

Hong Kong: The SFC consults on the Takeovers Code amendments

In brief

On 19 May 2023, the Hong Kong Securities and Futures Commission ("**SFC**") published its **consultation paper** on proposed amendments to the Hong Kong Codes on Takeovers and Mergers and Share Buy-backs. The proposed amendments cover various aspects, including delistings and privatisations, partial offers, the chain principle, the offer period and timetable, the offer price, etc. and mark the first comprehensive amendments since 2018. The consultation period will close on 23 June 2023.

Key proposals

Below is a summary of the key proposals. Some of the proposals are made in light of the recent court judgments and Takeovers Panel decision relating to the interpretations of the Hong Kong Code on Takeovers and Mergers ("**Takeovers Code**"), while the majority of the rest are to codify the SFC's existing practices.

	Proposed Changes
a. General	
1. Definition of "close relatives"	The SFC will codify its existing practice and expand the definition of "close relatives" of a person to include the person's grandparents, grandchildren, sibling's spouse, children of siblings, parents-in-law and spouse's siblings. As each of classes (2), (6) and (8) presumed concert parties includes "close relatives", these individuals will fall within the concert party presumptions and will have the burden of proof to rebut the presumptions.
2. Definition of "voting rights"	A note will be added to clarify that voting rights that are subject to any restrictions, whether by agreement, by operation of law and regulations, or pursuant to a court order, will still be regarded as voting rights exercisable at a company's general meeting.
b. Delistings and privatisations	
3. Alignment between condition (iii) to the Note to Rule 2.2 and Rule 2.11 of the Takeovers Code	The SFC will codify its existing practice and include purchases of disinterested shares made by an offeror and its concert parties after publication of a Rule 3.5 offer announcement in determining whether the threshold of acquiring 90% of the disinterested shares is met.
4. Clarification of the shareholders' meetings requirement under Rules 2.2 and 2.10 of the Takeovers Code	The proposed amendments are made in light of the two alternative views on whether Rule 2.10 of the Takeovers Code prohibits an offeror and its concert parties from attending and voting at the court-sanctioned shareholders' meeting for a Hong Kong privatisation scheme of arrangement, which were considered in the recent Hong Kong court judgments ¹ (please refer to our client alert published in April 2022 for more details). Rule 2.2 uses similar wording.

¹ Re Cosmos Machinery Enterprises Ltd [2021] HKCFI 2088 and Re Chong Hing Bank Limited [2021] HKCFI 3091 and [2022] 1 HKC 377

	Proposed Changes
	<p>To remove any ambiguity in the interpretation of Rules 2.2 and 2.10, the SFC will replace references to a "duly convened meeting of the holders of the disinterested shares" with a "duly convened meeting of shareholders" in these rules. A new note to Rule 2 will be added to clarify that whether a shareholders' meeting is duly convened is governed by an offeree company's constitutional documents and the company law of its place of incorporation.</p> <p>As such, if, for example, the company law of an offeree company's place of incorporation allows all shareholders, including the offeror and its concert parties, to attend and vote on a privatisation scheme of arrangement, Rule 2.10 will not override the law. Any votes cast by the offeror and its concert parties will be not counted in calculating the requisite voting thresholds under Rule 2.10.</p>
5. Last day for all conditions to be fulfilled under Rule 15.7 of the Takeovers Code	The SFC will codify its existing practice and expressly provide that no consent from the Executive will be required in a privatisation scheme of arrangement where the time delay between the court meeting and the effective date of the scheme is due to the court's timetable.
c. Gathering of irrevocable undertakings	
6. Revising the existing framework for an offeror to obtain irrevocable undertakings from shareholders	Note 4 to Rules 3.1, 3.2 and 3.3 and Practice Note 12 will be revised to allow an offeror to approach without prior consultation with the Executive a shareholder with a "material interest in an offeree company", i.e. a person who, either alone or in concert with others, controls 5% or more of the voting rights of the offeree company. In other words, the Executive must be consulted before any approach is made with a shareholder who does not have a material interest in the offeree company. An offeror can approach up to six shareholders, whether with or without a material interest in the offeree company, in an offer.
d. The chain principle	
7. Substantiality test under Note 8(a) to Rule 26.1 of the Takeovers Code	The SFC will codify its existing practice and amend the substantiality test under Note 8(a) to Rule 26.1 and Practice Note 19 by (a) adding market capitalisation as a parameter for comparing the relative values of both companies (this is relevant where both companies are listed) and (b) adding a look-back period of the three most recent financial periods if the relative values of assets and profits calculated based on the most recent audited financial statements produce an anomalous result.
e. Offer period and timetable	
8. Definition of "offer period"	To address the situations where an offeree company is subject to an unnecessarily prolonged offer period, e.g. the controlling stake of the offeree companies is under receivership, the definition will be amended to give the Executive the explicit power to end an offer period.
9. Final day rule under Rule 15.5 of the Takeovers Code	The SFC will codify its existing practice and amend Rule 15.5 by stating that any extension of Day 60 will not exceed four months after the despatch of the offer document, which is in line with the spirit of Rule 2.11 of the Takeovers Code.
10. Put up or shut up ("PUSU")	<p>The SFC will codify its existing practice and add a new Rule 3.9 of the Takeovers Code to give the Executive the explicit power to issue PUSU orders upon application by an offeree company, i.e. to require a potential offeror to make a Rule 3.5 offer announcement within a set time period (put up), or to announce that it will no longer proceed with an offer (shut up), to prevent an offeree company from being subject to a prolonged offer period. The Executive will consider factors including (i) the current duration of the offer period, (ii) the reason(s) for the delay in issuing a Rule 3.5 offer announcement, (iii) the proposed offer timetable (if any), (iv) any adverse effects that the offer period has had on the offeree company, and (v) the conduct of the parties to the offer.</p> <p>The new Rule 3.9 will also apply to share buy-back.</p>
11. Settlement of consideration and return of share certificates under	To align the timing requirements for settlement of consideration and return of share certificates, Rules 17 and 20.2 will be amended so that:

