

Client Alert

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SFC amends the Codes on Takeovers and Mergers and Share Buy-backs to protect minority shareholders' interest

Summary

On 13 July 2018, the Securities and Futures Commission (SFC) released its Consultation Conclusions (the "[Conclusions](#)") on proposed amendments to the Codes on Takeovers and Mergers and Share Buy-backs (the "**Codes**", each a "**Code**"). The amendments to the Codes took immediate effect on the same day. It is indicated in the Conclusions that where this timing may produce major difficulties, for example, in the case of transactions in progress that have already been announced, the Executive should be consulted and will endeavor to reach a solution which is fair to all parties. The amendments to the Codes aim to enhance shareholder protection and align the treatment of all companies that are subject to the Codes. Certain amendments represent a shift in SFC's previous practice.

What's changed?

The major amendments to the Codes are summarized below.

1. Separate voting thresholds for whitewash waivers and underlying transactions

The SFC has decided to:

- (a) increase the independent shareholders' approval requirement for a whitewash waiver from a simple majority to **at least 75%**; and
- (b) introduce an explicit requirement for the underlying transaction to be separately approved by the independent shareholders by **more than 50%**.

The SFC takes the view that a whitewash waiver should be subject to a more stringent approval requirement as shareholders are deprived of the opportunity to receive a general offer to buy their shares following a change of control of the offeree company. To avoid a possible anomaly between the voting requirements in the Hong Kong Listing Rules (simple majority) and the Codes, the SFC has decided that the underlying transaction should be subject to a simple majority vote.

Implications

In cases where the underlying transaction resolution is approved by a simple majority vote but the independent vote for the corresponding whitewash waiver resolution fails to reach the 75% threshold, so long as the whitewash waiver condition is waivable, the whitewash waiver applicant would still be able to proceed with the underlying transaction coupled with a general offer.





2. Delisting of offeree companies incorporated in jurisdictions with no compulsory acquisition rights

To protect minority shareholders of offeree companies incorporated in jurisdictions with no compulsory acquisition rights and to align the treatment of all companies that are subject to the Codes, the following measures must be put in place by offerors seeking to delist such companies in Hong Kong through general offers before a waiver from Rule 2.2(c) of the Code on Takeovers and Mergers (the "**Takeovers Code**") might be granted by the SFC:

- (a) the resolution to approve the delisting must be made subject to the offeror having received valid acceptances amounting to 90% of the disinterested shares.;
- (b) the general offer must remain open for acceptance for a longer period than normally required by Rule 15.3 of the Takeovers Code (14 days) after it becomes or is declared unconditional in all respects; and
- (c) shareholders who have not yet accepted the offer will be notified in writing of the extended closing date and the implications of not accepting the offer.

These requirements would also apply to real estate investment trusts (REITs) that are subject to the Codes.

Implications

For jurisdiction where its legal regime does not provide for compulsory acquisition rights, like the People's Republic of China (the "**PRC**"), before the amendments to the Takeovers Code were introduced, the SFC had granted a number of waivers from compliance with Rule 2.2(c) for privatizations of PRC companies on the basis that it was technically impossible to comply under the PRC law. The amendments represent a significant shift from the previous practice.

3. Dealing with the Executive, Panel and Takeovers Appeal Committee

The amended Codes clarify, codify and empower SFC's power in the following ways:

- (a) **Compensation** (new section 13.13 to the Introduction to the Codes)

The Takeovers and Mergers Panel (the "**Panel**") is empowered to make a ruling requiring compensation to be paid to current or former shareholders who have suffered as a result of a breach of the Takeovers Code.

- (b) **Compliance** (new sections 7.2 and 13.12 to the Introduction to the Codes)

The Executive or the Panel can issue pre-emptive compliance rulings if it is satisfied (i.e. a subjective test) that:

- (i) a person has breached the Codes; or



- (ii) there is a reasonable likelihood that a person will contravene a requirement imposed by or under the Codes.
- (c) **Co-operation** (new sections 5.2, 11.18 and 14.9 to the Introduction to the Codes)

Any person dealing with the Executive, the Panel or the Takeovers Appeal Committee must (among other things):

- disclose any information known to him and relevant to the subject matter;
- **correct or update** that information if it changes; and
- take all **reasonable care** to provide **true, accurate and complete information** – including an obligation to promptly correct or supplement the information **after** the matter has been determined.

Implications

The compliance ruling is a subjective test.

In cases there was a genuine disagreement between the parties and the Executives about how the Codes apply, the Executive would normally either issue a ruling to the parties which sets out the basis of its decision or refer the matter to the Panel for its decision if there is a particularly novel, important or difficult point at issue.

4. Disclosure of shareholdings and dealings

The amendments clarify the scope of disclosure of holdings of and dealings in relevant securities and relax some administrative requirements.

- (a) Clarify that an offeror must announce details of its relevant securities in all offers (i.e. securities exchange offers and cash offers) when an offer period begins (revised Rule 3.8 of the Takeovers Code).
- (b) Codify the existing practice that, when the offeree company is a REIT, two classes of associate of the offeree company by virtue of classes (7) and (8) of the definition of "associate" (a REIT's trustee and a REIT's management company) are required to disclose shareholdings of and dealings by them in the offeree board circular (new paragraph 3(p) to Schedule IX to the Codes).
- (c) Extend the deadline for filing of dealing disclosures from 10:00 a.m. to 12:00 noon on the business day following the date of the transaction. In case of a dealing in US time zones, the deadline is the second business day following the date of the transaction (revised Note 5 to Rule 22 and revised Rule 22.4 of the Takeovers Code).
- (d) Remove the requirement to make separate dealing disclosures to the offeror, offeree company or their financial advisers. Dealing disclosure should be made by submitting the prescribed forms to the SFC. SFC will arrange for the posting of the disclosure on the websites of SFC and The Stock Exchange of Hong Kong Limited (SEHK) (revised Note 6(a) to Rule 22 of the Takeovers Code).



5. Definition of "associate"

The definition of "associate" is amended to eliminate overlap and potential inconsistencies that arise out of the similarities between the definition of "associate" and the definition of "acting in concert".

6. Miscellaneous amendments

Various miscellaneous amendments codify SFC's existing practices.

(a) Dissemination of information in meetings during an offer period (Notes 2 and 3 to Rule 8.1 of the Takeovers Code)

- clarify the meaning of "meetings" to include interviews, discussions or any meetings held in person or by telephone or other electronic means
- require financial advisers to confirm that printed materials distributed during the meetings do not contain any material new information or significant new opinion

(b) Confirmation of publication and translation (new notes to Rules 8.6, 9.3, 9.4 and 12 of the Takeovers Code)

Codify the existing practice of requiring the issuer of a Code document to provide the Executive with confirmations of the accuracy of the translation, the publication of the document and the absence of material change to the version cleared by the Executive.

(c) Historical financial information in a Code document (new notes to Schedules I, II, III to the Codes)

To reduce administrative burden and the size of a Code document, if the offeror and/or offeree company are listed on SEHK, the offeror and/or offeree company may incorporate the historical financial information in the relevant Code document by reference to the documents published in accordance with the Hong Kong Listing Rules (instead of reproducing the same information in the Code document).

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