of the GEM Rules.

ANNOUNCEMENTS (Cont'd)

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

- exceeds 8% of the total assets of the listed issuer (GEM Rule 17.15); or
- is greater than the previously disclosed relevant advance by 3% or more of the listed issuer's total assets (GEM Rule 17.16).

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

ANNOUNCEMENTS (Cont'd)

Financial assistance to affiliated companies – where financial assistance and guarantees of financial assistance given by the listed issuer or any of its subsidiaries to affiliated companies (being those which are equity accounted for by the issuer) of the listed issuer together exceed 8% of the listed issuer's total assets (GEM Rule 17.18).

Pledge of controlling shareholder's interest – where the controlling shareholder of the listed issuer has pledged its interest in shares of the issuer to secure debts of the issuer or to secure guarantees or other support of obligations of the issuer (GEM Rule 17.19).

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ANNOUNCEMENTS (Cont'd)

Loan agreements – where:

- the listed issuer (or any of its subsidiaries) enters into a loan agreement that imposes specific performance obligations on any controlling shareholder (e.g. a requirement to maintain a specified minimum holding in the share capital of the listed issuer) and breach of such obligation will cause a default in respect of loans that are significant to the operations of the listed issuer (GEM Rule 17.20); or
- the listed issuer or any of its subsidiaries breaches the terms of a loan that is significant to the operations of the group, such that the lender may demand immediate repayment and the breach has not been waived by the lender (GEM Rule 17.21).

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

ANNOUNCEMENTS (Cont'd)

Accounts and auditors

Board meeting for approval of results – an issuer must inform the Exchange and publish an announcement at least 7 clear business days in advance of the date fixed for any board meeting at which the profits or losses for any period are to be approved for publication (GEM Rule 17.48).

Annual, half-year and quarterly results – must be published by way of announcement under Chapter 18 of the GEM Rules.

Change in auditor or financial year end – any change in a listed issuer's auditors or financial year end, the reason(s) for the change and any other matters that need to be brought to the attention of holders of the company's securities. The issuer's announcement must state whether the outgoing auditors have confirmed that there are no matters that need to be brought to the attention of holders of the company's securities (GEM Rule 17.50(4)).

The issuer must appoint an auditor at each annual general meeting (AGM) to hold office until the next AGM. Any proposal to remove an auditor before the end of its term of office must be approved by shareholders in general meeting (GEM Rule 17.100).

ANNOUNCEMENTS (Cont'd)

Company matters

Change of company name – once the board decides to change the company name (Schedule to Appendix 24 of the GEM Rules).

Memorandum and Articles of Association – any proposed alteration of the memorandum or articles of association (or equivalent documents) of the listed issuer (GEM Rule 17.50(1)).

Registered office – any change in the company's registered address, agent for service of process in Hong Kong or registered office or registered place of business in Hong Kong (GEM Rule 17.50(5)).

Share registrar – any change of the company's share registrar (including any overseas branch share registrar) (GEM Rule 17.50(3)).

Dividends – an issuer must inform the Exchange and publish an announcement at least 7 clear business days in advance of the date fixed for any board meeting at which the declaration, recommendation or payment of a dividend is expected to be decided (GEM Rule 17.48). Any decision of the board to declare, recommend or pay a dividend or not to do so must be announced immediately, and include the rate, amount and expected payment date (GEM Rules 17.49(1) and (2)).

ANNOUCEMENTS (Cont'd)

Company matters (Cont'd)

Change in nature of business – a proposed fundamental change in the issuer's/group's principal business activities must be announced immediately after it is the subject of any decision (GEM Rule 17.25).

Winding-up or Liquidation – the appointment of a receiver or manager, the presentation of any winding-up petition or the passing of any resolution authorising the winding up of the listed issuer, its holding company or any of its major subsidiaries (i.e. a subsidiary representing 5% under any of the percentage ratios (discussed in "Notifiable Transactions" later) or any similar insolvency events (GEM Rule 17.27(1)).

Decision to withdraw listing – a proposed withdrawal of listing must be notified to shareholders by way of publication of an announcement (GEM Rule 9.23).

ANNOUNCEMENTS (Cont'd)

Corporate governance

Audit committee – if the issuer fails to set up an audit committee or does not meet the membership requirements (GEM Rule 5.33). An announcement must be published of any change in membership of the audit committee (GEM Rule 17.50(3)).

Remuneration committee – if the issuer fails to set up a remuneration committee or does not comply with the requirements as to its composition or terms of reference (GEM Rule 5.36).

Directors and officers

Board composition and independent non-executive directors – an announcement must be made if number of the issuer's INEDs is less than three or one third of the number of directors on the board, or if it does not have at least one INED with appropriate professional qualifications or accounting or related financial management expertise (GEM Rule 5.06).

Change in company secretary – an announcement must be made once the board has decided to change the company secretary (GEM Rule 17.50(3)).

Change in compliance adviser – an announcement must be made as soon as a compliance adviser resigns, and arrangements must be made immediately to appoint a new compliance adviser. Once a new compliance adviser has been appointed, another announcement must be made (GEM Rules 17.50(3) and 6A.29).

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Corporate governance (Cont'd)

Change in compliance officer – an announcement must be published of any change to the issuer's compliance officer (GEM Rule 17.50(3)) or if the issuer does not have a compliance officer (GEM Rule 5.23).

Change in directors or supervisors – any change of directors, including, in the case of the resignation of a director, the reasons given by the director for his resignation (GEM Rule 17.50(2)). An announcement of the appointment of a new director or re-designation of a director must include the information specified in GEM Rule 17.50(2).

Change in disclosed information about directors – any change to the information specified in paragraphs (h) to (v) of GEM Rule 17.50(2) previously disclosed about a director must be announced (GEM Rule 17.50A). Such information relates mainly to matters which may cast doubt on the integrity of the directors involved and their suitability for continuing to serve as directors. Any change in the information specified in paragraphs (a) to (e) and (g) of GEM Rule 17.50(2) must be set out in the next published annual or interim report. The Rules include an obligation for directors to inform the issuer immediately of any information specified in GEM Rule 17.50(2) and any change to such information (GEM Rule 17.50B).

ANNOUNCEMENTS (Cont'd)

Meetings

Notice of general meetings – notice of an issuer's annual general meeting and other general meetings must be announced (GEM Rules 17.44 and 17.46(2)).

Results of general meetings – the results must be published before commencement of trading on the business day following the meeting (GEM Rule 17.47(5)).

ANNOUNCEMENTS (Cont'd)

Shares

Issues of securities – an issue of securities (including convertible securities or warrants, options or similar rights) will almost always require an announcement (except an exercise of options under an employee share scheme) either as inside information under GEM Rule 17.10(2)(a), or under Chapter 19 or 20, or under GEM Rule 17.30.

Changes in number of issued shares – certain changes in the number of issued shares must be reported to the Exchange for publication on the Exchange's website on the following business day (GEM Rule 17.27A). Issuers must also submit a monthly return of changes in its equity securities, debt securities and other securitised instruments (GEM Rule 17.27B).

Shares (Cont'd)

Share option schemes – an employee share option scheme must be approved by shareholders in general meeting and a listed issuer must publish an announcement of the outcome of the meeting as soon as possible and no later than the business day following the meeting (GEM Rule 23.02(1)(a)). Further announcements must be published on the grant of share options pursuant to a share option scheme specifying the information required by GEM Rule 23.06A.

Basis of allotment of securities – the basis of allotment of any securities offered to the public for subscription or sale or an open offer and of the results of the offer and, if applicable, of the basis of any acceptance of excess applications. The company must notify the Exchange of such matters no later than the morning of the next business day after the allotment letters or other relevant documents of title are posted (GEM Rule 16.13).

Shares (Cont'd)

Public float – The company must inform the Exchange immediately and publish an announcement if it becomes aware that the number of its listed securities held by the public has fallen below the prescribed minimum percentage (i.e. 25% unless a lower percentage of between 15% and 25% was approved by the Exchange on listing for a company having an expected market capitalisation at the time of listing of more than HK$10 billion) (GEM Rules 11.23(7), 11.23(10) and 17.36).

Share Repurchases – any purchase, sale, drawing or redemption by the issuer or its group members of its listed securities (whether on the Exchange or not) (GEM Rule 17.35). The company should also be aware of the provisions of the Code on Share Buy-backs which sets out detailed rules governing any offer to purchase, redeem or otherwise acquire the shares of a listed issuer made by or on behalf of the listed issuer to any of its shareholders.

Announcements which Require Pre-vetting by the Exchange

Announcements of the following matters or transactions must be submitted to the Exchange for review and approval before publication under GEM Rule 17.53(2):

a. very substantial acquisitions, very substantial disposals or reverse takeovers under GEM Rules 19.34 and 19.35;

b. transactions or arrangements within 12 months after listing which would result in a fundamental change in principal business activities under GEM Rules 19.88 to 19.90; and

c. matters relating to cash companies under GEM Rules 19.82 and 19.83.

Announcements other than those specified in GEM Rule 17.53(2) do not need to be pre-vetted by the Exchange, although companies may consult the Exchange regarding rule compliance issues. The Exchange also reserves the right under GEM Rule 17.53A to require listed companies to submit for review any draft announcement, circular or other document in individual cases.

For a summary of the pre-vetting requirements for announcements, reference should be made to the Exchange's Pre-vetting Guide at Attachment C.

MATTERS REQUIRING PRIOR CONSULTATION WITH EXCHANGE PRIOR TO ANNOUNCEMENT

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

i. whether the Exchange will allow the listed issuer to adopt alternative size test(s) to classify a transaction under GEM Rule 19.20;

ii. whether the Exchange will deem a party to a transaction to be a connected person of the listed issuer under GEM Rules 20.17 to 20.19. GEM Rule 20.20 requires a listed issuer to notify the Exchange of any proposed transaction with a party described in such rules unless the transaction is exempt;

iii. whether the transaction/matter falls under the special or exceptional circumstances described in the Listing Rules, e.g. a proposed issue of securities for cash under general mandate at a price representing a discount of 20% or more to the benchmarked price under GEM Rule 17.42B; or a proposed issue of warrants that would not meet certain specific requirements under GEM Rule 21.02; and

iv. In the case of matters affecting trading arrangements (including suspension or resumption of trading, and cancellation or withdrawal of listing), GEM Rule 17.53B requires that:

   a. listed issuers must consult the Exchange before issuing the relevant announcement; and

   b. the announcement must not include any reference to a specific date or timetable which has not been agreed in advance with the Exchange.

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ANNOUNCEMENTS (Cont'd)

Publication of Announcements

- Announcements must be published on the GEM website and on the listed issuer's own website.
- Listed companies must submit an electronic copy of the announcement through the Exchange's electronic submission system (HKEx-EPS).
- When doing so, companies must select all appropriate headlines from the list of headline categories which are set out in Appendix 17 to the GEM Rules.
- Unless stated otherwise in the Rules, all announcements must be published in both English and Chinese.

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ANNOUNCEMENTS (Cont'd)

Publication of Announcements (Cont'd)

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

On a normal business day:

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

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

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

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ANNOUNCEMENTS (Cont'd)

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

i. suspension announcements;

ii. announcements made in response to unusual movements in share price or trading volume;

iii. announcements denying the accuracy of news reports or clarifying that only its published information should be relied upon; and

iv. overseas regulatory announcements.

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LISTING DOCUMENTS AND CIRCULARS WHICH REQUIRE PRE-VETTING

GEM Listing Rule 17.53(1) requires the following documents to be submitted to the Exchange for review and approval before publication:

- listing documents (including prospectuses);
- circulars relating to cancellation or withdrawal of listing of listed securities;
- circulars for notifiable transactions which are subject to shareholders' approval;
- circulars for connected transactions;
- circulars to the company's shareholders seeking their approval of issues of securities that require specific mandates from the shareholders (under GEM Rules 17.39 and 17.40);

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LISTING DOCUMENTS AND CIRCULARS WHICH REQUIRE PRE-VETTING (Cont'd)

- circulars to the issuer's shareholders seeking their approval of transactions or arrangements that require independent shareholders' approval and the inclusion of separate letters from independent financial advisers to be contained in the relevant circulars under GEM Rule 17.47(7), which include:
  - a) spin-off proposals;
  - b) transactions which the Rules require to be subject to independent shareholders' approval (see GEM Rule 17.47(5)(b)) such as:
    - i. rights issues under GEM Rule 10.29;
    - ii. open offers under GEM Rule 10.39;
    - iii. refreshments of general mandates before next AGM under GEM Rule 17.42A;
    - iv. withdrawal of listings under GEM Rule 9.20; and
    - v. transactions or arrangements that would result in a fundamental change in the principal business activities of the listed issuer within 12 months after listing under GEM Rules 19.88 to 19.90;
- circulars to the issuer's shareholders seeking consent to an allotment of voting shares that will alter the control of the issuer (under GEM Rule 17.40)

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LISTING DOCUMENTS AND CIRCULARS WHICH REQUIRE PRE-VETTING (Cont'd)

- circulars to shareholders seeking their approval of any matter in relation to a share option scheme which is required under Chapter 23 of the GEM Listing Rules;
- circulars to shareholders seeking their approval of warrant proposals involving approvals by shareholders and all warrantholders under GEM Rule 21.07(3); and
- circulars or offer documents issued by the issuer in connection with takeovers, mergers or offers.

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DISCLOSURE OF CHANGES IN THE NUMBER OF ISSUED SHARES

- **Next Day Disclosure Requirements**

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

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DISCLOSURE OF CHANGES IN THE NUMBER OF ISSUED SHARES (Cont'd)

- The first category of changes in the number of issued shares which always require next day disclosure on the next business day under GEM Rule 17.27A(2)(a), include those that result from the following:
  - placings;
  - consideration issues;
  - open offers;
  - rights issues;
  - bonus issues;
  - scrip dividends;
  - repurchases of shares or other securities;
  - exercise of an option (whether under a share option scheme or not) by a director of the listed issuer;
  - capitalisation reorganisation; or
  - change in the number of issued shares not falling within any of the categories referred to above or in GEM Rule 17.27A(2)(b).

