

HKEx LISTING DECISION
Cite as HKEx-LD43-1 (First Quarter of 2005)

Summary	
Name of Parties	Parentco - the holding company of Company A, a Main Board listed issuer Company A- a Main Board listing applicant being spun off by Parentco
Subject	Whether in a case where Parentco had a public float approaching 50% of its equity capital, it was appropriate to grant a permanent waiver to Company A in respect of the minimum public float requirement of 25%?
Listing Rules	Listing Rule 8.08(1)(a) and (d); and Note (2)(b) to Listing Rule 8.08
Decision	The Exchange determined that there were no justifiable grounds for exercising its discretion to grant permanent relief from the minimum public float requirements of 25% in favour of Company A. The Exchange, however, determined to grant temporary relief under Note (2)(b) to Listing Rule 8.08 on the undertaking of Company A and its controlling shareholder to restore the required 25% public float level within eighteen months of Company A's listing.

SUMMARY OF FACTS

1. The listing application of Company A followed a spin-off application initiated by its controlling shareholder, Parentco. Parentco had a public float approaching 50% of its equity capital. The spin-off constituted a major transaction for Parentco requiring prior approval by the shareholders of Parentco.
2. Company A applied to the Exchange for a permanent waiver of the minimum public float requirement of 25% under Rule 8.08 and to allow Company A to maintain a minimum public float of 15% instead. The remaining 85% would be held by Parentco upon listing. The expected market capitalisation of Company A's shares upon listing was above the minimum market capitalisation set forth in Listing Rule 8.08 allowing the Exchange to exercise discretion to reduce the required minimum public float level.

3. Company A explained that the net proceeds to be raised from the public offering (both in Hong Kong and overseas) would be sufficient for the present requirements of Company A. Company A believed that to raise capital in excess of its current requirement for the sake of complying with the minimum public float requirement might have an adverse impact on shareholder value and, therefore, was not in the best interest of Company A. Parentco also considered it to be inappropriate to take any action to reduce its shareholding in Company A to below 85% by declaring a dividend in specie of shares of Company A held by Parentco.
4. It was submitted that given the absolute number of securities concerned and their widespread distribution, a lower percentage than that required under Listing Rule 8.08(1) would still enable the market to operate properly. In this regard, the sponsor submitted that:-
 - a. the market capitalisation of Company A's shares would be in excess of HK\$10 billion as required under 8.08(1)(d). Arguably, an inference could be made that a waiver should be granted to a company if its market capitalisation exceeded this level;
 - b. given the size of the offering, the expected dollar value of the proposed 15% public float of Company A would facilitate a far more open market than a great majority of other Main Board listed companies with public floats of 25% or more. Furthermore, if the recent daily turnover ratio level of the predecessor company could be relied on as a guide, it would require more than 40 days for all the public float shares to be transacted once. In view of the above, a reasonably liquid market for the shares could be maintained;
 - c. Company A intended to seek opportunities to expand. These would involve further issues of shares either to raise capital to fund expansion, or as consideration for future acquisitions which would thereby increase its public float to above 25% in the course of time;
 - d. the allocation of Company A's shares would require compliance with Practice Note 18 and this would result in a sufficient portion of securities to be offered in Hong Kong; and
 - e. the particular circumstances of the present share offering suggested that there would not be an undue concentration of shares in the public float. These circumstantial factors included preferential offers to existing shareholders of Parentco and employees of the Group and a worldwide distribution network that stimulated a strong yet dispersed shareholder subscription base.

THE ISSUE RAISED FOR CONSIDERATION

5. Whether in a case where Parentco had a public float approaching 50% of its equity capital, it was appropriate to grant a permanent waiver to Company A in respect of the minimum public float requirement of 25%?

APPLICABLE LISTING RULES OR PRINCIPLE

6. Listing Rule 8.08(1) (a) and (d) provide that:

‘There must be an open market in the securities for which listing is sought. This will normally mean that:-

- (1) (a) *at least 25% of the issuer’s total issued share capital must at all times be held by the public.*
- (b) *...*
- (c) *...*
- (d) *The Exchange may, at its discretion, accept a lower percentage of between 15% and 25% in the case of issuers with an expected market capitalisation at the time of listing of over HK\$10,000,000,000, where it is satisfied that the number of securities concerned and the extent of their distribution would enable the market to operate properly with a lower percentage, and on condition that the issuer will make appropriate disclosure of the lower prescribed percentage of public float in the initial listing document and confirm sufficiency of public float in successive annual reports after listing...’*

7. Note (2)(b) to 8.08 provides that where the public float percentage has fallen below the minimum, the Exchange may refrain from suspension if the Exchange is satisfied that there remains an open market in the securities and if (not exhaustively):

‘the issuer and the controlling shareholder(s) or single largest shareholder undertake to the Exchange to take appropriate steps to ensure restoration of the minimum percentage of securities to public hands with a specified period which is acceptable to the Exchange.’

