

**Frequently Asked Questions Series 28 (Released on 21 March 2014)**

**Rule Requirements Relating to Connected Transactions (effective 1 July 2014)**

**Status of “Frequently Asked Questions”**

The following frequently asked questions (FAQs) are designed to help issuers to understand and comply with the Listing Rules, particularly in situations not explicitly set out in the Rules or where further clarification may be desirable.

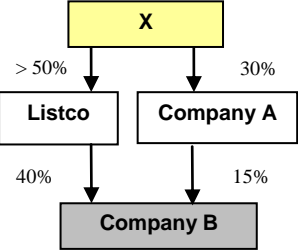
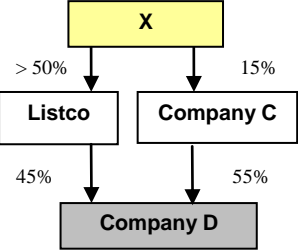
Users of the FAQs should refer to the Rules themselves and, if necessary, seek qualified professional advice. The FAQs are not substitutes for the Rules. If there is any discrepancy between the FAQs and the Rules, the Rules prevail.

In formulating our “answers”, we may have assumed certain underlying facts, selectively summarised the Rules or concentrated on one particular aspect of the question. They are not definitive and do not apply to all cases where the scenario may at first appear similar. In any given case, regard must be had to all the relevant facts and circumstances.

The Listing Division may be consulted on a confidential basis. Contact the Listing Division at the earliest opportunity with any queries.

No.	Main Board Rules	GEM Rules	Query	Response
<b>Persons connected with insignificant subsidiaries</b>				
1.	14A.09	20.08	<p>Listco has acquired certain fixed assets from Company A (being a substantial shareholder of a subsidiary of Listco), which constitutes a connected transaction subject to the announcement and reporting requirements.</p> <p>Will Listco need to report the above acquisition in its next annual report if Company A becomes qualified for the insignificant subsidiary exemption based on Listco's results at the end of the year?</p>	Yes. Listco is required to comply with the connected transaction requirements applicable at the time of entering into the transaction.
2.	14A.09, 14A.60, 14A.101	20.08, 20.58, 20.99	<p>Listco has entered into a framework agreement with Company A (being a substantial shareholder of a subsidiary of Listco) for purchasing certain raw materials at prices to be determined from time to time. It is not a connected transaction as Company A qualifies for the insignificant subsidiary exemption.</p>	If Listco continues to conduct the transactions under the framework agreement, it needs to comply with the announcement, reporting and annual review requirements, unless the transactions are fully exempt under the de minimis exemption.

No.	Main Board Rules	GEM Rules	Query	Response
			If a year later, Company A no longer meets the insignificant subsidiary exemption (and is therefore a connected person at the subsidiary level), what are the connected transaction requirements applicable to this case?	
<b>Definition of associates - Trustee interests</b>				
3.	14A.12(1)(b)	20.10(1)(b)	Will an employees' share scheme or occupational pension scheme be regarded as being established for a wide scope of participants based on the fact that the interests of connected persons in the scheme are together less than 30%?	No. The scheme must satisfy both conditions to qualify for the trustee exemption. Whether or not a scheme is established for a wide scope of participants would depend on the circumstances of the individual cases.
4.	14A.12(1)(b)	20.10(1)(b)	When determining the connected persons' aggregate interests in an employees' share scheme or occupational pension scheme, does the issuer have to take into account the interests of any employees who are relatives of the issuer's directors or substantial shareholder?	It will depend on whether the relatives are deemed to be associates of the directors/substantial shareholder in the proposed transaction with the trustee of the scheme. The issuer should provide information for the Exchange to assess whether or not to apply the deeming provision, and judgement needs to be exercised in considering whether these persons stand to benefit from the transaction.