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DISCLOSURE OF CHANGES IN THE NUMBER OF ISSUED SHARES (Cont'd)

- Categories of changes in the number of issued shares specified in GEM Rule 17.27A(2)(b) require next day disclosure in specified circumstances:
  - exercise of an option under a share option scheme other than by a director of the listed;
  - exercise of an option other than under a share option scheme not by a director of the listed issuer;
  - exercise of a warrant;
  - conversion of convertible securities; or
  - redemption of shares or other securities.
- The specified circumstances include:
  - where the event results in a change of 5% or more in the number of the listed issuer's issued shares; or
  - where the listed issuer is required to make disclosure of a first category change and an event has occurred but not been disclosed (either as a second category change or in a monthly return (because the 5% *de minimis* threshold has not been reached)).

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DISCLOSURE OF CHANGES IN THE NUMBER OF ISSUED SHARES (Cont'd)

- **Monthly Return**
  - in relation to movements in the listed issuer's equity securities, debt securities and any other securitised instruments during the period to which the monthly return relates
  - the return must be submitted no later than 30 minutes before the earlier of the commencement of the morning trading session or any pre-opening session on the fifth business day next following the end of each calendar month
  - the monthly return must be submitted irrespective of whether there has been any change in the information provided in the previous monthly return.

DISCLOSURE OF FINANCIAL INFORMATION

Annual Report and Accounts

A listed issuer must send a copy of its annual report including its annual accounts (and consolidated financial statements, if the company prepares them) together with a copy of the auditors' report to every shareholder of the company and every holder of the company's listed securities not less than **21 days** before the date of the company's AGM and not later than **3 months** after the end of the financial year.

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

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

DISCLOSURE OF FINANCIAL INFORMATION (Cont'd)

Annual Report and Accounts (Cont'd)

Financial statements must include the disclosures required under the relevant accounting standards adopted as well as the information specified in Chapter 18 of the GEM Rules ("**Chapter 18**"), including a statement of profit or loss and other comprehensive income, a statement of financial position and information on the rates of dividend paid or proposed for each class of shares.

Annual financial statements must be prepared in accordance with Hong Kong or International Financial Reporting Standards or China Accounting Standards for Business Enterprises ("**CASBE**") in the case of a Chinese issuer that has adopted CASBE (GEM Rule 18.08).

DISCLOSURE OF FINANCIAL INFORMATION (Cont'd)

Half-year reports and accounts

- Listed companies are also required to prepare either half-year reports or summary half-year reports and must send them to the company's shareholders and holders of the company's listed securities within 45 days of the end of the first 6 months of each financial year.

- Half-year reports must be reviewed by the listed issuer's Audit Committee (Note 2 to GEM Rule 18.55(9).

DISCLOSURE OF FINANCIAL INFORMATION (Cont'd)

Quarterly Reporting

- Quarterly reporting is a mandatory obligation under GEM Rule 18.66.
- An issuer listed on the GEM must publish quarterly results and send them to the company's shareholders and holders of their listed securities within 45 days of the end of the first and third quarters.

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DISCLOSURE OF FINANCIAL INFORMATION (Cont'd)

Preliminary Announcements of Results

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

For Annual Results

- within 3 months of the financial year end.

For Half-year and Quarterly Results

- within 45 days of the relevant period.

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

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DISCLOSURE OF FINANCIAL INFORMATION (Cont'd)

Consequences of failure to publish financial information

For GEM issuers, the Listing Rules do not provide that the Exchange will require trading in a listed issuer's shares to be suspended if it fails to publish its financial information on time.

However, failure to publish financial information timely may be interpreted as a breach of the statutory obligation to disclose inside information under Part XIVA SFO.

FINANCIAL REPORTING FOR MINERAL COMPANIES

- Mineral Companies must include in their half-yearly and annual reports details of exploration, development and mining production activities and a summary of expenditure incurred during the relevant period (if there has been no such activities, this must be stated) (GEM Rule 18A.14)

- Note however that companies may be required to update shareholders immediately of material changes in funding requirements or exploration activity under the requirement to disclose inside information under Part XIVA SFO.

- Mineral companies must provide an annual update of their resources and/or reserves in annual reports (GEM Rule 18A.16). Updates must be prepared in accordance with the accepted reporting standard under which they were previously disclosed or, if none, in accordance with one of the recognised reporting standards. Annual updates need not be supported by a Competent Person's Report and may take the form of a no material change statement.

- Other (non-Mineral Company) listed issuers that publicly disclose details of resources and/or reserves are also required to provide annual updates of those resources/reserves in their annual reports.

- The Exchange has published guidance on the disclosures required in the annual and interim reports of Mineral Companies and other listed issuers which publicly disclose details of their resources and/or reserves. (HKEx-GL47-13)

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BOARD MEETINGS

- The board should meet regularly and board meetings should be held at least four times a year at approximately quarterly intervals (Code Provision A.1.1).

Notice to Exchange in certain circumstances

The issuer must inform the Exchange and publish an announcement on the websites of GEM and the issuer at least seven clear business days before the date of any board meeting to consider the declaration, recommendation or payment of a dividend or at which an announcement of the financial results for any period are to be approved (GEM Rule 17.48).

Voting at board meetings

Subject to certain exceptions, a director of a listed issuer may not vote on, nor be counted in the quorum for, any board resolution approving any contract or arrangement or any other proposal in which he or any of his close associates has a material interest (GEM Rule 17.48A).

BOARD MEETINGS (Cont'd)

Notice to Exchange after meetings

The issuer must inform the Exchange immediately of any decision:

a) to declare, recommend or pay a dividend or make any other distribution on its listed securities and the rate and amount thereof;

b) not to declare, recommend or pay a dividend which would otherwise have been expected;

c) on preliminary announcement of profits or losses for any period; and

d) on any proposed change in the capital structure, including a redemption of listed securities (GEM Rule 17.49).

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SHAREHLDER'S MEETINGS

Notice of general meetings

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

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

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

Notice of general meetings must be given to all shareholders whether or not their registered address is in Hong Kong (GEM Rule 17.46(1)).

An issuer must also ensure that notice of every general meeting is announced (GEM Rule 17.44).

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SHAREHOLDER'S MEETINGS (Cont'd)

Mandatory voting by poll on all resolutions at general meetings

- Voting by poll is mandatory on all resolutions at all general meetings (GEM Rule 17.47(4));
- Listed issuers must appoint a scrutineer (who may be the issuer's auditors or share registrar or external accountants who are qualified to serve as auditors) to oversee the voting procedures;
- The results of the poll must be announced by the issuer as soon as possible and no later than 30 minutes before the earlier of the commencement of the morning trading session or any pre-opening session on the business day following the general meeting;
- The chairman of a general meeting is required to ensure that the detailed procedures for conducting a poll are explained and to answer any questions that are raised (Code Provision E.2.1).

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SHAREHOLDER'S MEETINGS (Cont'd)

Interested shareholders required to abstain from voting

- Any shareholder that has a "material interest" in a transaction or arrangement to be approved at a general meeting of shareholders is required to abstain from voting on the resolution (GEM Rule 2.26).

- Factors relevant to determining whether a shareholder has a "material interest" include:

  - whether the shareholder is a party to the transaction or a close associate of such a party; and

  - whether the transaction confers upon the shareholder or his associate a benefit not otherwise available to other shareholders of the issuer (GEM Rule 2.27).

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PRE-EMPTION RIGHTS

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

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

- 20% of the number of the company's issued shares as at the date of the resolution granting the general mandate; and
- if separately authorised by the shareholders in general meeting, shares equivalent to the number of shares repurchased (up to 10% of the number of the company's issued shares as at the date of the resolution granting the repurchase mandate).

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

PRE-EMPTION RIGHTS (Cont'd)

The restrictions under GEM Rules 17.39 to 17.42B do not apply to *pro rata* offers made to all existing shareholders **excluding** those resident in a place outside Hong Kong if the directors consider such exclusion necessary or expedient due to legal restrictions or requirements of any relevant regulatory authority or stock exchange in the relevant place. Directors must make enquiry as to relevant restrictions.

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

The above restrictions apply equally to listed companies incorporated in Hong Kong and those incorporated overseas. They do not however apply to an overseas listed issuer whose primary listing is on another stock exchange which is not subject to any other statutory or other requirement giving shareholders pre-emptive rights to shareholders over further issues of shares.

RESTRICTIONS ON ISSUES OF SECURITES IN 6 MONTHS AFTER LISTING

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

i. The issue of shares, the listing of which has been approved by the Exchange, under a Ch. 23 share option scheme;

ii. The exercise of conversion rights attaching to warrants issued as part of the IPO;

iii. Any capitalisation issue, capital reduction or consolidation or sub-division of shares;

iv. The issue of shares or securities under an agreement entered into before the commencement of dealing, the material terms of which were disclosed in the IPO prospectus; and

RESTRICTIONS ON ISSUES OF SECURITIES IN 6 MONTHS AFTER LISTING (Cont'd)

v. The issue of any shares or securities convertible into equity securities which:

a) is for the purpose of acquiring assets that would complement the issuer's business;

b) does not result in any controlling shareholder ceasing to be a controlling shareholder or result in a change of control of the issuer;

c) is subject to approval from shareholders that do not have a material interest in the related transaction and are not connected persons (or their associates);

d) is set out in a circular that meets the requirements of Chapter 19 of the GEM Rules and contains sufficient information for independent shareholders to make an informed judgement on the issue and related transaction (GEM Rule 17.29).

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ISSUES OF SECURITIES FOR CASH

- An announcement containing the information required by GEM Rule 17.30 must be published on the next business day of the directors' decision to issue securities for cash.

- In the case of a placing of securities for cash, securities cannot be issued under the general mandate if the price is at a discount of 20% or more to the benchmarked price of the securities (i.e. the higher of the closing price on the date of the agreement and the average closing price for the 5 trading days immediately before the earlier of:

  i. the date of announcement of the transaction;

  ii. the date of the agreement; and

  iii. the date on which the price is fixed).

  An exception applies where the issuer can satisfy the Exchange that it is in a serious financial position and can only be saved by an urgent rescue operation involving the issue of new securities at a discount of 20% or more, or that other exceptional circumstances exist (GEM Rule 17.42B).

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ISSUES OF SECURITIES FOR CASH (Cont'd)

- Where securities are issued for cash under a general mandate at a discount of 20% or more, the company must publish an announcement giving details of the allottees no later than 30 minutes before the earler of the commencement of trading or any pre-opening session on the next business day after the agreement involving the proposed issue is signed (GEM Rule 17.30A).

- If there are less than ten allottees, the announcement must include the name of each allottee (or its beneficial owner) and confirmation of its independence from the issuer.

- If there are more than ten allottees, the name of each allottee (or its beneficial owner) subscribing 5% or more of the issued securities must be stated along with a general description of all other allottees together with confirmation of their independence from the issuer.

- In calculating the 5% limit, the number of securities subscribed by the allottee, its holding company and their subsidiaries must be aggregated.

NOTIFIABLE TRANSACTIONS

Chapter 19 of the GEM Listing Rules specifies certain transactions (principally acquisitions and disposals), particulars of which have to be disclosed to the shareholders, the Exchange and the general public. In some cases, shareholders' approval is also required. The term "listed issuer" means the listed issuer itself **or** its subsidiaries. Where a transaction is both "notifiable" and "connected", the issuer must comply with both Ch. 19 and Ch.20.

A transaction is widely defined and includes:

- an acquisition or disposal of assets, including a deemed disposal
- certain transactions in relation to options to acquire or dispose of assets or to subscribe for securities
- entering into or terminating finance leases where their financial effects have an impact on the listed issuer's balance sheet and/or profit and loss account
- entering into or terminating operating leases which, by virtue of their size, nature or number, have a significant impact on the listed issuer's operations
- granting an indemnity or a guarantee or providing financial assistance other than to the listed issuer's subsidiaries
- any arrangement or agreement involving the formation of a joint venture entity in any form

The definition excludes (to the extent not specifically referred to above) transactions of a revenue nature in the ordinary and usual course of business and also the issue of new securities for cash (but these are within the definition of transaction which applies for connected transactions under Ch.20).

NOTIFIABLE TRANSACTIONS (Cont'd)

Transactions of a "Revenue Nature"

- Relevant non-exhaustive factors include:
  - whether previous transactions of same nature treated as notifiable transactions
  - historical accounting treatment of previous transactions of same nature
  - whether accounting treatment is in accordance with generally accepted accounting standards
  - whether transaction is a revenue or capital transaction for tax purposes (Note 4 of GEM Rule 19.04(1)(g))
- Transactions involving the acquisition and disposal of properties are generally not considered to be of a revenue nature unless carried out as one of the principal activities and in the ordinary and usual course of business of the listed issuer (Note 2 to GEM Rule 19.04(1)(g))

Transactions in the "Ordinary and Usual Course of Business"

- "Ordinary and usual course of business" = the existing principal activities of the listed issuer or an activity wholly necessary for its principal activities. Financial assistance is only provided "in the ordinary and usual course of business" of (i) a "banking company" (i.e. an authorized financial institution under the Banking Ordinance) or (ii) a licensed securities house providing financial assistance on normal commercial terms for a purpose specified in GEM Rule 19.04(1)(e)(iii) (GEM Rule 19.04(8))

NOTIFIABLE TRANSACTIONS (Cont'd)

Classification of Notifiable Transactions

Notifiable transactions are classified using the percentage ratios calculations set out in GEM Rule 19.06.