THE ANALYSIS

8. *The Consultation Paper On Proposed Amendments To The Listing Rules Relating To Initial Listing And Continuing Listing Eligibility And Cancellation Of Listing Procedures* issued by the Exchange in July 2002 mentioned that *‘the level of public float may have implications for minority shareholders’ protection.... For*

good corporate governance and shareholders' protection, we consider that the floor with regard to the minimum percentage of public float that the Exchange....can grant should be raised'. In the Consultation Conclusion of the said Consultation Paper, the Exchange considered it appropriate to raise the threshold of the minimum percentage of public float that the Exchange may grant to not less than 15%. The Exchange proposed to codify the then practice to require a minimum market capitalisation of HK\$10 billion. As a safeguard to protect the interests of minority shareholders, the Exchange proposed that there should be appropriate disclosure in the prospectus of the lower public float percentage and future annual reports. All these proposals have been adopted and incorporated in the current Listing Rule 8.08(1)(d).

9. The Exchange considered that eligibility for a grant of waiver under Listing Rule 8.08(1)(d) did not imply that an issuer with a market capitalisation greater than HK\$10 billion would be automatically granted a lower percentage public float. On the contrary, Listing Rule 8.08(1)(d) specifies that the Exchange will accept a lower percentage 'at its discretion'.
10. When exercising a discretion to grant waivers under the Listing Rules, it is the established practice of the Exchange to give due consideration to all relevant facts and circumstances. In light of the plain meaning of the general provisions of Listing Rule 8.08 and the statements made in the Consultation Paper issued in July 2002, the Exchange determined that Listing Rule 8.08(1)(d) should be interpreted to require an applicant to demonstrate:-
 - a. a reasonable basis for concluding that an open market for the securities in question can be maintained with the lower percentage public float; and
 - b. that such market can be maintained for a reasonable period of time after the time of permitting such lower public float.
11. In considering the present case, the Exchange was of the view that the measure of what constitutes an open market must be taken both in absolute terms, based on appropriate analysis of quantitative factors, and in relative terms, giving appropriate weight to qualitative factors specific to the applicant's history and the market sector in which it operates.
12. While accepting that Parentco had operated as a responsible corporate enterprise listed on the Main Board, the Exchange noted the following factors weighing against accepting a lower public float:-
 - a. in light of the nature of the spin-off in this case, the Exchange was of the view that Parentco as the controlling shareholder was in a position to ensure full compliance with the public float requirements and therefore should use its best endeavours to comply with the Listing Rules whenever

possible. Indications to the contrary without good reasons should weigh against the exercise of discretion by the Exchange;

- b. the spin-off transaction would cause a substantial reduction of the currently existing public float and the transaction was fundamentally voluntary; and
 - c. Company A had a relatively small market capitalisation as compared to the cases previously considered by the Exchange where a lower public float had been allowed.
13. Based on the material facts and analysis above, the Exchange determined that Company A had not established a reasonable basis for concluding that an open market for the securities in question could be maintained with the lower percentage public float. In particular, the Exchange gave significant weight to the recent trading history and public float level of the predecessor company with operations substantially similar to that of Company A. Given the relatively high degree of change in the public float level as compared to recent levels experienced by Parentco as well as other factors weighing against the exercise of discretion under Listing Rule 8.08(1)(d), the Exchange was of the view that there were no justifiable grounds to grant permanent relief from the requirements of Listing Rule 8.08(1)(a) in this case.
14. However, the Exchange considered it acceptable to allow Company A to proceed with the listing of its shares at the requested not less than 15% public float on the strength of the undertaking by Company A and the controlling shareholders to the Exchange that they would take appropriate steps to ensure restoration of the minimum percentage of securities to public hands within a specified period acceptable to the Exchange. Such temporary relief is specifically contemplated by Note (2)(b) to Listing Rule 8.08.
15. In determining the appropriate length of time for the restoration of the required minimum public float level under Listing Rule 8.08, the Exchange took into account that, as required by Listing Rule 10.07, Parentco would not be allowed to dispose any shares in Company A in the first six months after being listed on the Main Board and that, under Listing Rule 10.08, Company A would not be allowed to issue new shares within the first six months of listing.

THE DECISION

16. Based on the facts and circumstances of the case and the Exchange's analysis of the Listing Rules, the Exchange considered it inappropriate to grant permanent relief from the requirements of Listing Rule 8.08(1)(a) to Company A in this case.

17. However, the Exchange considered it appropriate to grant temporary relief to Company A upon its listing to allow the percentage of public float level to fall below the minimum as required by Listing Rule 8.08 on the undertaking of Company A and Parentco that they would take appropriate steps to ensure restoration of the minimum percentage of securities to public hands within eighteen months of Company A's listing.