HKEx LISTING DECISION
HKEx-LD69-1 (Published in July 2009)

Summary	
Parties	Company A – a Main Board listing applicant and its subsidiaries Parentco – Company A's controlling shareholder and a Main Board listed issuer
Subject	Whether Company A must before listing release Parentco's guarantees of its existing banking facility to demonstrate its financial independence from Parentco?
Listing Rules	Rules 8.04; 14A.90[1]; Paragraph 27A of Part A of Appendix 1
Decision	Satisfied that Company A was financially independent of Parentco, the Exchange determined that (a) Parentco's guarantees of Company A's banking facility need not be released before or at the time of listing; and (b) Company A might ask Parentco for a secured loan facility to refinance the existing loans if the terms offered by independent third parties were considered by the directors to be less favourable.

SUMMARY OF FACTS

1. Parentco proposed to spin-off Company A for a separate listing on the Exchange. After the spin-off, Company A and Parentco would operate the same line of business but in different geographical markets.

2. Company A had outstanding bank loans (drawn down from its existing banking facility) which were guaranteed by Parentco. The outstanding loan amount represented almost all of Company A's total borrowings and over 180% of its net assets as at the latest audited balance sheet date. These loans were due to mature shortly after Company A's proposed listing.

3. Company A intended to refinance the banking facility before its maturity by:

   a. securing a term loan facility offered by Parentco; or

   b. accepting banking facilities offered by independent financial institutions without guarantee from Parentco. Company A had received committed offers from a number of independent financial institutions to provide generally equivalent facilities to refinance Company A's outstanding bank loans.

[1] *Rule reference amended in July 2014.*

4. Company A wanted to preserve the refinancing options to enable it to consider the best possible terms in the debt market.

5. Company A consulted the Exchange on whether the guarantees from Parentco could continue after listing. In support of its case, Company A submitted that it could operate financially independently of Parentco.

THE ISSUE RAISED FOR CONSIDERATION

6. Whether Company A must before listing release Parentco's guarantees of its existing banking facility to demonstrate its financial independence from Parentco?

APPLICABLE LISTING RULES OR PRINCIPLE

7. Rule 8.04 states that both the issuer and its business must, in the opinion of the Exchange, be suitable for listing.

8. Paragraph 27A of Part A of Appendix 1 of the Rules requires a statement explaining how the issuer is satisfied that it is capable of carrying on its business independently of the controlling shareholder (including any close associate[2]) after listing, and particulars of the matters that it relied on in making the statement.

9. Listing Decisions HKEx-LD42-1 published in December 2004 and HKEx-LD48-1 published in December 2005 both report on instances of how listing applicants demonstrated their independence of their parent.

THE ANALYSIS

10. When reviewing whether an applicant can carry on its business independently of its controlling shareholder, the Exchange ordinarily considers the applicant's circumstances, including financial independence, operational independence and management independence. An applicant may be dependent on its controlling shareholder in one or more of these areas. Where the degree of dependence is excessive, this may raise concern about the applicant's suitability for listing.

11. One method an applicant commonly uses to demonstrate its financial independence is by repaying or capitalising all outstanding loans due to, or releasing guarantees provided by, its parent before listing. HKEx-LD42-1 reports on this release method.

12. While the Exchange accepts the release method to demonstrate an applicant's financial independence of its parent, it is not a mandatory requirement. The Exchange has accepted other methods to demonstrate an applicant's financial independence. Some examples are stated below.

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[2] *Rule amended in July 2014.*

Case 1: Using IPO proceeds to repay shareholder loans

13. In one case, the Exchange allowed the shareholder loan to be repaid from the proceeds of the new issue. The Exchange was satisfied of the applicant's financial independence after taking into account that it had successfully arranged for bank facilities to replace the loan before listing and the reason for using part of the IPO proceeds to repay the loan was to save interest costs. The listing document also clearly disclosed the application of the proceeds, including the applicant giving an irrevocable instruction to apply part of the proceeds to release the loan.

Case 2: Newly spun-off entity need not release parent's guarantees before listing

14. When considering a listing application of a newly spun-off entity a few years ago, the Exchange determined that the applicant was not required to prematurely release its parent's guarantees for its offshore banking facilities before its listing.

15. In assessing whether the applicant was able to operate financially independently of its parent, the Exchange took into account:

    a. the applicant's submission that the premature release of all of its parent's guarantees without the consent of the counterparties would give rise to early termination liabilities and practical and commercial difficulties, because there were many borrowers within the parent group and banking relationships were very complicated. Renegotiation of all of the facilities simultaneously would not be feasible or cost-effective. The banks in the foreign markets might impose considerable local liquidity constraints on any borrowers seeking significant funding at any one time;

    b. the applicant had obtained confirmations from major banks for credit facilities without guarantee or other financial support from its parent; and

    c. the applicant intended an orderly release of all parent group guarantees as soon as practicable. Its target was to commence negotiations, within six months after listing, with its lenders to refinance at least half of the indebtedness guaranteed by its parent at the listing date.

HKEx-LD48-1

16. The Exchange reported in Listing Decision HKEx-LD48-1 that the counter-guarantees granted by the applicant's controlling shareholder need not be released before listing subject to the applicant giving certain undertakings to the Exchange, including that the applicant would use its best endeavours to release all counter-guarantees in an orderly manner without delay within six months after listing.

17. In determining whether the applicant could operate financially independently of its controlling shareholder, the Exchange took into account the circumstances of the applicant, including its financial position and the complexity of the guarantee arrangement.

Factual Application

18. The Exchange was of the view that so long as Company A could show that it could operate financially independent of Parentco at the time of listing, it would not interfere with its commercial decisions on financial arrangements.

19. In determining whether Company A could operate financially independently of its controlling shareholder, the Exchange took into account that:

    a. Company A had a record of fund raising on a stand-alone basis without any credit support from Parentco;

    b. Company A had received firm offers from a number of independent financial institutions to provide generally equivalent finance facilities, on a stand-alone basis, to refinance the loans secured by Parentco's guarantees. The listing document would disclose this fact; and

    c. Company A had a strong financial position. Its business operations are in relatively matured and developed markets.

20. When examining Company A's case against the precedent cases, the Exchange noted that:

    a. similar to those cases, the premature release of Parentco's guarantees might not be commercially sound or practical in the prevailing economic climate where financial institutions might be more likely to impose stricter or less favourable terms for banking facilities;

    b. unlike other cases, Company A indicated that it might ask Parentco for a secured loan facility to refinance the existing loans if the terms offered by independent third parties were considered by the directors to be less favourable.

THE DECISION

21. Satisfied that Company A was financially independent of Parentco, the Exchange determined that:

    a. Parentco's guarantees of Company A's banking facility need not be released before or at the time of listing; and

    b. Company A might ask Parentco for a secured loan facility to refinance the existing loans if the terms offered by independent third parties were considered by the directors to be less favourable.

22. The Parentco's guarantee will be subject to continuing connected transaction requirements under Chapter 14A of the Rules.