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

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

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NOTIFIABLE TRANSACTIONS (Cont'd)

Chapter 19 sets out six categories of notifiable transactions:

1. A ***share transaction*** is an acquisition of assets (excluding cash) by a listed issuer where the consideration includes securities for which listing will be sought and where all percentage ratios are less than 5%;

2. A ***discloseable transaction*** is a transaction or a series of transactions by a listed issuer where any percentage ratio is 5% or more, but less than 25%;

3. A ***major transaction*** is a transaction or a series of transactions by a listed issuer where any percentage ratio is 25% or more, but less than 100% for an acquisition or 75% for a disposal;

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NOTIFIABLE TRANSACTIONS (Cont'd)

4. A ***very substantial disposal*** is a disposal or a series of disposals of assets by a listed issuer where any percentage ratio is 75% or more;

5. A ***very substantial acquisition*** is an acquisition or a series of acquisitions of assets by a listed issuer where any percentage ratio is 100% or more; and

6. A ***reverse takeover*** is "**an acquisition or a series of acquisitions** which, in the opinion of the Exchange, constitutes, or is part of a transaction or arrangement or series of transactions or arrangements which **constitute, an attempt to achieve a listing of the assets to be acquired and a means to circumvent the requirements for new applicants** set out in Chapter 11 of the GEM Listing Rules and normally refers to:

   (a) an acquisition/series of acquisitions of assets **constituting a very substantial acquisition** where there is or which will result in a **change in control** (i.e. 30% or more of the voting rights) of the listed issuer; or

   (b) an acquisition/series of acquisitions of assets **from the incoming controlling shareholder(s) or his/their associates within 24 months after the change in control** that had not been regarded as a reverse takeover, which individually or together **reach the threshold for a very substantial acquisition**.

NOTIFIABLE TRANSACTIONS (Cont'd)

❖ ***Reverse Takeovers (Cont'd)***

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

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

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

is used as the denominator of the percentage ratios (GEM Rule 19.06(6)(b))

NOTIFIABLE TRANSACTIONS (Cont'd)

Percentage Ratios

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

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

Total assets = current assets + non-current assets + fixed assets + intangible assets **(GEM Rule 19.04(12))**

Intangible assets include goodwill (whether positive or negative)

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

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

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

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

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NOTIFIABLE TRANSACTIONS (Cont'd)

(iv) Consideration ratio = Fair value of the consideration*

Total market capitalization of listed issuer**

*Determined at the date of the agreement according to Hong Kong Financial Reporting Standards or International Financial Reporting Standards (**GEM Rule 19.15(1)**)

Total market capitalization = average closing price of the listed issuer's securities for the 5 business days preceding the transaction (GEM Rule 19.07(4)**)

(v) Equity capital ratio = Number of shares to be issued by the listed issuer as consideration

Total number of the listed issuer's issued shares immediately before the transaction

When calculating the equity capital ratio, the numerator includes shares that may be issued upon conversion or exercise of any convertible securities or subscription rights to be issued or granted as consideration. Also, the listed issuer's debt capital (if any), including any preference shares, is not included in the calculation.

Exception

- If any size test produces an anomalous result or is inappropriate to the issuer's sphere of activity, HKEx may substitute other relevant size indicators or industry specific tests (GEM Rule 19.20).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Classification of Transactions

Transactions involving acquisition and disposal

- Where a transaction involves both an acquisition and a disposal, the Exchange will apply the percentage ratios to both the acquisition and the disposal. The transaction will be classified based on the larger of the acquisition or disposal, and subject to the requirements applicable to that classification.

- Where a shareholders' circular is required, each of the acquisition and disposal will be subject to the content requirements applicable to their respective transaction classification (GEM Rule 19.24).

NOTIFIABLE TRANSACTIONS (Cont'd)

Aggregation of transactions

The Exchange may require listed issuers to aggregate a series of transactions and treat them as if they were one transaction if they are all completed within a 12 month period or are otherwise related (GEM Rule 19.22)

Factors which the Exchange will take into account in determining whether transactions will be aggregated include whether the transactions:

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

❖ Aggregation is not automatic only because one factor is triggered. The Exchange will also consider whether the aggregation would result in a higher transaction classification.

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NOTIFIABLE TRANSACTIONS (Cont'd)

Aggregation of transactions (Cont'd)

With regards to the aggregation of transactions, the Exchange should be consulted at an early stage:

- in cases of doubt;
- if any of the factors above apply to any transaction entered into by the listed issuer in the preceding 12-month period; or
- if any transaction entered into by the listed issuer involves acquisitions of assets from a person or group of persons or any of his/their associates within 24 months of such person or group of persons gaining control of the listed issuer (other than at the subsidiary level).

The Exchange may aggregate transactions regardless of whether it was consulted by the listed issuer.

NOTIFIABLE TRANSACTIONS (Cont'd)

Requirements: Summary of requirements for different categories of notifiable transactions

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

Notes:
1. Shareholder approval is not required if the consideration shares are issued under a general mandate.
2. Any shareholder and his associates must abstain from voting if such shareholder has a material interest in the transaction.
3. For acquisitions of businesses and/or companies only. The accountants' report is for the 3 preceding years.
4. An accountants' report for the preceding 3 financial years is required.
5. An accountants' report on may be provided instead of a review by the listed issuer's auditors or reporting accountants.
6. Approval of the Exchange is also necessary.

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NOTIFIABLE TRANSACTIONS (Cont'd)

Announcement

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

- inform the Exchange; and
- publish an announcement on the GEM website and issuer's own website (GEM Rule 19.34)

Trading halt and short suspension of dealings

- Where a listed issuer has signed an agreement for a notifiable transaction and an announcement has not been published on a business day, the issuer must request a trading halt or a short suspension of dealings pending publication of the announcement.
- Where a listed issuer has signed an agreement for a notifiable transaction which it reasonably believes would require disclosure as inside information under Part XIVA SFO, the issuer must immediately request a trading halt or a short suspension of dealings pending publication of an announcement. Once an issuer has finalised the major terms of a notifiable transaction which it reasonably believes would require disclosure as inside information, it must ensure confidentiality of relevant information until publication of an announcement (GEM Rule 19.37(3)).

NOTIFIABLE TRANSACTIONS (Cont'd)

Announcement contents: general requirements

GEM Rule 19.58 requires all notifiable transaction announcements to include:

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

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for share transaction announcements

Announcements of Share Transactions must include the following additional information:

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

(GEM Rule 19.59)

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for announcements of notifiable transactions (other than share transactions)

All other announcements must include the additional information required by GEM Rule 19.60:

i. the general nature of the transaction including, if securities are involved, details of any restrictions applicable to subsequent sale of the securities;

ii. brief details of the assets being acquired or disposed of, including the name of the company/business or assets/properties and if the assets include securities, the name and general activities of the company in which the securities are held;

iii. in the case of a disposal:

- details of the gain or loss expected and the basis of its calculation (the gain or loss should be calculated by reference to the carrying value of the assets); and
- the intended application of the sale proceeds;

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for announcements of notifiable transactions (other than share transactions) (Cont'd)

iv. announcements for transactions that involve an issue of securities for which listing is sought must include:

- a statement that the announcement appears for information purposes only and does not constitute an invitation or offer to acquire, purchase or subscribe for the securities; and
- a statement that application has been or will be made to the Exchange for the listing of and permission to deal in the securities;

v. for a major transaction approved or to be approved by written shareholders' approval of a shareholder or a closely allied group of shareholders, the name of the shareholder(s), the number of securities held by each and the relationship between the shareholders;

vi. (except for discloseable transactions) the expected date of despatch of the circular to shareholders and, if this is more than 15 days after the announcement date, the reasons why this is so;

vii. if the transaction involves the disposal of an interest in a subsidiary, a declaration as to whether the subsidiary will continue to be a subsidiary after the transaction; and

viii. the expected date of despatch of the circular, and if this is more than 15 business days after publication of the announcement, the reasons why this is so.

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NOTIFIABLE TRANSACTIONS (Cont'd)

Pre-vetting requirements

- Generally, announcements for notifiable transactions do not need to be pre-vetted before publication;
- However, pursuant to the transitional provisions of GEM Rule 17.53(2) (which will cease to take effect on a date to be determined by the Exchange), announcements for any very substantial disposal, very substantial acquisition or reverse takeover must be pre-vetted.

Requirements for further announcements

Where a previously announced notifiable transaction is terminated or there is any material variation of its terms or material delay in the completion of the agreement, the listed issuer must as soon as practicable announce this fact by means of an announcement (GEM Rule 19.36).

NOTIFIABLE TRANSACTIONS (Cont'd)

Shareholders' approval requirements

Major Transactions, Very Substantial Disposals, Very Substantial Acquisitions and Reverse Takeovers must be made conditional on approval by shareholders in general meeting (GEM Rule 19.40)

Voting at general meetings on notifiable transactions

- All voting at general meetings must be taken by poll (GEM Rule 17.47(4)) and the results of the poll must be announced on the next business day following the meeting. The issuer must appoint its auditor, share registrar or external accountants to act as scrutineer for the vote taking.

- Any shareholder that has a material interest in the transaction must abstain from voting. Factors relevant to determining whether a shareholder has a "material interest" include:

  - whether the shareholder is a party to the transaction or a close associate of such a party;

  - whether the transaction confers upon the shareholder or his associate a benefit not available to other shareholders of the issuer (GEM Rule 2.27).

- On a reverse takeover where there is a change in control and an existing controlling shareholder will dispose of shares to any person, the existing controlling shareholder and his associates cannot vote in favour of the acquisition of assets from the incoming controlling shareholder or his associates at the time of the change in control.

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NOTIFIABLE TRANSACTIONS (Cont'd)

Shareholders' approval requirements (Cont'd)

Written shareholders' approval

Under GEM Rule 19.44, major transactions may be approved by written shareholders' approval in lieu of holding a general meeting only if:

- no shareholder would be required to abstain from voting if the listed issuer were to convene a general meeting for the approval of the transaction;
- the written shareholders' approval has been obtained from a shareholder or *closely allied group of shareholders* (as defined in GEM Rule 19.45) who together hold more than 50% of the voting rights at the general meeting to approve the transaction; and
- the reporting accountants do not give a qualified opinion in their accountants' report (GEM Rule 19.86).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Circular to Shareholders

GEM Rule 19.63 requires that a circular for a major transaction, very substantial disposal or very substantial acquisition and a listing document for a reverse takeover sent by a listed issuer to holders of its listed securities must:

i. provide a clear, concise and adequate explanation of its subject matter;

ii. if voting or shareholders' approval is required:

   a) contain all information necessary to allow the holders of the securities to make a properly informed decision;
   b) contain a heading emphasising the importance of the document and advising holders of securities, who are in any doubt as to what action to take, to consult appropriate independent advisers;
   c) contain a recommendation from the directors as to the voting action that shareholders should take, indicating whether or not the proposed transaction described in the circular is, in the opinion of the directors, fair and reasonable and in the interests of the shareholders as a whole; and
   d) contain a statement that any shareholder with a material interest in a proposed transaction and his close associates will abstain from voting on resolution(s) approving that transaction; and

iii. contain a confirmation that, to the best of the directors' knowledge, information and belief having made all reasonable enquiry, the counterparty and the ultimate beneficial owner of the counterparty are third parties independent of the listed issuer and connected persons of the listed issuer.

NOTIFIABLE TRANSACTIONS (Cont'd)

Circular to Shareholders (Cont'd)

The circular must be sent to shareholders:

- in the case of a major transaction to be approved by written shareholders' approval – within 15 business days after publication of the announcement (GEM Rule 19.41(a)); and

- for major transactions to be approved in general meeting, very substantial acquisitions and very substantial disposals, at the same time as or before the listed issuer gives notice of the general meeting to approve the transaction (GEM Rules 19.41(b) and 19.51).

The listed issuer must also despatch to its shareholders any revised or supplementary circular and/or provide any material information that has come to the attention of the directors after the issue of the circular (by way of announcement) on the transaction to be considered at a general meeting not less than 10 business days before the date of the relevant general meeting (GEM Rules 19.42 and 19.52).

The Listing Rules set out additional requirements for shareholders' circulars involving an acquisition or disposal of any business, company or companies or revenue-generating assets with an identifiable income stream or asset valuation.

Depending on the type of transaction, the listed issuer may be required to include in the circular an accountants' report, profit/loss statement or pro forma financial statement.

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for major transactions involving an acquisition of business or companies

The issuer is also required to include the following in a shareholders' circular in relation to a notifiable transaction which involves an acquisition of a business or one or more companies:

- an accountants' report on the business or company(ies) being acquired (although the Exchange may relax this requirement if the company will not become a subsidiary of the issuer);
- a pro forma statement of the assets and liabilities of the listed issuer's group combined with those of the business or company(ies) being acquired on the same accounting basis (GEM Rule 19.67(6)); and
- a discussion and analysis of the results of the business or company(ies) being acquired (GEM Rule 19.67(7)).

NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for major transactions involving an acquisition of any revenue generating assets (other than a business or company)

The additional requirements for a shareholders' circular in relation to a notifiable transaction which involves an acquisition of any revenue generating assets (other than a business or company) with an identifiable income stream include:

- a profit and loss statement and valuation for the 3 preceding financial years (or less if the asset has been held by the vendor for a shorter period) on the identifiable net income stream and valuation in relation to such assets, reviewed by the auditors or reporting accountants;

- a pro forma statement of the assets and liabilities of the listed issuer's group combined with the assets being acquired on the same accounting basis (GEM Rule 19.67(6)(b)); and

- a discussion and analysis of the results of the business or company(ies) being acquired (GEM Rule 19.67(7)).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for very substantial acquisitions (VSA) and reverse takeovers (RTO) involving an acquisition of any business or companies

The additional requirements for a VSA or RTO circular in relation to an acquisition of a business or one or more companies include:

- an accountants' report on the business or company(ies) being acquired;
- a pro forma income statement, balance sheet and cash flow statement of the enlarged group on the same accounting basis; and
- in relation to a VSA, a separate discussion and analysis of the performance of each of the group and any business or company(ies) being acquired or to be acquired for the period referred to in GEM Rule 7.05(1)(a) (GEM Rule 19.69(8)).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for very substantial acquisitions (VSA) and reverse takeovers (RTO) involving an acquisition of any revenue generating assets

The additional requirements for a circular to shareholders for a VSA or RTO relating to an acquisition of any revenue generating assets (other than a business or company) with an identifiable income stream or assets valuation include:

- a profit and loss statement and valuation for the 3 preceding financial years (or less if, other than in the case of an RTO, the asset has been held by the vendor for a shorter period) on the identifiable net income stream and asset valuation, reviewed by the auditors or reporting accountants;

- a pro forma profit and loss statement and net assets statement on the enlarged group on the same accounting basis (GEM Rule 19.69(4)(b)); and

- in relation to a VSA, a separate discussion and analysis of the performance of each of the group and any business or company acquired for the period referred to in GEM Rule 7.05(1)(a) (GEM Rule 19.69(8)).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for very substantial disposals (VSDs) involving a disposal of any business or companies

The additional requirements for a VSD circular involving a business or company being disposed of include:

- financial information on either: (a) the business or company(ies) being disposed of; or (b) the issuer's group with the business or company(ies) being disposed of shown separately as a disposal group(s) or a discontinuing operation(s) for the relevant period described in GEM Rule 7.05(1)(a);

- the financial information must include at least the income statement, balance sheet, cash flow statement and statement of changes in equity and must be reviewed by the issuer's auditors or reporting accountants; and

- a pro forma income statement, balance sheet and cash flow statement of the remaining group on the same accounting basis (GEM Rule 19.68(2)(a)).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for very substantial disposals (VSDs) involving a disposal of revenue-generating assets (other than a business or companies)

The additional requirements for a VSD circular in relation to a disposal of revenue generating assets (other than a business or company) with an identifiable income stream or assets valuation include:

- a profit and loss statement and valuation for the 3 preceding financial years (or less where the asset has been held by the issuer for a shorter period) on the identifiable net income stream and valuation in relation to such assets which must be reviewed by the auditors or reporting accountants; and

- a pro forma profit and loss statement and net assets statement on the remaining group on the same accounting basis.