	Proposed Changes
Rules 17 and 20.2 of the Takeovers Code	<p>(a) For successful offers, share certificates for untaken or untendered shares in an offer (including partial offers) or a share buy-back by general offer must be posted to or be made ready for collection by the accepting shareholder at the same time as the payment of consideration, and in any event no later than seven business days after the later of (i) the date the offer becomes, or is declared, unconditional, and (ii) the date of receipt of a duly completed acceptance. The relevant deadline for partial offers would be seven business days after the close of the partial offer.</p> <p>(b) For unsuccessful offers, share certificates must be returned to accepting shareholders no later than seven business days after the withdrawal or lapse of the offer. The same timing should apply when an accepting shareholder withdraws their acceptance after 21 days from the first closing date of the offer, if the offer has not by then become unconditional as to acceptances.</p>
f. Offer price	
12. Disclosure of an indicative offer price in a Rule 3.7 talk announcement	The SFC will codify its existing practice and add new notes to Rule 3.7 of the Takeovers Code so that disclosure of an indicative offer price in a Rule 3.7 talk announcement is not normally permitted prior to a Rule 3.5 offer announcement save in exceptional circumstances. When an indicative offer price is disclosed, it will be treated as a price floor for any offer that materialises.
13. Deduction of dividends from offer price	The proposed amendments to Note 11 to Rule 23.1 and Note 3 to Rule 26.3 of the Takeovers Code are to codify the Takeovers Panel decision relating to Dalian Port (PDA) Company Limited on the effect of dividends and withholding tax on an offer price. Unless an offeror specifically reserves its rights in an announcement, no deduction of dividends from the offer price will be allowed. Where the payment of dividends is subject to a withholding tax, the offer price should be reduced by the gross amount received or receivable by the offeree company shareholders.
g. Partial offers	
14. No extension of the closing date under Rule 28.4 of the Takeovers Code	<p>Where the acceptance condition is met after the first closing day, the offeror must declare a partial offer unconditional as to acceptance on the day the acceptance condition is met, and the offer period will not be allowed to extend beyond the 14th day after the day the acceptance condition has been met. This applies irrespective of whether the approval under Rule 28.5 of the Takeovers Code (if required) has been obtained.</p> <p>The approval under Rule 28.5 of the Takeovers Code, if required, will not be considered part of the acceptance condition for the offer and must be obtained on or before the final closing day. There would be no further extensions to the offer period.</p>
15. Comparable offer for convertible securities, warrants, etc.	A new Rule 28.10 of the Takeovers Code will be added as an explicit requirement to make appropriate Rule 13 offers for convertible securities, warrants, options, etc. during a partial offer, which could result in the offeror holding shares carrying 30% or more of the voting rights of the offeree company.
16. Tick-box approval requirement under Rule 28.5 of the Takeovers Code	Rule 28.5 of the Takeovers Code will be amended to clarify that the tick-box approval requirement does not apply to an offeror that, together with its concert parties, already holds more than 50% of the voting rights of the offeree company.
17. Exempt principal traders connected with an offeror	A new Note 3 to Rule 28 of the Takeovers Code will be added to clarify that the restrictions on exempt principal traders under Rules 35.3 and 35.4 of the Takeovers Code apply in the context of a partial offer, i.e. (a) securities owned by an exempt principal trader connected to an offeror must not be assented to the offer until the offer becomes or is declared unconditional as to acceptances, and (b) securities owned by an exempt principal trader connected with an offeror or the offeree company should not be allowed to approve a partial offer that is akin to voting in the context of general offers.

For further information and to discuss what this development might mean for you, please get in touch with our lawyers set out under Contact Us or your usual Baker McKenzie contact.



Contact Us



Christina Lee

Partner

Hong Kong

christina.lee@bakermckenzie.com



Hang Wang

Partner

Beijing

hang.wang@bakermckenzie.com



Emmy Lo

Knowledge Lawyer

Hong Kong

emmy.lo@bakermckenzie.com

© 2023 Baker & McKenzie. **Ownership:** This site (**Site**) is a proprietary resource owned exclusively by Baker McKenzie (meaning Baker & McKenzie International and its member firms, including Baker & McKenzie LLP). Use of this Site does not of itself create a contractual relationship, nor any attorney/client relationship, between Baker McKenzie and any person. **Non-reliance and exclusion:** All information on this Site is of general comment and for informational purposes only and may not reflect the most current legal and regulatory developments. All summaries of the laws, regulation and practice are subject to change. The information on this Site is not offered as legal or any other advice on any particular matter, whether it be legal, procedural or otherwise. It is not intended to be a substitute for reference to (and compliance with) the detailed provisions of applicable laws, rules, regulations or forms. Legal advice should always be sought before taking any action or refraining from taking any action based on any information provided on this Site. Baker McKenzie, the editors and the contributing authors do not guarantee the accuracy of the contents and expressly disclaim any and all liability to any person in respect of the consequences of anything done or permitted to be done or omitted to be done wholly or partly in reliance upon the whole or any part of the contents of this Site. **Attorney Advertising:** This Site may qualify as "Attorney Advertising" requiring notice in some jurisdictions. To the extent that this Site may qualify as Attorney Advertising, PRIOR RESULTS DO NOT GUARANTEE A SIMILAR OUTCOME. All rights reserved. The content of this Site is protected under international copyright conventions. Reproduction of the content of this Site without express written authorisation is strictly prohibited.

