

TOPIC 4 - OVERVIEW

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1. CONVERTIBLE BONDS

- All proposed convertible debt issues must be **approved by the SEHK** prior to issue and are subject to the Main Board Listing Rules and the GEM Listing Rules
- Convertible bonds (other than those issued by a state or supranational) convertible into **equity securities** will only be considered for admission if the equity securities are:
 - A class of listed equity securities; or
 - A class of equity securities listed or dealt in on a stock market recognized by the SEHK
- Convertible bonds can be listed in other circumstances as long as **holders have access to the necessary information** to form an opinion on the **value of the underlying equity securities**
- Bonds (other than those issued by a state or supranational) convertible into property other than equity securities, may be listed as long as **holders have access to the necessary information** to form an opinion on the **value of the underlying property**
- An issuer must publish an announcement as soon as practicable on any change in the rights
 - Attached to any class of listed securities
 - Attaching to any shares into which any listed debt securities are convertible/exchangeable
- Convertible bonds converted into ordinary shares will **dilute the holding of existing shareholders** of a listed issuer and may affect the financial profile of the issuer. Accordingly, a proposed issue of convertible bonds **can constitute inside information** requiring appropriate disclosure as per the SFO
- Convertible bonds are normally listed on an exchange to obtain listing status, thus permitting **investors subject to investment restrictions** (institutions and funds) to invest in them. Often called a **listing of convenience**

2. RIGHTS ISSUES

- The offer of a right to existing shareholders allowing them to subscribe for additional securities in proportion to their existing holdings, usually at a discount to the market price
- There is a **concern** that the holding of minority shareholders may be diluted as they are less likely to have the funds available to take up their rights

2.1 Underwriting Normally Required

- Underwriting **provides a degree of certainty** to an issuer and potential investors through the commitment of sound financial institutions, enabling an issuer to plan on the basis of assured funds
- Underwriting of rights issues applies to both Main Board and GEM
- The underwriter must either be:
 - Licensed/registered for Type 1 activity (Dealing in securities)
 - The controlling or substantial shareholders of the issuer
- Where the underwriter of a rights issue can terminate the underwriting on the occurrence of a **force majeure event***, the listing document must contain details of the fact. Such disclosure must:
 - Appear prominently on the front cover of the listing document
 - Include a summary of the force majeure clause(s)
 - State that there are risks in dealing in such rights
 - Be in a form approved by the SEHK
- * An event that is **unexpected or extraordinary**, outside the control of the parties, which gives one party the contractual right to terminate (eg wars, terrorism, natural disasters)
- If the underwriter's ordinary course of business is not underwriting, this fact must be fully disclosed in the listing document

2.2 Non-underwritten Issues

- Where a rights issue is proposed without being fully underwritten, the **SEHK needs to be consulted** at an early stage. The following will need to be disclosed on the **front cover of the listing document**:
 - The fact that the issue is not fully underwritten
 - Any minimum amount to be raised for the issue to proceed
- Listing document will need to state:
 - Intended use of net proceeds of issue according to level of subscriptions
 - Whether each substantial shareholder has taken up entitlement in full or in part

- Listing documents for non-underwritten issues must disclose:
 - Non-underwritten nature of offer disclosed on front cover of listing document
 - Minimum amount required to be raised for issue to proceed
 - Intended use of net proceeds
 - If each substantial shareholder has undertaken to take up entitlement

2.3 Procedural Requirements

- If a proposed rights issue would increase either issued share capital or market cap of issuer by more than 50%, then
 - Rights issue must be approved by minority shareholders
 - A circular shall be sent out to shareholders explaining purpose and proposed use of issue proceeds
 - SEHK may require issue to be fully underwritten
- Any rights issue **proposed within 12 months of a new issuer first listing** on the SEHK must be approved by minority shareholders
- A rights offer is usually made with a negotiable instrument, such as a **renounceable provisional letter of allotment**
- The negotiable instrument should state the time within which the offer may be accepted – a **minimum of 10 days**, and can be longer if there are a large number of overseas members. SEHK must be consulted if acceptance period is to be more than 15 days
- If there are unsubscribed securities in a rights issue, the issuer may:
 - Make such securities available for subscription by all shareholders and allocated on a fair basis; or
 - Dispose of securities in the market for the benefit of the people to whom they were offered by way of rights
- A rights issue must be supported by a **listing document**, which must comply with the relevant provisions of the Listing Rules