NOTIFIABLE TRANSACTIONS (Cont'd)

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

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

Source: the Hong Kong Stock Exchange

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NOTIFIABLE TRANSACTIONS (Cont'd)

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

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

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NOTIFIABLE TRANSACTIONS (Cont'd)

Requirements for reverse takeovers (RTO)

- Exchange will treat an issuer proposing an RTO as a new listing applicant (GEM Rule 19.54)
- Enlarged group or assets to be acquired must be able to meet the financial tests in GEM Rule 11.12A and all other basic listing requirements
- Listed issuer must issue a prospectus and pay an initial listing fee
- The Definition of RTO
  - an acquisition or series of acquisitions by a listed issuer which, in the opinion of the Exchange, constitutes, or is part of a transaction or arrangement or series of transactions or arrangements which constitute, an attempt to achieve a listing of the assets to be acquired and a means to circumvent the requirements for new listing applicants (the "**Principle Based Test**")

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NOTIFIABLE TRANSACTIONS (Cont'd)

Requirements for reverse takeovers (RTO) (Cont'd)

- The Bright Line Tests applicable to two specific forms of RTO

  a. an acquisition or a series of acquisitions of by a listed issuer which **constitute a very substantial acquisition ("VSA")** where there is, or which will result in, a **change of control** (i.e. 30%) of the listed issuer (other than at the level of its subsidiaries); or

  b. an acquisition or a series of acquisitions of assets by a listed issuer which **constitute a VSA** from a person or group (or their associates) under any agreement or arrangement entered into by the listed issuer within **24 months** of that person or group gaining **control** of the listed issuer (where the original transaction did not constitute an RTO). In determining whether one or more transactions constitute a VSA, the denominator in the percentage ratio calculation is measured at the time of the change of control or the acquisition(s), whichever produces the lower figure.

- To fall within the Bright Line Tests, there must be a change in control of the listed issuer and a VSA by the incoming controlling shareholder at the time of the change in control or within the following 24 months. A VSA which is within the Bright Line Tests will be a reverse takeover and the listed issuer proposing the VSA will be treated as a new listing applicant.

- If a VSA falls outside the Bright Line Tests, the Exchange will apply the Principle Based Test to assess whether the acquisition(s) are an attempt to list the assets acquired and circumvent the new listing requirements).

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NOTIFIABLE TRANSACTIONS (Cont'd)

Listing Committee Report 2010: The Application Of The RTO Rules To "Extreme Cases"

- Where there is no change in control, the Exchange will treat a VSA which attempts to list the assets acquired and circumvent the new listing requirements as an RTO only if it considers the VSA to be an "**extreme case**".

If it is, the Exchange will treat the listed issuer proposing the RTO as a new listing applicant.

- In determining whether a VSA is an extreme case, the Exchange takes the following factors into account:
  - the size of the acquisition relative to the size of the issuer;
  - the quality of the acquired business – whether it can meet the trading record requirements for new listings, or whether it is unsuitable for listing (e.g. an early stage exploration mining company);
  - the nature and scale of the issuer's business before the acquisition (a key question is whether it is a listed shell);
  - any fundamental alteration to the issuer's principal business (e.g. the existing business would be discontinued or very immaterial to the enlarged group's operations post acquisition);
  - any other events and transactions, whether they be historical, proposed or intended, which, when considered alongside the acquisition, constitute a sequence of arrangements designed to circumvent the RTO Rules (e.g. a disposal of the issuer's original business simultaneous with a very substantial acquisition); and

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NOTIFIABLE TRANSACTIONS (Cont'd)

- In determining whether a VSA is an extreme case, the Exchange takes the following factors into account (cont'd):
  - any issue to the vendor of Restricted Convertible Securities which would provide it with de facto control of the issuer. Restricted Convertible Securities are highly dilutive convertible securities with a conversion restriction mechanism (e.g. restriction from conversion that would cause the securities holder to hold 30% interest or higher) which avoids triggering a change of control under the Code on Takeovers and Mergers.
- Non-extreme VSAs
  - The Exchange will not apply the RTO Rules to a VSA within the principle based test which it does not consider to be extreme. The Exchange may nevertheless require the issuer to prepare a transaction circular under an enhanced disclosure and vetting approach.

NOTIFIABLE TRANSACTIONS (Cont'd)

Extreme VSAs

- Where the Exchange considers a VSA to be extreme, but the acquired assets or enlarged group are unable to meet the requirements for new listing, the RTO Rules will be applied and the transaction will not be able to proceed.
- The Exchange's Guidance Letter HKEx-GL78-14 describes "extreme VSAs" as VSAs which are considered extreme, but the acquired assets meet the minimum profit requirement under Rule 8.05 and circumvention of the requirements for new listings is not a material concern.
- The Exchange refers extreme VSAs to the Listing Committee for its decision.
- Where the Listing Committee determines that the RTO Rules will apply, the issuer will be treated as a new listing applicant and will be subject to the requirements applicable to new listing applicants.
- Where the Listing Committee determines that the RTO Rules will not apply to an extreme VSA, the issuer will be required to:

  a) prepare a transaction circular under an enhanced disclosure and vetting approach;

  b) appoint a financial adviser to conduct due diligence on the acquisition.
- In cases involving the acquisition of new businesses or assets, enhanced disclosure is likely to be of limited use, as the business or assets in question will have little in the way of operating history or track record. Such cases are therefore more likely to be regarded as new listings.

NOTIFIABLE TRANSACTIONS (Cont'd)

Reverse takeovers and the restriction on disposals after a change of control

- The Listing Rules prohibit a listed issuer from disposing of its existing business within 24 months after a change in control unless assets acquired by the listed issuer after the change in control can meet the trading record requirement of GEM Rule 11.12A. If not, on a disposal by a listed issuer of its existing business within 24 months of a change in control, the issuer will be treated as a new listing applicant.
- In its 2008 and 2009 reports, the Listing Committee clarified that the aim of GEM Rules 19.91 and 19.92 was to prevent circumvention of the reverse takeover rules by a new controlling shareholder deferring the sale of an existing business until after the asset injection, thereby avoiding classification as a VSA.
- A waiver of GEM Rule 19.91 can therefore be sought for a legitimate sale of an existing business within 24 months of a change of control provided that:
  a. the incoming controlling shareholder has not injected assets into the listed issuer; or
  b. after factoring in the disposal(s) of the issuer's existing business, the asset injection(s) before and after the change in control would not have constituted a VSA.

(See Listing Committee's Annual Reports of 2008 and 2009 and Listing Decision HKEx-LD7-2011)

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NOTIFIABLE TRANSACTIONS (Cont'd)

Additional requirements for transactions involving mineral assets

A Mineral Company which proposes to acquire or dispose of assets which are solely or mainly mineral or petroleum assets as part of a major transaction (i.e. 25% or more of existing activities) or above (a **Relevant Notifiable Transaction**) must:

- comply with the requirements for notifiable transactions of GEM Chapter 19 and, if relevant, the requirements for connected transactions of GEM Chapter 20;
- prepare a Competent Person's Report, which must form part of the circular to shareholders, on the resources and/or reserves being acquired or disposed of as part of the Relevant Notifiable Transaction;
- in the case of a major (or above) acquisition, produce a Valuation Report, which must form part of the circular to shareholders, on the mineral or petroleum assets being acquired;
- ensure that the Valuation Report must be prepared by a Competent Evaluator being someone who:
  - (a) meets the independence test under GEM Rule 18A.22;
  - (b) has at least 10 years' relevant and recent general mining/petroleum experience;
  - (c) has at least 5 years' relevant and recent experience in the assessment and/or valuation of mineral or petroleum assets; and
  - (d) has all necessary licences.

Other listed issuers (i.e. non-Mineral Companies) that propose to acquire assets which are solely or mainly mineral or petroleum assets as part of a Relevant Notifiable Transaction must also comply with the above requirements. On completion of the transaction, the listed issuer will be treated as a Mineral Company, unless the Exchange decides otherwise

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NOTIFIABLE TRANSACTIONS (Cont'd)

Pre-vetting requirements

GEM Rule 17.53(1) requires that circulars or listing documents in respect of notifiable transactions must be pre-vetted (that is, reviewed and approved by the Exchange) before publication, including listing documents and prospectuses (e.g. for notifiable transactions, such as reverse takeovers, that are treated as new listings).

CONNECTED TRANSACTIONS

Introduction

- Generally, a connected transaction is any transaction between a listed **issuer** or any of its **subsidiaries** and a connected person;
- For classification **purposes, the Exchange may aggregate a series of transactions that are completed over a 12-month period** or are otherwise related;
- Factors which the Exchange takes into account in determining whether connected transactions should be aggregated are whether they:
  1. are entered into by the listed issuer with the same party or parties connected/associated with one another;
  2. involve the acquisition or disposal of securities or an interest in one particular company or group of companies;
  3. involve the acquisition or disposal of parts of one asset; or
  4. together lead to substantial involvement by the listed issuer in a business activity not previously part of its principal business activities.

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CONNECTED TRANSACTIONS (Cont'd)

Definitions – " Transaction"

The term "transaction" for the purposes of the connected transaction requirements includes the following:

a. the acquisition or disposal of assets (including deemed deposits set out in GEM Rules 19.29;

b. any transaction involving an option to acquire or dispose of assets or to subscribe for securities;

c. entering into or terminating finance or operating leases;

d. granting an indemnity or providing or receiving financial assistance;

e. entering into a joint venture;

f. issuing new securities of the issuer or its subsidiaries;

g. provision or receipt of services;

h. sharing of services ;

i. providing or acquiring raw materials, intermediate products and finished goods; and

j. a qualified property acquisition.

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CONNECTED TRANSACTIONS (Cont'd)

Definitions – "Connected Persons"

"**Connected persons**" are defined to include:

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

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

i. 10% under the percentage ratios for each of the three preceding financial years; or

ii. 5% under the percentage ratios for the latest financial year;

b) a **person who was a director** of the listed issuer or any of its subsidiaries in the past 12 months, or an **associate** of such a person; or

c) a **connected subsidiary**.

A **"connected subsidiary"** is a non-wholly owned subsidiary of the listed issuer where any connected person(s) of the listed issuer (other than at the level of its subsidiaries) are entitled to exercise, or control the exercise of, 10% or more of the voting power at general meetings of the non-wholly owned subsidiary or a subsidiary of such a non-wholly owned subsidiary. This excludes an indirect interest in the subsidiary which is held by the connected person(s) through the listed issuer (GEM Rule 20.14).

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

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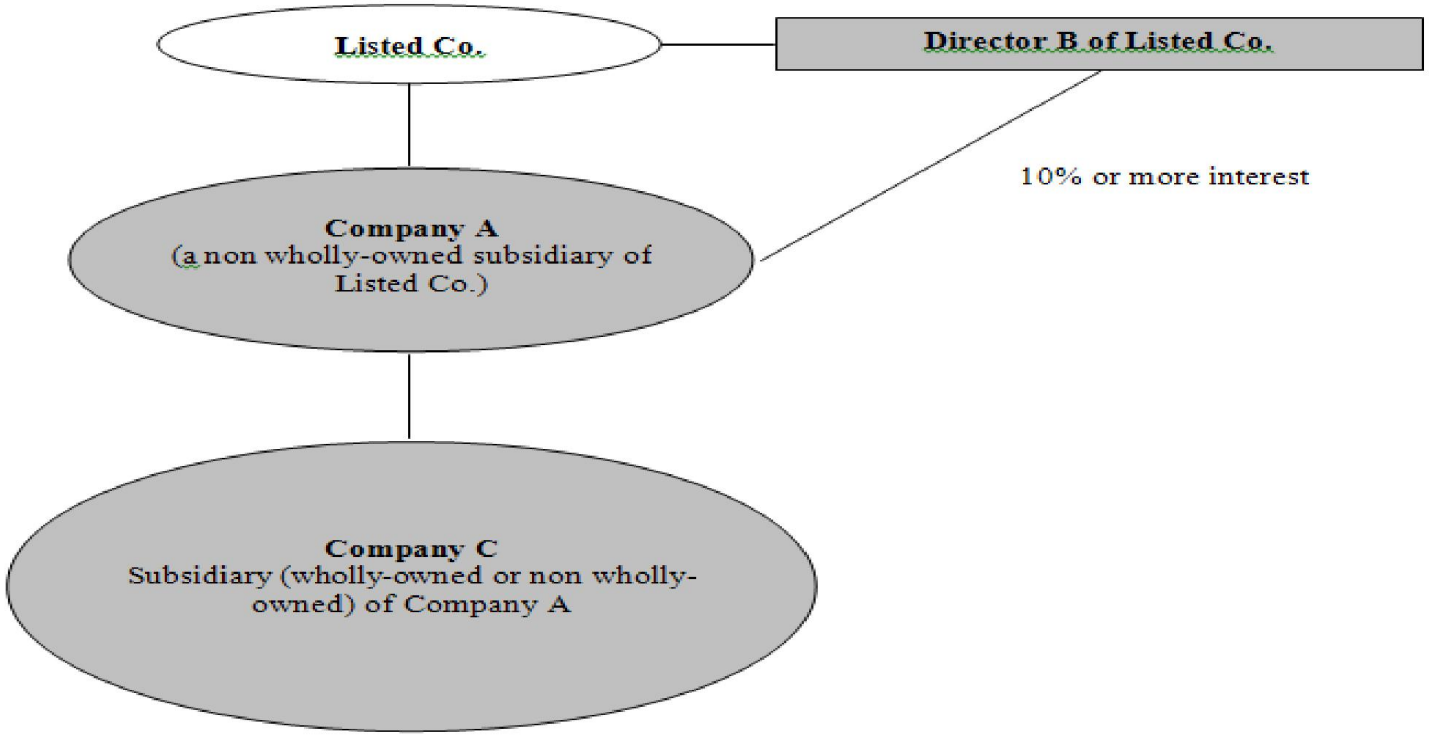
CONNECTED TRANSACTIONS (Cont'd)

Definitions – "Connected Persons" (Cont'd)



Company A and Company C are connected persons of the listed company as Company A is a non-wholly owned subsidiary in which a connected person at the issuer level (Director B) holds 10% of the shares. Company C as its subsidiary is also connected.