No.	Main Board Rules	GEM Rules	Query	Response
<b>Definition of associates - Company held by connected person through its interest in the issuer</b>				
5.	14A.14	20.12	<p>Is Company B an associate of Mr. X in the following scenario?</p>  <pre> graph TD   X[X] -- "&gt; 50%" --&gt; Listco[Listco]   X -- "30%" --&gt; CompanyA[Company A]   Listco -- "40%" --&gt; CompanyB[Company B]   CompanyA -- "15%" --&gt; CompanyB   style X fill:#ffff00   style CompanyB fill:#cccccc </pre>	<p>Yes, because Company B is a 30%-controlled company of Mr. X, and it is not exempt under Rule 14A.14 as Company A (being Mr. X's associate) has an interest in Company B of more than 10%.</p>
6.	14A.14	20.12	<p>Is Company D as an associate of Mr. X in the following scenario?</p>  <pre> graph TD   X[X] -- "&gt; 50%" --&gt; Listco[Listco]   X -- "15%" --&gt; CompanyC[Company C]   Listco -- "45%" --&gt; CompanyD[Company D]   CompanyC -- "55%" --&gt; CompanyD   style X fill:#ffff00   style CompanyD fill:#cccccc </pre>	<p>No. The exemption under Rule 14A.14 applies in this case because:</p> <ul style="list-style-type: none"> <li>(i) Mr. X's 45% interest in Company D is held through Listco; and</li> <li>(ii) Company C is not an associate of Mr. X. Neither Mr. X nor any of his associates has a direct interest in Company D.</li> </ul>

No.	Main Board Rules	GEM Rules	Query	Response
<b>Definition of connected transaction</b>				
7.	14A.06(27) 14A.24(2)(a)	20.06(27) 20.22(2)(a)	<p>Under the non-competition agreement between Listco and its controlling shareholder, Listco has been granted a right of first refusal to acquire certain assets from the controlling shareholder at a price and on terms to be negotiated between the parties.</p> <p>If Listco decides not to exercise the “right of first refusal” when the controlling shareholder proposes to sell the assets, will it be regarded as non-exercise of an option and subject to the connected transaction requirements?</p>	<p>Given that the terms of the acquisition are subject to further negotiation between the parties, the right of first refusal does not constitute an option under Rule 14A.06(27). Therefore, non-exercise of the right of first refusal by Listco does not constitute a non-exercise of an option.</p>
8.	14A.24(2)	20.22(2)	<p>Listco has been granted an option to acquire a coal mine from its controlling shareholder within a period of three years from the date of grant.</p> <p>(a) Under the option agreement, the option will be terminated if the mining license</p>	<p>(a) No. Since the termination of the option is made under the term of the agreement and Listco has no discretion over the termination, it does not constitute a transaction under Note to Rule 14A.24(2)(a).</p> <p>(b) Yes. As Listco decides not to exercise the option, it must classify the transaction under Rule 14A.79(4)</p>

No.	Main Board Rules	GEM Rules	Query	Response
			<p>cannot be obtained within 12 months from the date of the agreement. Will such termination constitute a connected transaction for Listco?</p> <p>(b) If Listco allows the option to lapse upon expiry of the option period (and the mining license was obtained), will this constitute a connected transaction for Listco?</p>	<p>and comply with the applicable announcement and shareholder approval requirements before expiry of the option period.</p>
<b>Transactions with connected persons</b>				
9.	14A.24(4), 14A.25	20.22(4), 20.23	<p>A wholly owned subsidiary of Listco proposes to obtain a bank loan which will be guaranteed by Listco's substantial shareholder on normal commercial terms. No security over the assets of Listco's group will be provided for the guarantee.</p> <p>Listco has agreed to indemnify the substantial shareholder for the loan guaranteed by it. Does the provision of the</p>	<p>No. The indemnity is a financial assistance provided by Listco in favour of its wholly owned subsidiary, and is not a connected transaction.</p>

