



Hong Kong

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## HKEX PUBLISHES LISTING DECISIONS ON REASONS FOR REJECTION AND RETURN OF NEW LISTING APPLICATIONS

On 13 April 2016, the Stock Exchange of Hong Kong Limited (**the Exchange**), a wholly-owned subsidiary of the Hong Kong Exchanges and Clearing Limited (**HKEx**), published two new Listing Decisions.

Listing Decision HKEX-LD100-2016<sup>1</sup> sets out the Exchange's reasons for rejecting seven of the nine listing applications rejected in 2015, while Listing Decision HKEX-LD101-2016<sup>2</sup> sets out the reasons for the return of the three listing applications returned in 2015.

Since October 2013, when the Listing Rules and related guidance on the new sponsor regime were introduced, the Exchange has noticed that the vetting process of new listing applications has been more efficient and applications have been presented to the Listing Committee within a shorter timeframe. Applicants that were found to be ineligible or unsuitable for listing were also identified and rejected more quickly under the new regime.

### *The rejection cases in 2015*

Company	Main Board / GEM	Reasons for Rejection
1	Main Board	The company was a mining company whose principal operations and assets were in a high risk jurisdiction.

### **Reasons for Rejection of Listing Applicants: Listing Decision HKEX-LD100-2016**

This Listing Decision considers seven companies which sought to list on the Main Board and Growth Enterprise Market (**GEM**) and were rejected by the Exchange in 2015.

Pursuant to Chapter 8 of the Main Board Listing Rules (**MBLR**) and Chapter 11 of the GEM Rules (**GLR**), new applicants must satisfy detailed eligibility requirements including a requirement that both the applicant and its business must be suitable for listing in the opinion of the Exchange.

Suitability for listing depends on many factors (MBLR 2.06 and GLR 20.09). Compliance with the Listing Rules' qualification requirements may not be enough to ensure an applicant's suitability for listing. Reference should be made to Guidance Letter HKEX-GL68-13 which sets out guidance on factors the Exchange takes into account when assessing suitability.

<sup>1</sup> [http://en-rules.hkex.com.hk/net\\_file\\_store/new\\_rulebooks//d/ld100-2016.pdf](http://en-rules.hkex.com.hk/net_file_store/new_rulebooks//d/ld100-2016.pdf)

<sup>2</sup> [http://en-rules.hkex.com.hk/net\\_file\\_store/new\\_rulebooks//d/ld101-2016.pdf](http://en-rules.hkex.com.hk/net_file_store/new_rulebooks//d/ld101-2016.pdf)

		<p>The legal and political uncertainties in the company's principal location which also had a high Corruption Perceptions Index<sup>3</sup> gave rise to concerns as to whether the company would be able to carry out its business in a viable manner and retain ownership of its assets. There was also an issue relating to a pending renewal of an exploration licence which had resulted in mining projects ceasing operating after the track record period.</p>
2	Main Board	<p>The company was involved in a gambling-related venture, receiving income from casino operators for introducing VIP players to designated VIP rooms at casino operators' venues. The VIP players were sourced and introduced by junket agents who were paid commission by the company.</p> <p>The Exchange rejected the application on the basis of failure to meet the suitability requirement, for the following reasons:</p> <p>a. <u>Deteriorating financial performance</u></p> <p>The Exchange considered that the company's deteriorating financial performance during the track record period was unlikely to be short-term given the outlook for the industry and high competition.</p> <p>b. <u>Questionable payments to a connected person</u></p> <p>The Exchange had concerns over the completeness, accuracy and genuineness of the lump sum service fees paid to a connected person which represented a material portion of the company's selling, general and administrative expenses during the track record.</p> <p>c. <u>Track record results not representative of future performance</u></p> <p>The Exchange had concerns that the company's track record results were not representative of its future performance due to material changes made to its revenue model since the third quarter of the second year of the track record period.</p>
3	Main Board	<p>The company provided services in the construction industry.</p> <p>The Exchange rejected the application due to:</p> <p>a. <u>Material Impact Non-compliances</u></p> <p>During the track record period, the company undertook projects which exceeded its permitted scope and the company's main operating subsidiaries failed to comply with the work safety licence requirement until shortly before the date of listing application (collectively, the <b>Material Impact Non-compliant Business</b>);</p> <p>b. <u>Failure to satisfy MBLR 8.05(1)</u></p> <p>The company could not demonstrate that it could meet the minimum profit requirement after exclusion of the profit contributed by the Material Impact Non-compliant Business.</p>

<sup>3</sup> The Corruption Perceptions Index is prepared by Transparency International, the global civil society organisation leading the fight against corruption. It ranks countries according to their perceived levels of public-sector corruption in relation to the bribery of public officials, kickbacks in public procurement, embezzlement of public funds, and questions that probe the strength and effectiveness of public sector anti-corruption efforts.