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CONNECTED TRANSACTIONS (Cont'd)

Definitions – "Associates of an Individual"

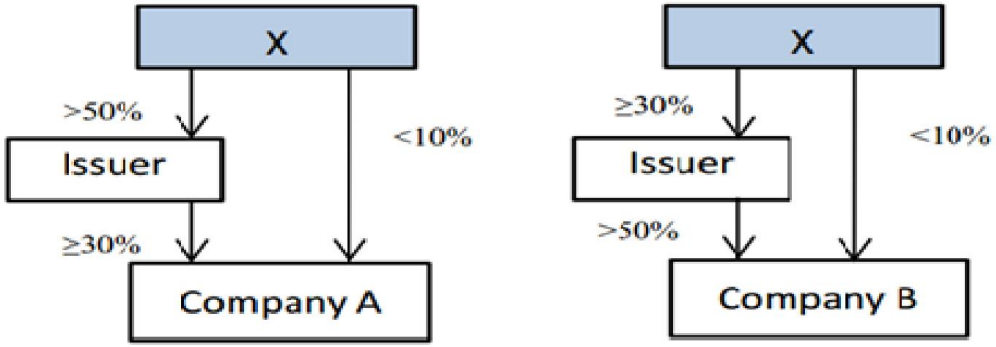
The **associates** of a connected person who is an **individual** include:

a) his spouse, his (or his spouse's) child (natural or adopted) or step-child under the age of 18 years (each an "**immediate family member**");

b) the trustees, acting in their capacity as trustee of any trust of which the **individual** or his **immediate family member** is a beneficiary or, in the case of a discretionary trust, is (to his knowledge) a discretionary object (the "**trustees**");

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

- A company is not an associate of an individual if the interests of the connected person and his associates in the entity are together less than 10%. (GEM Rule 20.12)



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CONNECTED TRANSACTIONS (Cont'd)

Definitions – "Associates of an Individual" (Cont'd)

The **associates** of a connected person who is an **individual** include:

d) a person cohabiting with him as a spouse, or his child, step-child, parent, step-parent, sibling or step-sibling (each a "**family member**");

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

Definitions – "Associates of an Individual" (Cont'd)

The **associates** of a connected person who is an **individual** include:

f) a parent-in-law, brother-in-law, sister-in-law, son-in-law, daughter-in-law, grandparent, grandchild, uncle, aunt, nephew, niece or cousin of the connected person (each a "relative") whose association with the **connected person** is such that, in the opinion of the Exchange, the proposed transaction should be subject to the connected transaction requirements; and

g) a company in which the **relatives** (individually or together) or the relatives together with the connected person, the trustees, his immediate family members and/or family members control the exercise of **50%** or more of the voting power or control the composition of a majority of the board of directors, and any of its **subsidiaries**, whose association with the **connected person** is such that, in the opinion of the Exchange, the proposed transaction should be subject to the connected transaction requirements.

CONNECTED TRANSACTIONS (Cont'd)

Definitions – "Associates of a company"

The **associates** of a connected person who is a **company** include:

a) its **subsidiary** or **holding company**, or **fellow subsidiary** of such a holding company (together, the "**group companies**");

b) the trustees of any trust of which the company is a beneficiary or, to the company's knowledge, discretionary object (the "**trustees**");

c) a company in which the company, the group companies and/or the trustees (individually or together), can:

   i. exercise or control the exercise of 30% or more of the voting power at general meetings; or

   ii. control the composition of a majority of the board of directors; and

d) a subsidiary of a company in (c).

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CONNECTED TRANSACTIONS (Cont'd)

Deemed connected persons

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

a) Has entered, or proposes to enter into:

   i. a transaction with the group; and

   ii. an agreement, arrangement, understanding or undertaking (whether formal or informal and whether express or implied) with respect to the transaction with a director, chief executive or substantial shareholder of the issuer or any of its subsidiaries or person who was a director within the previous 12 months; and

b) should, in the Exchange's opinion, be considered as a connected person.

CONNECTED TRANSACTIONS (Cont'd)

Connected transactions where there is no transaction with a connected person

Acquisition of interest in a company

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

a) is (or is proposed to be) a **controller** (i.e. a director, chief executive or controlling shareholder of the listed issuer); or

b) is, or will as a result of the transaction, become, an associate of a controller or proposed controller of the listed issuer.

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

The Exchange may aggregate the interests of the controller and his/its associates in the target company to determine if they are together the target company's substantial shareholder. Rule 20.26 does not apply to a listed issuer's acquisition if the controller or his/its associates are together a substantial shareholder of the target only because of their indirect shareholdings in the target company held through the listed issuer's group.

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CONNECTED TRANSACTIONS (Cont'd)

Financial assistance

Financial assistance includes granting credit, lending money, or providing an indemnity against obligations under a loan, or providing security for, or guaranteeing a loan.

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

a) a connected person; or

b) a Commonly Held Entity

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

a) a connected person; or

b) a Commonly Held Entity.

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CONNECTED TRANSACTIONS (Cont'd)

Financial assistance (Cont'd)

Financial assistance must comply with the Connected Transaction Rules if it involves:

a) Financial Assistance for the Benefit of Connected Interests – i.e. the listed issuer or its subsidiaries providing an indemnity, guarantee or other financial assistance to and/or for the benefit of a connected person or Commonly Held Entity; or

b) Granting Security to Connected Interests – i.e. the listed issuer or its subsidiaries grant security over the group's assets for financial assistance provided by a connected person or a Commonly Held Entity to the listed issuer or its subsidiaries.

CONNECTED TRANSACTIONS (Cont'd)

Financial assistance (Cont'd)

The term "Commonly Held Entity " refers to a company whose shareholders include:

a) a member of the listed issuer's group; and

b) a connected person(s) at the issuer level who, individually or together, can exercise or control the exercise of 10% or more of the voting power at the company's general meeting (GEM Rules 20.24 and 20.25).

CONNECTED TRANSACTIONS (Cont'd)

Options involving Connected Persons

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

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

Options granted by listed group to a connected person

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

- on grant of the option to a connected person, the transaction is classified as if the option had been exercised. The percentage ratios are calculated based on the consideration for the transaction (which is taken to include the premium and the exercise price), the value of the underlying assets, and the revenue attributable to the assets;

- the issuer must announce:
  i. any exercise or transfer of the option by the option holder; and/or
  ii. if the option is not exercised in full, the option holder notifying the listed issuer's group that it will not exercise the option, or the expiry of the option, whichever is the earlier (GEM Rule 20.77).

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CONNECTED TRANSACTIONS (Cont'd)

Options acquired by listed group from a connected person

If the listed issuer's group acquires or accepts an option granted by a connected person where the option is exerciseable at the discretion of the listed group:

- on acquisition by, or grant of the option to, the group, only the premium is taken for the purpose of calculating the percentage ratios. However, if the premium represents 10% or more of the sum of the premium and the exercise price, the percentage ratios are calculated based on the premium, the exercise price, the value of the underlying assets and the revenue attributable to such assets;

- on exercise of the option by the group, the exercise price, value of the underlying assets and the revenue attributable to such assets are used for the purpose of calculating the percentage ratios; and

- non-exercise of the option or transfer of the option to a third party are treated as if the option was exercised. The exercise price, value of the underlying assets, the revenue attributable to such assets and (if applicable) the premium for transferring the option are used for the purpose of calculating the percentage ratios;

CONNECTED TRANSACTIONS (Cont'd)

Options acquired by listed group from a connected person (Cont'd)

- if the listed group transfers the option to a third party, terminates the option or decides not to exercise the option:

  - the transaction is classified as if the option was exercised. The exercise price, value of the underlying assets, the revenue attributable to such assets and (if applicable) the consideration for transferring the option, or the amount receivable or payable by the listed group for terminating the option are used for the purpose of the percentage ratios; or

  - the Exchange may allow the listed issuer to classify the transaction using the asset and consideration ratios based on the **higher** of:

    1) the exercise price less the value of the assets subject to the option (for a **put option** held by the listed issuer's group); **or** the value of the assets subject to the option less the exercise price (for a **call option** held by the listed issuer's group); and
    2) the consideration or amount payable or receivable by the listed group (GEM Rule 20.77(4)).

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Options acquired by listed group from a connected person (Cont'd)

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

- a valuation of the option assets prepared by an independent expert using generally acceptable methodologies; and

- a confirmation from the INEDs and an independent financial adviser that the transfer, termination or non-exercise of the option is fair and reasonable and in the interests of the listed issuer and its shareholders as a whole.

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

CONNECTED TRANSACTIONS (Cont'd)

Joint ventures involving Connected Persons

The entrance into any arrangement or agreement involving the formation of a joint venture entity in any form, such as a partnership or company or any other form of joint arrangement, by a listed issuer and a connected person constitutes a connected transaction.

Continuing Connected Transactions

Continuing connected transactions are connected transactions that:

a) involve the provision of goods, services or financial assistance;

b) are carried out on a continuing or recurring basis; and

c) are expected to extend over a period of time.

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

Classification of Connected and Continuing Connected Transactions

i. Non-exempt transactions which must be: (a) reported in the listed issuer's annual report; (b) announced on the websites of the Exchange and the listed issuer; and (c) approved by the issuer's independent shareholders;

ii. Transactions exempt from the reporting, announcement and independent shareholders' approval requirements ("**wholly exempt**" transactions); and

iii. Transactions exempt from the independent shareholders' approval requirement only (but subject to the reporting and announcement requirements) ("**partially exempt**" transactions).

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CONNECTED TRANSACTIONS (Cont'd)

Connected transaction requirements

Written agreement requirement

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

Reporting requirement

The listed issuer's next published annual report and accounts must include details of the connected transaction including the transaction date, the transaction parties and a description of their connected relationship, a brief description of the transaction and its purpose, the total consideration and terms and the nature and extent of the connected person's interest.

Notification and announcement requirements

The listed issuer must notify the Exchange as soon as possible after the terms of the connected transaction have been agreed upon and publish an announcement as soon as possible.

Independent shareholders' approval requirements

Connected transactions and continuing connected transactions must be approved by the issuer's independent shareholders. Any shareholder who has a material interest in the transaction must abstain from voting.

Voting on the resolution approving the connected transaction must be by way of poll.

CONNECTED TRANSACTIONS (Cont'd)

Connected transaction requirements (Cont'd)

Independent board committee and financial adviser requirements

An **independent board committee** must be established to advise shareholders as to:

- whether the terms of the connected transaction are fair and reasonable;
- whether the connected transaction is on normal commercial terms or better and in the group's ordinary and usual course of business;
- whether the transaction is in the interests of the listed issuer and the shareholders as a whole; and
- how to vote, taking into consideration the views of the independent financial adviser.

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

Written independent shareholders' approval

The Exchange may waive the general meeting requirement and accept a written independent shareholders' approval if:

1. No shareholder of the issuer would be required to abstain from voting if a general meeting were held, and
2. The written independent shareholders' approval is obtained from a shareholder of closely allied group of shareholders who (together) hold more than 50% of the voting rights in general meeting (GEM Rule 20.35).

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CONNECTED TRANSACTIONS (Cont'd)

Connected transaction requirements (Cont'd)

Shareholders' circular requirement

The listed issuer must send a circular to shareholders:

- at the same time as or before it gives notice of the general meeting to approve the transaction; or
- if the transaction is to be approved by way of written shareholders' approval from a shareholder or closely allied group of shareholders, within 15 business days after the publication of the announcement.

The shareholders' circular must comply with the contents requirements of GEM Rules 20.58 and 20.59 and must include the letter from the independent board committee and the independent financial adviser's opinion.

CONNECTED TRANSACTIONS (Cont'd)

Continuing connected transaction (CCT) requirements

Additional requirements for CCTs

- In the case of continuing connected transactions, the agreement governing the transaction must be on normal commercial terms and must be for a fixed period.
- It must not exceed 3 years except in special circumstances where the nature of the transaction requires a longer period.
- In this case, the issuer must appoint an independent financial adviser to explain why the agreement requires a longer period and that it is normal business practice for agreements of this type to be of a longer duration.
- The reporting requirements must be followed for each subsequent financial year during which the listed issuer undertakes the continuing connected transaction.

Annual cap requirement

- The listed issuer must set a maximum aggregate annual cap expressed in monetary terms, the basis of which must be disclosed.
- The annual cap must be determined by reference to previous transactions and figures in the group's published information or be based on reasonable assumptions if no previous transaction exists.
- The annual cap must be approved by shareholders if the continuing connected transaction requires shareholder approval.
- If the annual cap is exceeded, or if the relevant agreement is renewed or its terms are changed materially, the listed issuer must re-comply with the announcement and independent shareholders' approval requirements.