No.	Main Board Rules	GEM Rules	Query	Response
			indemnity constitute a connected transaction for Listco?	
10.	14A.24(4), 14A.25	20.24(4), 20.23	<p>Subsidiary X is owned as to 90% by Listco and 10% by Mr. A who is a connected person at the subsidiary level.</p> <p>Listco has agreed to provide a guarantee for the full amount of a loan facility granted by a bank to Subsidiary X. Will it be regarded as provision of financial assistance to Mr. A on the basis that he is not required to provide any guarantee for the loan facility in proportion to his interest in Subsidiary X?</p>	No. The guarantee is provided by Listco for the benefit of Subsidiary X. It is not regarded as provision of financial assistance to Mr. A.
11.	14A.25	20.23	Listco has entered into an agreement to acquire a target company from Company A. Listco has also entered into an agreement with Company A for purchase of raw materials at the then market prices from time to time for a 3-year period after the completion of the acquisition.	Yes, as the terms are not fixed at the time Company A is an independent third party, Listco must comply with all applicable announcement, reporting, annual review and shareholder approval requirements in relation to the agreement for the purchase transactions.

No.	Main Board Rules	GEM Rules	Query	Response
			<p>Company A is an independent third party at the time of entering into the above agreements, but it will become a substantial shareholder of Listco by receiving consideration shares issued by Listco to it upon completion of the acquisition of the target company.</p> <p>Will the purchase of raw materials from Company A constitute a connected transaction?</p>	
<b>When a continuing transaction subsequently becomes connected</b>				
12.	14A.60	20.58	<p>Rule 14A.60 applies where the issuer has entered into an agreement with fixed terms for a continuing transaction.</p> <p>Please clarify the meaning of</p> <p>(a) an agreement with fixed terms; and</p> <p>(b) a framework agreement.</p>	<p>(a) An agreement with fixed terms refers to an agreement which sets out the specific terms for a continuing connected transaction, including the actual or per unit consideration in monetary terms, or a fixed formula for determining the consideration, or specific reference prices (e.g. prices prescribed by government or commodity prices quoted on an exchange) which form the basis of the consideration</p>



No.	Main Board Rules	GEM Rules	Query	Response
				<p>and where the volume transacted (e.g. number of units) is fixed.</p> <p>(b) A framework agreement refers to an agreement which sets out the framework within which a series of continuing connected transactions are to be conducted over a period. The actual terms of each transaction would be negotiated on a per transaction bases. The consideration for individual transactions may be subject to pricing guidelines or based on a range of parameters. Some of these agreements provide that the individual transaction will be conducted at market prices or the terms of individual transactions will be negotiated on an arm's length basis.</p>
<b>De minimis exemptions</b>				
13.	14A.76(1), 14A.76(2) 14A.90	20.74(1), 20.74(2), 20.88	An issuer proposes to obtain a loan from its controlling shareholder on normal commercial terms. Since the loan will be secured by certain assets of the issuer, it is not exempt under Rule 14A.90.	The issuer may apply the de minimis exemption. It should compute the assets ratio and consideration ratio based on the principal amount of the loan and the revenue ratio based on the annual interests payable to its controlling shareholder. Given the loan is to be secured by the issuer's assets, the issuer should also

No.	Main Board Rules	GEM Rules	Query	Response
			Can the issuer apply the de minimis exemptions to the above transaction? If yes, how should the issuer compute the size tests for classifying the transaction?	compute the asset ratio and consideration ratio based on the value of the assets and also the revenue ratio based on any identifiable revenue stream generated from the assets.
<b>Connected transactions involving options</b>				
14.	14A.79(4)(b)	20.77(4)(b)	<p>An issuer is allowed to adopt the new alternative tests under Rule 14A.79(4)(b) for classifying transfer or termination or non-exercise of options if an asset valuation is provided by an independent expert using generally acceptable methodologies.</p> <p>(a) Does an issuer have to seek the Exchange’s prior consent to adoption of the alternative tests under Rule 14A.79(4)(b) ?</p> <p>(b) Please clarify what are “generally acceptable methodologies” referred to in Rule 14A.79(4)(b) and who is qualified to provide such asset valuation.</p>	<p>(a) Yes.</p> <p>(b) The valuation should follow the valuation standards that are widely used by professional asset/business valuers in the market and the valuer must be regulated by a recognised professional body. Examples of acceptable valuation standards include International Valuation Standards, Hong Kong Institute of Surveyor Valuation Standards on Trade-related Business Assets and Business Enterprise, The Hong Kong Business Valuation Forum Business Valuation Standards.</p>