		<p>c. <u>Directors' suitability</u></p> <p>Despite the directors' awareness of the breaches of the company's permitted scope of activity before the track record period, the company continued to enter into new contracts with contract values exceeding the permitted scope during the track record period. The directors were also aware that the company was in breach of the work safety licence requirement, but the company continued to carry on its business without the work safety licences for most of its track record period. The company and its sponsor failed to satisfy the Exchange that the directors met the requirements for integrity, competence and skill, care and diligence under Main Board Rules 3.08 and 3.09.</p>
4	Main Board	<p>The company was a mining company which began commercial production of a mine in 2014, and recorded immaterial revenue in 2014 and in the first half of 2015. The company applied for a waiver from strict compliance with the requirements of Main Board 8.05 under Main Board Rule 18.04.</p> <p>The Exchange rejected the application on the basis that the company failed to satisfy Main Board Rule 8.05(1). The company was not qualified for the waiver under Main Board Rule 18.04 as it failed to demonstrate that the mine had a clear path to commercial production and a demonstrable path to profitability.</p>
5	Main Board	<p>The company was a property investment company.</p> <p>The Exchange rejected the application based on the totality of the following factors:</p> <p>a. <u>No track record of existing business structure</u></p> <p>The company did not have a track record of its structure to provide comfort on the effectiveness of its internal controls, management and operational systems. There were also questions as to the company's ability to comply with the management continuity requirement for the track record period.</p> <p>b. <u>Extreme reliance on fair value gains to meet profit requirement</u></p> <p>The company relied on fair value gains from investment properties for more than 80% of its net profit during the track record period. While reliance on fair value gains does not per se render an applicant engaged in a property business unsuitable for listing (see paragraph 3.2(7) of Guidance Letter HKEx-GL68-13), in this case the degree of reliance was considered extreme.</p> <p>c. <u>Deteriorating financial performance</u></p> <p>There was significant deterioration in the company's financial performance after the track record period due to the poor market outlook and increased finance costs and operating expenses. The company's forecast indicated that the downward trend would continue after listing and that the company would continue to rely heavily on fair value gains rather than actual business operations. The Exchange was of the view that the company did not satisfactorily demonstrate that its business was sustainable.</p>

6	GEM	<p>The company was an exhibition organiser.</p> <p>The application was rejected on the basis that one of the company's directors (<b>Director A</b>) was considered unsuitable under GEM Rules 5.01 and 5.02. The director in question had failed to fulfil his fiduciary duties to act in good faith in the interests of the company in respect of two advances to third parties made by the company's subsidiaries at his instruction. The advances exposed the company to significant credit risk and were in violation of relevant laws and regulations. The director also failed to notify the company's subsidiaries of partial repayments received by him and deposited into his personal account. As a result of his failure to disclose such information, there were material misstatements in the company group's audited accounts.</p> <p>The company also failed to comply with relevant laws and regulations in six instances related to its core business during the track record period. These systemic non-compliances were of a serious nature and raised concerns as to whether the company's directors (including Director A) were suitable to act as directors. The company also failed to enhance its internal controls to prevent reoccurrence of the systematic non-compliances until the Exchange commented on them. The Exchange therefore considered that the enhanced internal controls had not been tested for effectiveness.</p>
7	GEM	<p>The company provided printing services.</p> <p>The application was rejected due to concerns as to the sustainability of the company's business, primarily due to its loss of its largest customer to a competitor after the track record period. The Exchange was of the view that the company's deteriorating financial performance combined with intense competition and the loss of their top customer meant that the company's profit forecast could not be substantiated. Further, the company planned to use more than 90% of its net IPO proceeds to acquire new machines for its business, despite the fact that the utilisation rates of its existing machines were between 46% and 55% during the track record period. The Exchange considered that the resulting additional depreciation charges and related additional fixed costs (staff and maintenance etc.) would further negatively impact the company's future profitability.</p>

## Reasons for Return of Listing Applications: Listing Decision HKEX-LD101-2016

This Listing Decision sets out the reasons for the return of three listing applications in 2015.

Pursuant to MBLR 9.03(3) and GLR 12.09(1), an applicant is required to submit a listing application form, an Application Proof and all other relevant documents under MBLR 9.10A(1) and GEM Rules 12.22 and 12.23. The information provided must be substantially complete except in relation to information that by its nature can only be finalised and incorporated at a later date.

Where the Exchange considers that the information provided is not substantially complete, it will return the application to the sponsor (although a copy is retained for the Exchange's records).

*The returned cases in 2015*

The Exchange returned three applications in 2015.

Company	Main Board / GEM	Reasons for Return
1	Main Board	<p>The company provided financial services.</p> <p>The application was returned due to omission of material information regarding loans guaranteed by connected persons.</p> <p>The company initially stated in its Application Proof that neither it nor its related parties had guaranteed any loan granted to its independent customers during the track record period. The company only revised its draft listing document to disclose that connected persons had provided guarantees for loans to independent customers after the Exchange's comments. The loans accounted for 3.5% to 11.1% of the total amount of loans granted during the track record period.</p> <p>In the view of the Exchange, transactions involving connected persons should be subject to a higher level of scrutiny because they have the potential to significantly influence the management or decisions of the applicant.</p> <p>The Exchange emphasises that material information does not necessarily require the amount involved to be large.</p> <p>The Exchange was also concerned about the effectiveness of the company's corporate governance as there was no guarantee agreement between the company and the connected persons, while the company had entered into guarantee agreements with the non-connected persons.</p>
2	GEM	<p>The company provided conferencing services.</p> <p>The application was returned due to the omission of the following material information in the Application Proof in relation to a company director, who was also its chairman and controlling shareholder:</p> <ul style="list-style-type: none"> <li>• a compulsory winding up order granted by the court against a company of which the director was an executive director and a minority shareholder; and</li> <li>• the director was also a director of two Hong Kong listed companies which had failed to comply with the Listing Rules during his tenure.</li> </ul> <p>The Exchange considered that these omissions were material because the information related to the integrity, character and competency of the director.</p>

3	GEM	<p>The company operates in the catering business.</p> <p>The application was returned because the company failed to provide, when filing its Form 5A, a profit forecast memorandum covering the period up to the year ending [year T + 1] as required under GLR 12.22(14b).</p> <p>Where an application proof does not contain a profit forecast, an applicant is required to provide a final or an advanced draft of a profit forecast memorandum covering the period up to the next financial year end date after the listing and a cash flow forecast memorandum covering at least 12 months from the expected date of publication of the listing document.</p> <p>The application was returned because the company failed to provide the required information to the requisite dates. The profit forecast memorandum only covered the year ending [year T].</p>
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