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CONNECTED TRANSACTIONS (Cont'd)

Continuing connected transaction (CCT) requirements (Cont'd)

Annual review requirement

Each year, the independent non-executive directors of the listed issuer must review the continuing connected transactions and confirm in the annual report and accounts that the transactions have been entered into:

a) in **the ordinary and usual course of business** of the group;

b) either on **normal commercial terms** or better; and

c) in accordance with the relevant agreement on terms that are fair, reasonable and in the interests of the listed issuer's shareholders as a whole.

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

a) have not received the approval by the board;

b) were not, in all material respects in accordance with the group's pricing policies if the transactions involve provision of goods and services;

c) were not entered into, in all material respects, in accordance with the relevant agreement; and

d) have exceeded the annual cap.

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CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt connected transactions

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

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

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CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt transactions (Cont'd)

Intra-group transactions

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

a) none of the subsidiaries concerned are connected persons; and

b) no connected persons at the issuer level exercise or control the exercise of 10% or more of the voting power at any general meeting of any of the subsidiaries concerned.

Connected transactions are also exempt from the Listing Rules' requirements where they are between the issuer's non wholly-owned subsidiary of which a connected person of the issuer (at the issuer level) controls 10% or more of the voting power at any general meeting of such non wholly-owned subsidiary and any of its subsidiaries which are connected persons only by virtue of being the subsidiaries of such non wholly-owned subsidiary or where the transaction is between any of these subsidiaries.

CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt transactions (Cont'd)

De minimis transactions

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

a) less than 0.1%;

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

c) less than 5% and the total consideration is less than HK$3 million.

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

Wholly exempt transactions (Cont'd)

Certain issues of new securities

Issues of new securities by a listed issuer or its subsidiaries to a connected person are wholly exempt where:

a) the connected person receives a pro rata entitlement to securities in its capacity as shareholder;

b) securities are issued under a share option scheme which complies with Chapter 23 or securities are issued under a share option scheme in existence before the issuer was listed on the Exchange for which approval for listing was granted at the time of listing;

c) the connected person subscribes for securities in a right issue or open offer:

   i. through excess application under GEM Rules 10.31(2) or 10.42(1); or

   ii. in his or its capacity as an underwriter or sub-underwriter of the rights issue or open offer, and GEM Rules 10.31(2) or 10.42(1) (arrangement to dispose of excess securities) has been complied with;

Wholly exempt transactions (Cont'd)

Certain issues of new securities (Cont'd)

Issues of new securities by a listed issuer or its subsidiaries to a connected person are wholly exempt where:

d) securities are issued under a "top-up placing and subscription" that meets the following conditions:

   i. the new securities are issued to the connected person:

      1. after such connected person has reduced its holding in the same class of securities by placing them to third parties who are not its associates under a placing agreement; and

      2. within 14 days after the date of the placing agreement;

   ii. the number of new securities issued to the connected person does not exceed the number of securities placed by it; and

   iii. the new securities are issued at a price not less than the placing price. The placing price may be adjusted for the expenses of the placing.

CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt transactions (Cont'd)

Purchase of own securities

Share repurchases by a listed issuer or its subsidiary from a connected person on a recognised stock exchange are wholly exempt from the connected transaction requirements (unless the connected person knowingly sells shares to the listed issuer). Share repurchases under a general offer made under the Code on Share Repurchases are also wholly exempt.

Directors' service contracts

A director entering into a service contract with the listed issuer or its subsidiary is wholly exempt.

CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt transactions (Cont'd)

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

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

- the indemnity/insurance is for liabilities that may be incurred in the course of the director performing his duties; and

- the indemnity/insurance is in a form allowed under the laws of Hong Kong, and, where the company providing or purchasing the insurance is incorporated outside Hong Kong, the laws of the company's place of incorporation.

Sharing of administrative services

The sharing of administrative services between a group and a connected person on a cost basis is wholly exempt, provided that the costs are identifiable and are allocated to the parties involved on a fair and equitable basis.

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CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt transactions (Cont'd)

Buying or selling consumer goods or services

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

a) the goods or services must be of a type ordinarily supplied for private use or consumption;

b) they must be for the buyer's own consumption or use, and not be:

   i. processed into the buyer's products or for resale; or

   ii. used by the buyer for any of its businesses or contemplated businesses. This condition does not apply if the buyer is the group and there is an open market and transparency in the pricing of the goods or services;

c) they must be used or consumed by the buyer in the same state as when they were bought; and

d) the transaction must be on no more favourable terms to the connected person, or no less favourable terms to the group, than those available to or from independent third parties.

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CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt transactions (Cont'd)

Transactions with associates of a passive investor

A connected transaction of a revenue nature in the ordinary and usual course of the group's business and on normal commercial terms or better is wholly exempt where:

a) the transaction is a connected transaction only because it involves an associate (the "Relevant Associate") of a substantial shareholder of the listed issuer; and

b) the substantial shareholder is a passive investor in the listed issuer and meets the following criteria:

   i. it is a sovereign fund, or a unit trust or mutual fund authorised by the Securities and Futures Commission or an appropriate overseas authority;

   ii. it has a wide spread of investments other than the securities of the listed issuer's group and the Relevant Associate;

   iii. it and the Relevant Associate are connected persons only because it is a substantial shareholder of the listed issuer;

   iv. it is not a controlling shareholder of the listed issuer or its subsidiaries;

   v. it does not have any representative on the board of directors of the listed issuer or its subsidiaries, and is not involved in the management of the group (including any influence over the listed issuer's management through negative control (e.g. its veto rights) on material matters of the listed issuer); and

   vi. it is independent of the directors, chief executive, controlling shareholder(s) and any other substantial shareholder(s) of the listed issuer or its subsidiaries.

Wholly exempt transactions (Cont'd)

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

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

a) the indemnity/insurance is for liabilities that may be incurred in the course of the director performing his duties; and

b) the indemnity/insurance is in a form allowed under the laws of Hong Kong, and, where the company providing or purchasing the insurance is incorporated outside Hong Kong, the laws of the company's place of incorporation (GEM Rules 20.93 and 20.94).

CONNECTED TRANSACTIONS (Cont'd)

Partially exempt connected transactions

Connected transactions (other than an issue of new securities by the listed issuer) are exempt from the independent shareholders' approval requirement only (and are subject to the reporting and announcement requirements) where:

a) The connected transaction is on normal commercial terms or better; and

b) All the percentage ratios (except the profits ratio) is/are:

   i. Less than 5%; or

   ii. Less than 25% and the total consideration is less than HK$10 million.

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CONNECTED TRANSACTIONS (Cont'd)

Exemption for connected persons at the subsidiary level

Transactions with persons connected only at the subsidiary level are exempt from the shareholders' approval requirement if:

a) the transactions are on normal commercial terms or better;

b) the transactions are approved by the issuer's board of directors; and

c) the issuer's INEDs confirm that the terms of the transactions are fair and reasonable, and they are on normal commercial terms and in the interests of the issuer and its shareholders as a whole (GEM Rule 20.99).

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CONNECTED TRANSACTIONS (Cont'd)

Wholly exempt CCTs

The following exemptions for connected transactions apply to continuing connected transactions:

- the sharing of administrative services;
- buying or selling consumer goods or services; and
- transactions with associates of a passive investor and de minimis transactions.

In the case of the *de minimis* exemption, the percentage ratios are calculated on an annual basis.

Partially exempt CCTs

Continuing connected transactions are exempt from only the independent shareholders' approval requirements where each or all of the percentage ratios (except the profits ratio) is/are on an annual basis:

a) less than 5%; or

b) less than 25% and the annual consideration is less than HK$10 million.

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Exemptions for financial assistance

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

Financial assistance provided by a listed issuer or its subsidiaries (which is not a bank) to a connected person or a Commonly Held Entity is fully exempt if it is:

a. provided on normal commercial terms (or better to the group); and

b. the assistance provided is proportional to the equity interest directly held by the issuer or its subsidiary in the connected person or the Commonly Held Entity and any guarantee provided by the listed issuer's group is given on a several basis.

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

a) provided on normal commercial terms (or better to the group); and

b) no security over the assets of the listed issuer or its subsidiaries is granted in respect of the financial assistance.

Exchange's discretion

In any situation, the Exchange reserves the right to specify that an exemption will not apply to a particular transaction, or to require the listed issuer to meet the independent shareholders' approval requirements.

Requirement for INEDs

- INEDs must make up at least one third of a listed issuer's board.
- The minimum number of INEDs is three INEDs, at least one INED must have 'appropriate professional qualifications or accounting or related financial management expertise'.
- The Listing Rules provide guidance as to what such financial expertise entails.
- But ultimately it is the responsibility of the board to determine on a case by case basis whether a candidate is suitable for the position.

Requirement for INEDs (Cont'd)

In assessing the independence of a non-executive director, the Exchange will be likely to question the independence of a candidate in the circumstances below:

a) The director holds more than a 1% shareholding interest (whether legal or beneficial and including any rights to call for the issue of shares) in the listed issuer, or if he has received any shareholding interest as a gift, or by means of other financial assistance (eg, a loan), from the listed issuer or its connected person. A director holding a 5% or more shareholding interest will not normally be considered independent;

b) The director is a professional adviser to the listed issuer, its holding company or any of their subsidiaries or connected persons, or to any person who was a controlling shareholder within the past one year or their associates if there is no controlling shareholder, the chief executive or a director of the listed issuer within the past one year or their associates, in each case subject to a one-year cooling-off period;

c) The director is appointed to protect the interests of a particular shareholder;

d) The director has a material interest in any principal business activity of, or is involved in any material business dealings with, the group or with any connected person of the listed issuer;

Requirement for INEDs (Cont'd)

e) The director is 'connected with' a director, the CEO or any person who was a substantial shareholder in the past two years. GEM Rule 5.09(6) provides further elaboration on what constitutes a 'connection' (normally includes relatives);

f) The director is an 'executive' (including one who exercises a management function or acts as a company secretary) or director of the group or of any connected person of the listed issuer, subject to a two-year cooling-off period;

g) The director is financially dependent on the group or any connected persons of the listed issuer.

If a listed issuer fails to meet the requirements as to the minimum number of INEDs or the qualification of the INEDs, it must inform the Exchange immediately and publish an announcement on the Exchange's website as well as its own.

The issuer then has three months to appoint a sufficient number of INEDs or an INED with appropriate professional qualifications to meet the Rules' requirements.

Audit Committee

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

The majority of audit committee members must be INEDs and it must be chaired by an INED. The duties of the audit committee are Code provisions under the Code on Corporate Governance Practices.

The audit committee's terms of reference must include, among others:

a) monitoring the relationship with the issuer's auditors, including responsibility for making recommendations to the board on the appointment, reappointment and removal of the auditors;

b) monitoring the integrity of the issuer's financial statements and reviewing significant financial reporting judgements contained in them; and

c) overseeing the issuer's financial reporting system and internal control procedures.

Code provision C2.2 further requires that the board's review of its internal controls must include a review of the adequacy of the resources, qualifications and experience of staff, training programmes and budget of the issuers' accounting and reporting function.

Directors' service contracts

Shareholders' prior consent is required before the grant of a service contract to a director of the listed issuer or any of its subsidiaries, if the contract is for 3 years or more or requires the listed issuer to give more than one year's notice or pay the equivalent of more than one year's remuneration on termination.

Directors' Remuneration

Directors' fees and any other reimbursement or emolument (including allowances and benefits in kind) paid to a director must be disclosed in full in the annual reports and accounts of an issuer on an individual and named basis (GEM Rule 18.28).

The company must also disclose information in respect of the 5 highest paid individuals during the financial year under GEM Rule 18.30.

This information is however only required if any of those individuals is/are not directors whose emoluments will be disclosed under GEM Rule 18.28.

Remuneration Committee

GEM Rules 5.34 to 5.36 require:

a) issuers to establish a remuneration committee with a majority of INED members;

b) an INED as chairman of the remuneration committee;

c) written terms of reference for the remuneration committee; and

d) an issuer that fails to comply with these Rules to immediately announce its reasons for not doing so and any other relevant details. The issuer will have a three-month period to rectify its non-compliance.

The Corporate Governance Code allows for two different types of remuneration committee:

- In the first model, the board delegates to the remuneration committee authority to determine the remuneration of executive directors and senior management.
- In the second model, the board retains that authority, with the remuneration committee taking an advisory role.

The minimum terms of reference of the remuneration committee are set out in Code provision B.1.2. The terms of reference should be made available on the GEM website and the listed issuer's website.

Nomination Committee

It is a Code provision under the Corporate Governance Code that a listed issuer should establish a nomination committee with a majority of INEDs, chaired by an INED or the board chairman (Code provision A.5.1).

The nomination committee's written terms of reference should include:

a) reviewing the board's structure, size and composition (including the skills, knowledge and experience) at least annually;

b) identifying and recommending potential board members; and

c) assessing the independence of INEDs.

CORPORATE GOVERNANCE (Cont'd)

Compliance Adviser

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

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

a) before publication of any regulatory announcement, circular or financial report;

b) where a transaction which might be a notifiable or connected transaction is contemplated (including share issues and repurchases);

c) where the listed issuer proposes to use the IPO proceeds in a manner different from that set out in the listing document;

d) where the business activities, developments or results of the issuer deviate from any forecast, estimate or other information in the listing document; and

e) where the Exchange makes an inquiry of the issuer under GEM Rule 17.11.

Authorised Representatives

A listed issuer is required to appoint 2 authorised representatives to act as its principal channel of communication with the Exchange.

These must be two directors or a director and the company secretary.

Whenever they are outside Hong Kong, the authorised representatives must appoint suitable alternates and provide the Exchange with the alternates' contact details.

The Exchange must be given prior notification of an authorised representative's proposed termination of his role and the reasons for it.

Company Secretary

An issuer must appoint a company secretary being 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 company secretary.

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

a) members of the Hong Kong Institute of Chartered Secretaries;
b) solicitors or barristers (as defined in the Hong Kong Legal Practitioners Ordinance); and
c) certified public accountants (as defined in the Hong Kong Professional Accountants Ordinance).