No.	Main Board Rules	GEM Rules	Query	Response
<b>Aggregation of transactions</b>				
15.	14A.09, 14A.81	20.08, 20.79	<p>A few months ago, Listco entered into a one-off transaction with Mr. A (the Previous Transaction) who at that time qualified for the insignificant subsidiary exemption.</p> <p>Mr. A is recently appointed as a director of Listco and no longer qualifies for the insignificant subsidiary exemption. When Listco enters into a new transaction with Mr. A, will it need to aggregate the proposed transaction with the Previous Transaction for the purpose of the connected transaction Rules?</p>	No, because the Previous Transaction was not a connected transaction for Listco.
<b>Financial assistance</b>				
16.	14A.76, 14A.87	20.74, 20.85	Does the de minimis exemption under Rule 14A.87 apply to financial assistance provided by an issuer or its subsidiary which is not a banking company?	Rule 14A.87 applies to banking companies only. For an issuer which is a non-banking company, it may apply the de minimis exemption under Rule 14A.76 if the financial assistance is provided to connected person on normal commercial terms and falls within the de

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				minimis threshold.
17.	14A.89	20.87	<p>Company A is 60% owned by Listco and 40% by Listco's controlling shareholder.</p> <p>Company A has obtained a bank facility for which Listco has provided a full guarantee in favour of the bank (the "Bank Guarantee"). As Company A is a connected subsidiary of Listco, the provision of the Bank Guarantee constitutes a connected transaction for Listco.</p> <p>Can Listco apply the exemption under Rule 14A.89 if Listco's controlling shareholder has agreed to a counter-guarantee to Listco for 40% of the outstanding loan balance drawn by Company A under the bank facility?</p>	No. The exemption under Rule 14A.89 applies only if the guarantee provided by Listco is in proportion to its interest in Company A and on a several basis.
<b>Directors' indemnity/ insurance/ service contracts</b>				
18.	14A.91	20.89	(1) Does the new exemption for providing directors' indemnity apply if the indemnity relates to the director's	(1) No, because provision of indemnity that relates to such director's liabilities is not allowed under the Hong Kong Companies Ordinance.

No.	Main Board Rules	GEM Rules	Query	Response
			<p>liabilities to third parties in connection with negligence, default and breach of duty by directors?</p> <p>(2) What if the indemnity covers directors' liabilities which are not limited to those arising from his proper discharge of duties?</p>	<p>(2) No, because the indemnity does not meet all the conditions set out in the Rule.</p>
19.	14A.91, 14A.95, 14A.96	20.89, 20.93, 20.94	<p>If a director's service contract covers provision of indemnity or purchase of insurance which is not exempt under Rules 14A.91 and 14A.96, can the issuer apply the directors' service contract exemption under Rule 14A.95?</p>	<p>No.</p>
20.	14A.95	20.93	<p>Mr. A is a director of Listco. Under his director service contract, he may be entitled to receive share awards to be granted under Listco's share award scheme.</p> <p>Can Listco apply the directors' service</p>	<p>No. Transactions or arrangements involving issuance of new shares by a listed issuer to its connected persons are exempt from the connected transaction Rules only if they fall under the circumstances described in Rule 14A.92. Therefore, the grant of share awards in form of new shares to Mr. A will be subject to the</p>

