



Hong Kong

October 2017

## COURT ALLOWS JUDICIAL REVIEW OF TVB HONG KONG TAKEOVERS PANEL RULING

On 4 October 2017, The Honourable Justice Wong in the Court of First Instance granted leave to Television Broadcasts Limited (TVB) and allowed a judicial review<sup>1</sup> of the Takeovers and Mergers Panel (**Hong Kong Takeovers Panel**) ruling (**Ruling**) regarding a share buy-back (**Share Buy-Back Offer**)<sup>2</sup> which TVB announced in early 2017.

Previously, on 10 May 2017, the Hong Kong Takeovers Panel ruled that a waiver of the general offer obligation (**Whitewash Waiver**) in relation to the Share Buy-Back Offer should be granted, subject to certain conditions: (1) a majority of votes cast at the general meeting in favour of the resolution to approve the offer (without adjustment of voting rights); and (2) the Whitewash Waiver should not be put to a vote of shareholders in general meeting. For more information about the Ruling, please see Charltons' July 2017 newsletter<sup>3</sup>.

The Court of First Instance quashed the Ruling and declared that section 19 of Schedule 1 to the Broadcasting Ordinance (Cap 562) applies to the shareholders' approval of the Whitewash Waiver. Section 19 is a scale-back provision, so that where the votes of non-Hong Kong resident shareholders exceed 49%, their votes will be scaled back proportionately. However, this is in conflict with General Principle 1 of the Codes on Takeovers and Mergers and Share Buy-backs (**Codes** collectively and **Takeovers Code** and **Buy-Backs**

**Code** respectively), which provides that all shareholders are to be treated even-handedly and all shareholders of the same class are to be treated similarly. This is an important decision in that it deals with the relationship between the general law (in particular the Broadcasting Ordinance) and the Codes, and the Hong Kong Takeovers Panel's jurisdiction under the law.

### Overview

In January and February 2017, TVB announced an offer to repurchase 27.4% of its issued shares. Young Lion Holdings Ltd and parties considered as acting in concert with it (**Concert Group**) have an aggregate 29.9% interest in TVB. The Concert Group has indicated that they do not intend to participate in the Share Buy-Back Offer, with the consequence that if the other shareholders tender the maximum amount of shares, the Concert Group's combined interests may increase to 41.19%. Four representatives of the Concert Group are non-executive directors of TVB, and an increase in the Concert Group's interests in TVB due to the buy-back would be regarded as an acquisition of voting rights under the Codes. This would mean that pursuant to Rule 26.1 of the Takeovers Code, the Concert Group, having passed the 30% threshold, would be required to make a mandatory general offer to all TVB shareholders on equal terms. However, the Takeovers Executive is empowered to grant a waiver of the mandatory general offer requirement, known as a "whitewash waiver".

TVB's Share Buy-Back Offer was conditional upon: (1) the passing of an ordinary resolution to approve the offer by the independent shareholders at an extraordinary general meeting

1 [http://legalref.judiciary.hk/lrs/common/ju/ju\\_frame.jsp?DIS=111592&curpage=T](http://legalref.judiciary.hk/lrs/common/ju/ju_frame.jsp?DIS=111592&curpage=T)  
2 [http://www.sfc.hk/web/EN/files/CF/pdf/Panel%20Decision/Final%20version%20170510%20\(clean\).pdf](http://www.sfc.hk/web/EN/files/CF/pdf/Panel%20Decision/Final%20version%20170510%20(clean).pdf)  
3 <https://www.charltonslaw.com/tvb-ruling-on-whitewash-waiver-by-takeovers-panel/>

(EGM) – a requirement of the Companies Ordinance (Cap 622); and (2) the grant of a whitewash waiver by the Takeovers Executive (and not having been withdrawn).

The Takeovers Executive referred a number of issues stemming from TVB's application for a whitewash waiver to the Hong Kong Takeovers Panel. An important issue was whether the provisions in section 19 of Schedule 1 to the Broadcasting Ordinance make any difference in light of General Principle 1 of the Codes.

Under Rule 32.1 of the Takeovers Code, the Takeovers Executive treats an application for a waiver from the requirement to make a mandatory offer in the case of a share buy-back by general offer in accordance with Rule 26 as if it were an application for a whitewash waiver in accordance with Note 1 on dispensations from Rule 26. According to Note 1, the Takeovers Executive will normally waive the obligation if there is an independent vote at a shareholders' meeting. Further, pursuant to paragraph 2(e) of Schedule VI, such grant is subject to approval of the proposals by an independent vote at a meeting of the holders of any relevant class of securities.