If a person does not have the above qualifications, the Exchange will take the following factors into account in determining whether he has "relevant experience" for the appointment:

a) the length of employment with the listed issuer or with other listed issuers and the roles he played;
b) his familiarity with the Listing Rules and other relevant law and regulations including the Securities and Futures Ordinance, the Companies Ordinance and the Takeovers Code;
c) relevant training taken and/or to be taken; and
d) his professional qualifications in other jurisdictions.

Board diversity

It is a Code principle under the Corporate Governance Code that a listed issuer's board should have a balance of skills, experience and diversity of perspective appropriate to the requirements of the issuer's business.

The nomination committee (or the board) should have a policy on board diversity which should be disclosed in the issuer's corporate governance report. Alternatively, a summary of the diversity policy may be disclosed. A note to Code provision A.5.6 sets out the following guidance on what is meant by "diversity":

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

Environmental, Social and Governance (ESG) reporting

ESG reporting is a requirement under GEM Rule 17.103 and is the overall responsibility of the board.

Listed issuers must state whether or not they have complied with the "comply or explain" provisions of the ESG Guide. If there is any deviation from any of those provisions, reasons for such deviation must be provided in the ESG report.

The ESG Guide sets out two key subject areas for reporting:

a) Environmental; and

b) Social.

Each subject area is divided into several aspects, and each aspect sets out the:

a) general disclosure requirements; and

b) Key Performance Indicators ("**KPIs**")

to measure ESG performance.

The ESG Guide is not comprehensive and issuers are encouraged to identify and disclose additional ESG issues and KPIs relevant to their businesses. They may adopt international ESG reporting guidance for their relevant industry or sector if it includes disclosure provisions comparable to the "comply or explain" provisions of the ESG Guide.

An ESG report must be included in the listed issuer's annual report, or separately in an ESG report published in print or on the issuer's website. The ESG report and annual report must cover the same reporting period.

THE CODE ON CORPORATE GOVERNANCE PRACTICES

- The Code on Corporate Governance Practices (the "**Code**") is set out in Appendix 15 of the GEM Listing Rules.
- Two tiers of recommended practices.
- The first tier contains the "Code Provisions" which are the minimum standards with which listed companies are expected to comply.
- Companies must state in their half-year and annual reports whether they have complied with the Code Provisions. If they have chosen to deviate from the Code Provisions, considered reasons for each deviation must be stated.
- The second tier of recommended practices consists of recommended best practices which listed companies are encouraged to adopt. Listed companies are encouraged, but are not required, to include a statement as to compliance with the recommended best practices and considered reasons for any deviations from them in their financial reports.
- The Code covers 20 principal areas, including: Directors; Remuneration of Directors and Senior Management; Accountability and Audit; Delegation by the Board and Communication with Shareholders.

THE CODE ON CORPORATE GOVERNANCE PRACTICES (Cont'd)

Code provisions in relation to directors

i. Full board meetings should be held at least 4 times a year at approximately quarterly intervals;

ii. Different people should perform the roles of chairman and chief executive;

iii. All directors should be subject to retirement by rotation once every 3 years;

iv. The directors should conduct an annual review of the internal controls of the issuer and its subsidiaries;

v. Directors should provide records of training they received to the issuer;

vi. Issuers should arrange appropriate insurance cover for directors;

vii. In the circular nominating an INED for election, issuers should include the reasons why the board considers an INED to be independent. Shareholders should vote on a separate resolution to retain an INED who has served on the board for more than nine years;

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THE CODE ON CORPORATE GOVERNANCE PRACTICES (Cont'd)

Code provisions in relation to directors (Cont'd)

viii. An audit committee should meet the external auditor at least twice a year and an audit committee's terms of reference should include arrangements for employees to raise concerns about financial reporting improprieties;

ix. Non-executive directors, including INEDs, should attend board, committee and general meetings and contribute to the issuer's strategy and policies; and

x. Management should provide monthly updates of the issuer's performance, position, and prospects to board members sufficient to enable them to discharge their duties.

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THE CODE ON CORPORATE GOVERNANCE PRACTICES (Cont'd)

The Corporate Governance Report

- Listed issuers are required to include a Corporate Governance Report prepared by the board in their annual reports and any summary financial report.
- The Corporate Governance Report must include certain mandatory disclosures which are set out at paragraphs G to Q of Appendix 15 to the GEM Rules.
- Failure to include any of the mandatory disclosures is regarded as a breach of the GEM Rules.
- The mandatory disclosures relate to corporate governance practices, directors' securities transactions, the board of directors, the chairman and chief executive, non-executive directors, board committees, auditor's remuneration, the company secretary, shareholders' rights and significant changes to the issuer's constitutional documents during the year.

SECURITIES TRANSACTIONS BY DIRECTORS OF LISTED COMPANIES

Absolute Prohibition

A director of a listed issuer must not deal in the securities of the company:

a) at any time when he is in possession of inside information in relation to those securities or if clearance to deal has not been given;

b) on the publication date of the company's financial results;

c) during the 60 days preceding the publication of the annual results or, if shorter, the period from the end of the relevant financial year up to the publication date of the results; and

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

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

Further, a director of a listed issuer must not deal in its securities if he is in possession of inside information in relation to those securities by virtue of his position as a director of another listed issuer.

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

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SECURITIES TRANSACTIONS BY DIRECTORS OF LISTED COMPANIES

Duty of notification

A listed issuer is required to establish a procedure whereby a director is required to provide written notification to the chairman or a director (other than himself) designated by the board and receive a dated written acknowledgement before dealing in any securities of the listed issuer.

A response to a request for clearance to deal must be given to the relevant director within 5 business days and the clearance to deal must be valid for no more than 5 business days of clearance being received.

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

DISCLOSURE OF INTERESTS UNDER PART XV SFO

Part XV of the SFO contains complex provisions requiring substantial shareholders (holders of 5% or more) and directors and chief executives to disclose their interests in listed companies.

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

a) their interests and short positions in any shares of the listed issuer or its associated corporations;

b) their interests in any debentures of the listed issuer or its associated corporations; and

c) any change in or cessation of any such interest.

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

DISCLOSURE OF INTERESTS UNDER PART XV SFO (Cont'd)

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

A company will be "controlled" by a director if the director directly or indirectly controls one third or more of the voting power at general meetings of the company or if the company or its directors are accustomed to act in accordance with his directions.

Directors must also disclose their interests in the underlying shares of equity derivatives. The term "equity derivative" is defined to include any contract which gives a person rights, options or interests in respect of the underlying shares.

Generally speaking, a person has a short position in shares if he:

a) borrows shares under a securities borrowing and lending agreement; or

b) holds or issues a financial instrument under which he has a right to require another person to take the underlying shares or is under an obligation to deliver the underlying shares.

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

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DISCLOSURE OF INTERESTS UNDER PART XV SFO (Cont'd)

Where a person is, or will become, a director or chief executive of a company on its listing on the Exchange, he has **10 business days** in which to file notice of the following interests:

a) an interest in the shares of the listed issuer or in the shares of an associated corporation;

b) a short position in the shares of the listed issuer or in the shares of an associated corporation;

c) an interest in debentures of the listed issuer or in the debentures of an associated corporation.

A new director of a listed issuer must give notice of the above interests within **10 business days** of being appointed as a director.

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DISCLOSURE OF INTERESTS UNDER PART XV SFO (Cont'd)

Subsequent filings by directors and the chief executive of a listed issuer are required on the occurrence of certain events, called "relevant events". In the case of interests in shares and any short positions, the relevant events include:

i. when a director becomes interested in the shares of the listed issuer or any of its associated corporations (e.g. on the grant to the director of share options);

ii. when a director ceases to be interested in such shares;

iii. when a director enters into a contract to sell any such shares;

iv. when a director assigns any right granted to him by the listed issuer to subscribe for such shares;

v. when an associated corporation grants a director a right to subscribe for shares in the associated corporation or the director exercises or assigns such rights;

DISCLOSURE OF INTERESTS UNDER PART XV SFO (Cont'd)

vi. when the nature of the director's interest changes (e.g. on the exercise of an option);

vii. when a director comes to have, or ceases to have, a short position in the shares of the listed issuer or in the shares of an associated corporation;

viii. if the director has an interest, or a short position, in the shares of the listed issuer, or in the shares of an associated corporation, at the time he becomes a director of chief executive of the listed issuer; and

ix. if a director has an interest, or a short position, in the shares of an associated corporation, at the time when it becomes an associated corporation.

Notice of the relevant events at (i) to (vii) above must be filed with the listed issuer and the Exchange within **3 business days** after the relevant event. Notice of the relevant events at (viii) and (ix) above must be filed within **10 business days** after the relevant event.

❖ *Failure to make proper and timely disclosure as required by Part XV is a criminal offence which carries a maximum penalty of a fine of HK$100,000 and imprisonment for up to two years.*

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DISCLOSURE OF INTERESTS UNDER PART XV SFO (Cont'd)

The listed issuer also has a duty to keep registers of:

a) the interests and short positions of its substantial shareholders (i.e. holders of 5% or more of any class of voting shares);

b) the interests and short positions of its directors and chief executive in the shares of the listed issuer and its associated corporations;

c) the interests of its directors and chief executive in the debentures of the listed issuer and its associated corporations.

These registers must be kept either at the registered address of the listed issuer or at the place where the register of shareholders is kept. When the issuer receives a notice in the prescribed form, it must enter the information on the form in the register within 3 business days after it is received.

The interests and short positions of a listed issuer's directors and chief executive in the shares, underlying shares and debentures of the company and its associated corporations must also be disclosed in the company's annual accounts and half-year reports.

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INSIDER DEALING

Insider dealing takes place when:

i. a person who is (a) connected with a listed issuer and having information which he knows is inside information; or (b) contemplating (or has contemplated) making a takeover offer for a listed issuer and who knows that the information that the offer is contemplated (or is no longer contemplated) is inside information in relation to the listed issuer:

   1) deals, or counsels or procures another to deal, in the company's listed securities or their derivatives or in those of a related corporation (otherwise than for the purpose of the takeover in the case of (b) above); or

   2) discloses the information knowing or having reasonable cause to believe that the recipient will use the information to deal, or to counsel or procure another person to deal, in the company's listed securities or their derivatives or in those of a related corporation;

INSIDER DEALING (Cont'd)

ii. a person who has received inside information from a connected person or a person who is contemplating or has contemplated making a takeover offer for a listed issuer either deals, or counsels or procures another person to deal, in the company's listed securities or their derivatives or those of a related corporation; or

iii. a person who has information which he knows is inside information in relation to a listed issuer in any of the circumstances referred in paragraphs (i) and (ii) above:

1) counsels or procures another person to deal, knowing or having reasonable cause to believe that the person will deal, in the company's listed securities or their derivatives or in those of a related corporation outside Hong Kong on an overseas stock market; or

2) discloses the information knowing or having reasonable cause to believe that the recipient will use the information to deal, or to counsel or procure another person to deal, in the company's listed securities or their derivatives or in those of a related corporation outside Hong Kong on an overseas stock market.

INSIDER DEALING (Cont'd)

Key definitions

"**securities**" – defined widely and includes shares, stocks, debentures, loan stocks, bonds and notes as well as any rights, options or interests in respect of any of the foregoing;

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

"**Related corporations**" of a listed issuer – its subsidiaries and holding companies and other subsidiaries of any holding company of the listed issuer. In addition, where two or more companies are controlled by the same individual, each of those companies and their subsidiaries are regarded as "related corporations" of each other.

INSIDER DEALING (Cont'd)

Key definitions (Cont'd)

"**Control**" for these purposes – the individual controls either the composition of the company's board of directors or more than half of the voting power at general meetings of the company, or holds more than half of the company's issued shares.

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

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

MARKET MISCONDUCT

Other types of market misconduct include:

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

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MARKET MISCONDUCT (Cont'd)

False Trading

False trading takes place when a person:

i. intentionally or recklessly engages in conduct which creates a false or misleading appearance:
   a. of active trading in securities or futures contracts traded on an exchange or through an authorised automated trading service ("**ATS**") in Hong Kong; or
   b. with respect to the market for, or the price of, such securities or futures contracts;

ii. engages in similar conduct similar to (i) above in Hong Kong which has a similar effect on securities or futures contracts traded on an overseas market;

iii. is involved in one or more transactions with the intention that, or being reckless as to whether, they create or maintain an artificial price for securities or futures contracts traded on an exchange or through an ATS in Hong Kong; or

iv. engages in conduct similar to (iii) above in Hong Kong which has a similar effect on securities or futures contracts traded on an overseas market.

A person who engages in an on-market "wash sale" or "matched order" is presumed to have committed false trading.

- "Wash sale" – a trade in which a person buys or sells securities without there being a change in beneficial ownership
- "Matched order" – where a person offers to buy or sell securities at a price that is substantially the same as that at which he or an associate has made or proposes to make, an offer to sell or buy substantially the same number of such securities.

MARKET MISCONDUCT (Cont'd)

Price rigging

Price rigging occurs when a person engages in:

i. a wash sale of securities which maintains, increases, reduces, stabilises or causes fluctuations in, the price of securities traded on an exchange or through an ATS in Hong Kong; or

ii. any fictitious or artificial transaction or device with the intention that, or being reckless as to whether, it maintains, increases, reduces, stabilizes or causes fluctuations in, the price of securities or futures contracts traded on an exchange or through an ATS in Hong Kong.

The same conduct by a person in Hong Kong which affects securities or futures contracts traded on an overseas market will also constitute price rigging if such conduct is unlawful in the country in which the relevant market is situated.

MARKET MISCONDUCT (Cont'd)

Stock market manipulation

- These provisions relate only to transactions in securities.

- Stock market manipulation occurs when a person, in Hong Kong or elsewhere, engages directly or indirectly in two or more transactions in the securities of a company that by themselves or in conjunction with any other transaction increase, reduce, maintain or stabilise the price of any securities traded on an exchange or through an ATS in Hong Kong, or are likely to do so, with the intention of inducing another person to buy or subscribe for, or to refrain from selling, securities issued by that corporation or a related corporation.

- The same conduct by a person in Hong Kong which affects securities traded on an overseas market will also amount to stock market manipulation if the same conduct is unlawful in the relevant country.