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			contract exemption under Rule 14A.95 if the share awards are granted to Mr. A in form of new shares of Listco?	announcement, reporting and shareholder approval requirements under Chapter 14A.
21.	14A.96	20.94	<p>Listco proposes to purchase insurance for Mr. A against liabilities to third party that may be incurred in the course of performing his duties as a director of Listco as well as the manager of certain subsidiaries of Listco.</p> <p>Does the new exemption for purchasing directors' insurance apply to the above insurance arrangement?</p>	Yes, provided that the arrangement is in the form permitted under the laws of Hong Kong and Listco's place of incorporation.
<b>Transactions with associate of passive investor</b>				
22.	14A.99	20.97	<p>To qualify for the "passive investor" exemption, the passive investor must not have any representatives on the board of directors of the issuer or its subsidiaries.</p> <p>Can the passive investor have any board seat(s) at an insignificant subsidiary of the</p>	No.

No.	Main Board Rules	GEM Rules	Query	Response
			issuer?	
<b>Waiver for provision of guarantees to connected subsidiaries or commonly held entities for public sector contracts awarded by tender</b>				
23.	14A.104	20.102	<p>An issuer proposes to provide a guarantee to a third party creditor for the obligations of a connected subsidiary under a government contract awarded by tender.</p> <p>While the other shareholders of the connected subsidiary will not give a similar guarantee to the creditor, they agree to provide a counter-indemnity to the issuer in proportion to their interest in the subsidiary.</p> <p>Does the issuer qualify for applying the waiver under Rule 14A.104?</p>	No. Rule 14A.104 only applies if the issuer can meet all the three conditions under the Rule. In this case, the issuer fails to meet the condition that the other shareholders of the connected subsidiary must also give similar joint and several guarantee to the creditor.
<b>Transitional arrangements for Rule amendments</b>				
24.	14A.09, 14A.12(1)(a), 14A.14, 14A.28, 14A.76(1)(c),	20.08, 20.10(1)(a), 20.12, 20.26, 20.74(1)(c),	Before the Rule amendments becoming effective, Listco has entered into an agreement for certain connected transactions (one off or continuing), which is subject to all or some of the connected transaction	No. Listco should comply with the connected transaction requirements applicable at the time of entering into the agreement. We may consider waivers from the shareholder approval requirement.

No.	Main Board Rules	GEM Rules	Query	Response
	14A.96, 14A.97, 14A.101	20.94, 20.95, 20.99	<p>requirements.</p> <p>Can Listco apply the new/revised Rules to exempt the transactions from the announcement, circular and/or shareholders' approval requirements if it meets all the exemption conditions under the relevant new/revised Rules?</p>	
25.	14A.12(1)(a), 14A.14, 14A.76(1)(c), 14A.96, 14A.97	20.10(1)(a), 20.12, 20.74(1)(c), 20.94, 20.95	<p>Before the Rule amendments becoming effective, Listco has entered into an agreement for certain continuing connected transactions, and has complied with the announcement, circular and/or shareholders' approval requirements applicable to the agreement.</p> <p>Can Listco apply the new/revised Rules to the continuing connected transactions to be conducted under the agreement after Rule amendments?</p>	<p>Yes if the transactions to be conducted under the agreement after the Rule amendments can meet all the exemption conditions under the relevant new/revised Rules (e.g. the transactions have a total value of less than HK\$3 million which are therefore fully exempt under the revised Rules). Listco may announce that it will apply the exemption to these transactions, and the reporting or annual review of the transactions will not be required in the next annual report(s).</p>



No.	Main Board Rules	GEM Rules	Query	Response
26.	14A.56	20.54	Before the Rule amendments becoming effective, will the Exchange accept auditors' confirmation for annual review of continuing connected transactions prepared using the wording provided in Practice Note 740 issued by the Hong Kong Institute of Certified Public Accountants?	Yes. The amendment is only a codification of existing practice.