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New restrictions to capital raising activities will take effect on 3 July 2018

Summary

On 4 May 2018, The Stock Exchange of Hong Kong Limited (HKEx) published its Consultation Conclusions on Capital Raisings by Listed Issuers (the Conclusion), which largely adopts the proposals in the Consultation Paper released in September 2017 with minor modification.

The changes in the Listing Rules intend to restrict highly dilutive and deeply discounted capital raising activities, and other market practices that may jeopardize the interests of minority shareholders. The Listing Rules amendments will take effect on **3 July 2018**.

Highly dilutive capital raisings

The most significant change in the amended Listing Rules is the imposition of a 25% value dilution threshold. Under the new Rule 7.27B, a listed company may not undertake rights issues, open offers and specific mandate placings, individually or when aggregated within a rolling 12-month period, that would result in a material value dilution (25% or more on a cumulative basis), unless there are exceptional circumstances e.g. the issuer being in financial difficulties. The value dilution is calculated by reference to the number of shares issued and the extent of the price discounts. HKEx will publish further guidance materials on the calculation of cumulative value dilution.

Rights issues and open offers

Other major changes to the Listing Rules include:

	Rights issues	Open offers
Minority shareholders' approval	Required, if the rights issue would increase the number of issued shares or the market capitalisation by more than 50%[1] (Rule 7.19A(1))	Required, unless the new shares are to be issued under the authority of an existing general mandate (Rule 7.24A)
Mandatory underwriting requirement	Removed (Rule 7.19(1) & Rule 7.24(1))	

[1] The 50% is calculated on the proposed rights issue by itself or when aggregated with other rights issues / open offers:

a) within 12 months before the announcement of the proposed rights issue; or
b) dealings in shares issued pursuant to which commenced within such 12 months, together with the number of shares upon full conversion of any bonus securities, warrants or other convertible securities as part of such rights issues / open offers (if any).

	Rights issues	Open offers
Requirements of underwriters (if any)	Type 1 licensed person under the Securities and Futures Ordinance and an independent third party OR the controlling or substantial shareholders (subject to certain conditions) (Rule 7.19 (1) & Rule 7.24)	
Connected transaction exemption for underwriting	Removed (Rule 14A.92(2)(b) removed)	
Disposal of unsubscribed shares	Mandatory excess application arrangements or compensatory arrangements to place the shares to independent placees for the benefit of the unsubscribing shareholders (Rule 7.21(1) & Rule 7.26A(1))	
Excess applications made by the controlling shareholders and their associates	Limited to a maximum of the offer size minus their pro-rata entitlements. (Rule 7.21(3)(b) & Rule 7.26A(3)(b))	

Placing of warrants or convertible securities

In general, an issuer must seek shareholder's approval in general meeting (i.e. cannot use general mandate) for the following transactions:

- placing of warrants for cash consideration (Rule 13.36(7); codification of existing listing decision LD 90-2015)
- placing of convertible securities for cash consideration when initial conversion price is lower than the market price of the shares at the time of placing (Rule 13.36(6)).

Disclosure of use of proceeds from equity fundraisings in interim/annual reports

An issuer must disclose a detailed update on the use of proceeds from all equity fundraisings in interim and annual reports (Paragraphs 11(8) and 41A of Appendix 16).

Minimum adjusted price after a share subdivision or bonus issue

An issuer must not undertake a share subdivision or bonus issue of shares if its adjusted price will be less than HK$1 based on the lowest closing price during the past six-month period (Rule 13.64A).

Take Away

Listed companies should consolidate relevant information to calculate the cumulative dilutive effect of their capital raising activities (rights issues, open offers and specific mandate placings) in the past 12 months. If a listed company anticipates its future capital raising activities may trigger the 25% threshold, they should consult the HKEx before they proceed to signing or announcing the transaction. The HKEx has the discretion to withhold the approval for or impose additional requirements on capital raising activities if the proposed issue is of a very large size or the price discount is considered to be very deep.

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