MARKET MISCONDUCT (Cont'd)

Disclosure of information about prohibited transactions

Disclosure of information about prohibited transactions occurs when a person, in Hong Kong or elsewhere, discloses or disseminates, or authorises or is concerned in the disclosure or dissemination of, information about the effect of a prohibited transaction (being a transaction which contravenes the provisions of Part XIII or XIV of the SFO) on the price of securities or the price for dealings in future contracts traded on a Hong Kong market, if the person or an associate of his:

a. participates in the prohibited transaction; or

b. benefits or expects to benefit, directly or indirectly, from the disclosure, circulation or dissemination of the information.

MARKET MISCONDUCT (Cont'd)

Disclosure of false or misleading information including transactions

This form of market misconduct concerns the disclosure of false or misleading information about securities or futures contracts that is likely to induce investment decisions or have a material price effect.

A person will have engaged in market misconduct if he discloses or is involved in the disclosure of:

i. information likely to induce others to enter into transactions or to affect the price of securities or futures contracts, that is false or misleading in a material fact or through the omission of a material fact; and

ii. he knows or is reckless or (for civil market misconduct only) negligent as to whether, the information is false or misleading in a material fact or through the omission of a material fact.

Negligence will not suffice to establish criminal liability.

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MARKET MISCONDUCT (Cont'd)

Dual civil and criminal regimes

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

Criminal penalties

The maximum criminal sanction is 10 years' imprisonment and/or a fine of up to $10 million. The court may also impose disqualification, cold shoulder and disciplinary referral orders. Failure to comply with a disqualification or cold shoulder order is an offence liable to a maximum fine of $1 million and up to 2 years' imprisonment.

No double jeopardy

A person will not be subject to the 'double jeopardy' of both civil proceedings under Part XIII and criminal proceedings under Part XIV for the same conduct. The SFO provides that a person who has been subject to criminal proceedings under Part XIV may not be subject to MMT proceedings if those proceedings are still pending or if no further criminal prosecution could be brought against that person again under Part XIV in respect of the same conduct and vice versa.

MARKET MISCONDUCT (Cont'd)

Proceedings of the MMT

The MMT may identify a person as having engaged in market misconduct if:

i. he has perpetrated any market misconduct;

ii. the market misconduct was perpetrated by a corporation of which he is an officer with his consent or connivance; or

iii. another person engaged in market misconduct and he assisted or connived with that person in the perpetration of the market misconduct, knowing that such conduct constitutes or might constitute market misconduct.

MARKET MISCONDUCT (Cont'd)

Orders of the MMT

a) a disqualification order – that a person shall not, without the leave of the Court of First Instance, be or continue to be a director, liquidator, or receiver or manager of the property or business, of a listed corporation or any other specified corporation or in any way, whether directly or indirectly, be concerned or take part in the management of a listed corporation or other specified corporation for up to 5 years;

b) a cold shoulder order – that a person shall not, without the leave of the Court of First Instance, in Hong Kong, directly or indirectly, deal in any securities, futures contract or leveraged foreign exchange contract, or an interest in any of them or a collective investment scheme for up to 5 years;

c) a cease and desist order – that the person must not again engage in any specified form of market misconduct;

MARKET MISCONDUCT (Cont'd)

Orders of the MMT (Cont'd)

d) a disgorgement order – that the person pay to the Government an amount up to the amount of any profit gained or loss avoided as a result of the market misconduct;

e) Government costs order – that the person pay to the Government its costs and expenses in relation to the proceedings and any investigation;

f) SFC costs order – that the person pay the SFC's costs and expenses in relation to any investigation; and

g) disciplinary referral order – that any body which may take disciplinary action against the person as one of its members be recommended to take such action against him.

MARKET MISCONDUCT (Cont'd)

Civil liability – Private right of action

The SFO creates a private right of civil action in favour of anyone who has suffered financial loss as a result of market misconduct or any offence under Part XIV to seek damages from the person who committed the market misconduct or Part XIV offence. The perpetrator is liable to pay damages, unless it is fair, just and reasonable that he should not.

A person will be taken to have committed market misconduct if:

i. he has perpetrated any market misconduct;

ii. the market misconduct was perpetrated by a corporation of which he is an officer with his consent or connivance; or

iii. any other person committed market misconduct and he assisted or connived with that person in the perpetration of the market misconduct, knowing that such conduct constitutes or might constitute market misconduct.

MARKET MISCONDUCT (Cont'd)

Liability of officers

Section 279 of the SFO imposes a duty on all officers of a corporation to take reasonable measures to ensure that proper safeguards exist to prevent the corporation from acting in a way which would result in the corporation perpetrating any market misconduct. The duty applies to all forms of market misconduct and not just insider dealing.

The definition of an "**officer of a corporation**" includes a director (including a shadow director and any person occupying the position of a director), manager or secretary of, or any other person involved in the management of, the corporation. The last category (ie. any other person involved in management) could, in principle, catch supervisors and anyone else with management responsibilities.

Under Section 258, where a corporation has been identified as having been engaged in market misconduct and the market misconduct is directly or indirectly attributable to a breach by any person as an officer of the corporation of the duty imposed on him by Section 279, the MMT may make one or more of the orders detailed above in respect of that person even if that person has not been identified as having engaged in market misconduct himself. However, a breach of the Section 279 duty will not expose a person to civil suits by third parties unless he has been identified as having engaged in market misconduct.

MARKET MISCONDUCT (Cont'd)

Civil liability of officers

As described above, the SFO clearly provides that anyone who suffers financial loss as a result of market misconduct or a Part XIV offence has a right of civil action to seek compensation. As noted above, an officer of a corporation which perpetrated market misconduct is taken to have committed market misconduct himself, if the corporation perpetrated the misconduct with his consent or connivance.

Criminal liability of officers

Under Section 390 of the SFO, where it is proved that an offence committed under Part XIV was aided, abetted, counselled, procured or induced by, or committed with the consent or connivance of, or attributable to the recklessness of, any officer of the corporation, or any person purporting to act in any such capacity, that person, as well as the corporation, is guilty of the offence and liable to be punished accordingly.

OBLIGATIONS UNDER THE CODES ON TAKEOVERS AND MERGERS AND SHARE BUY-BACKS

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

The primary purpose of the Codes is to ensure that all shareholders affected by takeovers, mergers and share buy-backs of relevant companies are treated fairly.

In order to achieve fair treatment, the Codes require equality of treatment of shareholders and disclosure of timely and adequate information to shareholders.

The Takeovers Code in particular has the objective of protecting minority shareholders when control of their company changes.

The Takeovers Code is concerned with:

i. offers for, and takeovers and mergers of, all relevant companies; and

ii. partial offers, offers by a parent company for shares in its subsidiary and certain other transactions where control (as defined) of a company is to be obtained or consolidated.

Mandatory offer requirement: Rule 26

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

i. when any person (or two or more persons acting in concert) acquires, whether by a series of transactions over a period of time or not, 30% or more of the voting shares of a company; or

ii. when any person (or two or more persons acting in concert) who holds between 30% and 50% of the voting shares of a company, acquires additional voting shares that increase his or their holding of voting shares by more than 2% from the lowest percentage holding by that person (or the concert group) in the previous 12 month period.

"Persons acting in concert"

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

i. a company, its parent, its subsidiaries, its fellow subsidiaries, associated companies of any of the foregoing, and companies of which such companies are associated companies; and

ii. a company with any directors (together with their close relatives, related trusts and companies controlled by any of the directors, their close relatives or related trusts) of it or its parent company.

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

Requirements of the Takeovers Code

Rules 1 and 2 of the Takeovers Code set out the steps which should be taken by the boards of directors of the offeree and offeror companies in the course of takeover and merger transactions.

They require firstly that any offer of takeover of a listed issuer should be put in the first instance to the board of the listed issuer or its advisers before the offer is announced to the public.

The identity of the offeror must also be disclosed.

The board of the listed issuer must establish an independent committee of the board to make a recommendation:

i. as to whether or not the offer is fair and reasonable; and

ii. as to acceptance and voting.

The board must also retain an independent financial adviser to advise the independent board committee as to those matters.

THE CODE ON SHARE BUY-BACKS

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

1. **On Market** – this is the most usual method and is normally carried out pursuant to the 10% general mandate normally granted at the AGM.

2. **Off-Market** – Off-market share buy-backs must be approved by the Executive Director of the Corporate Finance Division of the Securities and Futures Commission ("**SFC**") under Rule 2 of the Share Buy-backs Code. Approval is normally conditional on the approval of at least three-quarters of the votes cast by "disinterested shareholders".

3. **Exempt** – exempt share buy-backs include an employee share buy-back; a share buy-back made in accordance with the terms attached to the shares; and a share buy-back that is required by the law of the jurisdiction in which the offeror is incorporated or established.

4. **By General Offer** – this usually takes the form of a tender offer of a certain percentage of all shareholders' holdings. A share buy-back by General Offer requires approval by at least 50% of shareholders in general meeting. A shareholder with a material interest in the share buy-back will not be allowed to vote. If the buy-back will result in privatisation or de-listing of the issuer, the approval of 75% of shareholders is required.

On-market share buy-backs

An issuer whose primary listing is on the Exchange may only purchase shares on the Exchange in the following circumstances:

- the shares proposed to be repurchased are fully-paid up;
- an Explanatory Statement complying with the detailed contents requirements of GEM Rule 13.08 is issued to the shareholders; and
- its shareholders have given specific approval or a general mandate to make the repurchase(s) by way of an ordinary resolution passed at a general meeting of the issuer duly convened.

On-market share buy-backs (Cont'd)

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

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

THE CODE ON SHARE BUY-BACKS (Cont'd)

Dealing restrictions of on-market buy-backs

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

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THE CODE ON SHARE BUY-BACKS (Cont'd)

Off-market share buy-backs

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

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

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THE CODE ON SHARE BUY-BACKS (Cont'd)

Buy-back by general offer

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

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

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

THE CODE ON SHARE BUY-BACKS (Cont'd)

Reporting requirements for buy-backs

The issuer must submit for publication to the Exchange through HKEx-EPS a next day disclosure return no later than 30 minutes before the commencement of the morning trading session (or any earlier pre-opening session) on the business day following the buy-back showing the number of shares bought-back, the purchase price paid per share (or the lowest and highest prices paid).

Listed issuers must also include in their annual report and accounts a monthly breakdown of purchases of shares made during the financial year under review showing the number of shares purchased each month (whether on the Exchange or otherwise), the purchase price paid per share (or the lowest and highest prices paid) and the aggregate price paid. The directors' report must refer to the purchases made during the year and the directors' reasons for making such purchases.

THE CODE ON SHARE BUY-BACKS (Cont'd)

Status of purchased shares

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

Restriction on new issue of shares following buy-back

An issuer whose primary listing is on the Exchange cannot issue, or announce a proposed new issue of shares, in the 30 days after its buy-back of shares (whether on the Exchange or otherwise), without the Exchange's prior approval. Exchange approval is not required for issues of securities pursuant to the exercise of warrants, share options or similar instruments which were outstanding before the share buy-back.

THE CODE ON SHARE BUY-BACKS (Cont'd)

Takeovers implications of share buy-backs

Under Rule 32.1 of the Takeovers Code, a share repurchase is considered to be an acquisition by shareholders whose shares are **not** bought-back.

This is because their percentage holding of shares increases even though the actual number of shares held does not.

As a result, a shareholder, or group of shareholders acting in concert, could obtain control of the issuer and become obliged to make a mandatory general offer obligation under Rule 26.

The Executive will normally grant a whitewash waiver in the case of general offer obligations triggered by off-market share buy-backs or share buy-backs by general offer.

Effectively the Rule 32 whitewash mechanism applies only to a shareholder who is a director or a person who is acting in concert with a director of the company. An unconnected shareholder would not normally be regarded as having triggered a mandatory bid obligation under Rule 26 if the increase in his shareholding is solely due to share buy-backs by the company.

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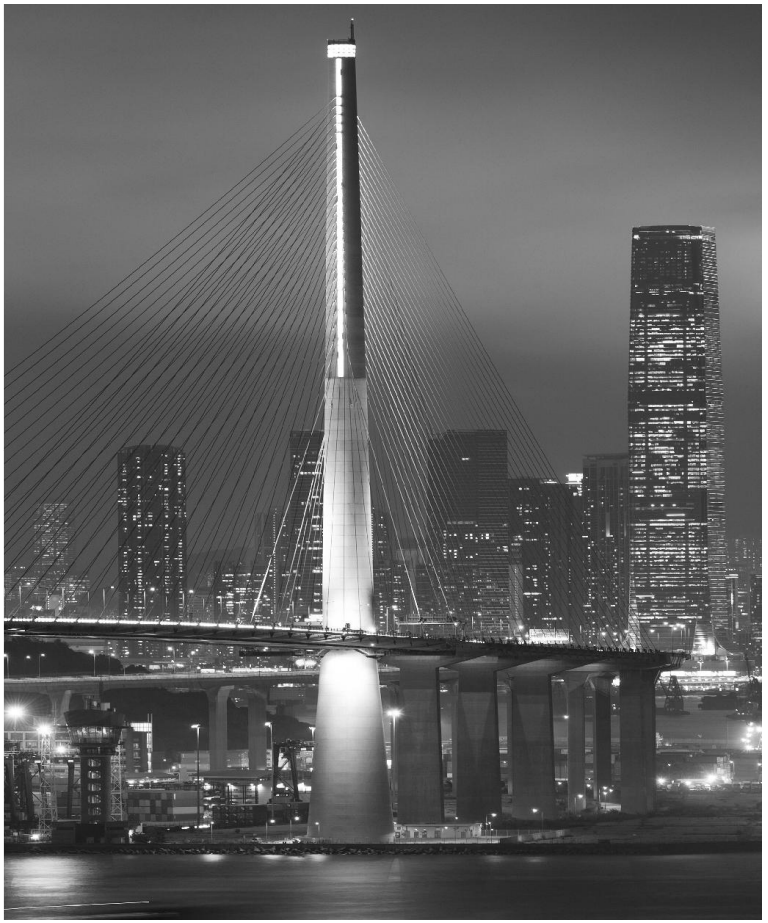

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