3. SHARE OPTIONS

- A share option scheme (Scheme) involves a listed issuer **granting options over new shares** to, or for the benefit of, specified participants of a Scheme
- Schemes are governed by the MBLR
- Schemes have been **of concern to the SEHK** because of potential abuse over granting of options to senior management and substantial shareholders

3.1 Approval Requirements

- A **new Scheme must be approved by shareholders** of the listed issuer in general meeting
- An **announcement must be published** on the outcome of the shareholders' meeting as soon as possible and not later than 30 minutes before the next trading session following the meeting
- **An existing Scheme of a newly admitted issuer** does not need to be approved by its shareholders after listing, however all the details of the Scheme must be clearly set out in the listing document

3.2 Scheme Document

- Scheme document must be **circulated to shareholders** or made available for inspection in Hong Kong not less than 14 days before the general meeting, and at the meeting itself
- **Scheme terms** must be provided to all participants on joining the Scheme
- Any **Scheme changes** must be provided to all participants when changes take effect
- **Scheme document must cover** the following:
 - **Purpose** of Scheme
 - **Participants** of the Scheme and basis of their eligibility
 - **Total number of securities** if issued upon exercise of all options and percentage of issued share capital that they would represent
 - **Maximum entitlement** of each Scheme participant
 - **Exercise period** – not to exceed 10 years from date of grant
 - **Minimum holding period** before an option can be exercised
 - **Performance targets** to be achieved before options can be exercised and if none, a statement to that effect
 - **Amount payable on application** or acceptance of option, if any, and period within which payment must be made
 - Basis of determining **exercise price**
 - **Rights** attaching to the securities and, if appropriate, the options themselves
 - **Life of Scheme**, which must not exceed 10 years
 - Circumstances when options will **automatically lapse**
 - Provision for adjustment of exercise price or number of securities in the event of a capitalisation issue, rights issue etc

- Provision for cancellation of options granted but not exercised
- Transferability of options
- Specific terms of Scheme that can be changed by directors or administrators without shareholder approval
- Total number of securities issued upon exercise of all options cannot exceed 10% of the relevant class of securities
- Granting options beyond the 10% limit will need shareholder approval in general meeting
- Number of securities which may be issued upon exercise of ALL outstanding options granted and yet to be exercised must not exceed 30% of the relevant class of securities
- Total number of securities issued upon exercise of options cannot exceed 1% of relevant class of securities in any 12-month period

3.3 Grants – Specific Requirements

- Each grant of options to a director, chief executive or substantial shareholder of a listed issuer must be approved by independent non-executive directors (INED) as well as shareholders
- Any grant of options to a **substantial shareholder or INED** must be approved by shareholders **if** the securities issued and to be issued upon exercise of all options already granted and to be granted in the 12-month period up to and including the date of the grant
 - Represent in aggregate over 0.1% of relevant class of securities in issue; and
 - Have an aggregate value in excess of HK\$5 million
- No options can be granted while **inside information** exists until it has been properly disclosed. It may only grant options until, and including) the trading day after the announcement of such information
- No options may be granted during **one month prior** to the earlier of:
 - Date of board meeting for approval of issuer's results; and
 - Deadline to publish results announcement for any year, half-year, quarter or any other interim period

3.4 Disclosure Requirements

- A listed issuer must provide a summary of each Scheme approved by its shareholders in its **annual report**, covering:
 - Purpose of the Scheme
 - Participants of the Scheme
 - Total number of shares available for issue under the Scheme, including percentage of issued share capital that it represents
 - Maximum holding entitlement of each Scheme participant
 - The period during which securities must be taken up
 - Minimum holding period before an option can be exercised
 - Any amount payable on application or acceptance of an option

- Basis of determining exercise price
- Remaining life of Scheme
- For each Scheme of a listed issuer or any of its subsidiaries, the following information must be **published in annual and interim reports**:
 - Details of **outstanding options at beginning and end of the financial period**, including number, date of grant, vesting period, exercise period and exercise price
 - Details of **options granted during the financial period**, including number, date of grant, vesting period, exercise period, exercise price and closing price of the securities immediately before options were granted
 - **Number of options exercised during the financial period** with exercise price and weighted average price of securities immediately before date of exercise
 - **Number and exercise price of options cancelled** during the financial period
 - **Number of options that have lapsed** during the financial period