According to General Principle 1 of the Codes, all shareholders are to be treated even-handedly and all shareholders of the same class are to be treated similarly.

However, TVB held a licence to provide a "domestic free television programme service" under the Broadcasting Ordinance, and was thus subject to the special controls regime under the Broadcasting Ordinance, particularly the scale-back provision under section 19 of Schedule 1. The crucial scale-back provision relevantly provides:

"(1) Subject to subsection (2), notwithstanding anything contained in the articles of association of a licensee or any provision of any law apart from this section, where any question or matter is to be determined by a poll at any general meeting of the licensee, the following shall apply –

...

(b) where the total voting control exercised by unqualified voting controllers would otherwise exceed, in the aggregate, 49% of the total voting control exercised on the poll by both qualified and unqualified voting controllers, the votes cast on the poll by unqualified voting controllers shall, for the purpose of determining

the question or matter, be reduced by multiplying those votes by the percentage determined by the formula specified in paragraph (c);

..."

(emphasis added)

The Broadcasting Ordinance differentiates between qualified voting controller and non-qualified voting controller. Qualified voting controller means a shareholder who is ordinarily resident in Hong Kong for seven years, and non-qualified voting controller means one who is not a qualified voting controller. Section 19(1)(c) formula is a "scaling back" mechanism, so that where the votes of non-Hong Kong resident shareholders exceed 49%, their votes will be scaled back proportionately. As a result of the Concert Party's interest in the Share Buy-Back Offer, they will have to abstain from voting, and given past voting patterns, it is expected that unqualified voting controllers' votes will exceed 49%.

The Hong Kong Takeovers Panel ruled that a whitewash waiver should be granted conditional on:

(1) the majority of votes cast (without adjustment under the scale-back provision) at the general meeting should be in favour of the resolution to approve the Share Buy-Back Offer (**Majority Vote Condition**); and

(2) the question as to whether there should be a whitewash waiver should not be put to a vote of shareholders in general meeting (**No Vote Condition**).

TVB applied for leave for judicial review of the Ruling, seeking an order of *certiorari* to bring up and quash the Ruling and a declaration that the scale-back provision in the Broadcasting Ordinance is applicable to the shareholders' approval of the Whitewash Waiver. If TVB is successful in its application for judicial review, the issue as to whether a whitewash waiver should be granted must be remitted back to the Takeovers Executive.

Underlying TVB's application was their view that a whitewash waiver should either be granted on the usual condition of approval by an independent vote at a shareholders' meeting (to which the scale-back provision would apply) or not at all.

### TVB's grounds for judicial review

TVB filed six grounds for judicial review of the Ruling:

1. that the Ruling was *ultra vires* – the Hong Kong Takeovers Panel does not have jurisdiction or power to disregard or direct others to disregard Broadcasting Ordinance provisions;
2. that the Hong Kong Takeovers Panel erred in law in misconstruing the true meaning and effect of the scale-back provision;
3. that the Ruling was made for an improper purpose and was an abuse of the Hong Kong Takeovers Panel's power in that the panel is attempting to circumvent the scale-back provision;
4. that the Hong Kong Takeovers Panel misconstrued General Principle 1, and thus erred in law – the panel took into account an irrelevant consideration, and failed to take into account a relevant consideration;
5. that the Ruling ignored the requirement in Schedule VI of the Codes that a whitewash waiver should be subject to approval by shareholders. The Hong Kong Takeovers Panel thus erred in law, took into account an irrelevant consideration, failed to take into account a relevant consideration, acted unreasonably, and did so for an improper purpose; and
6. that the Ruling went beyond the factual limits of the case – the Hong Kong Takeovers Panel failed to recognise that the Share Buy-Back Offer by its terms is and must be conditional upon any whitewash waiver (if granted) being put to a vote by TVB's shareholders. The panel thus erred in law, took into account an irrelevant consideration, failed to take into account a relevant consideration, acted unreasonably, and did so for an improper purpose.

## Grounds 1-3

The Hon Justice Wong considered the first three grounds (*ultra vires*, misconstruction of statute, and improper purpose) together. Her Honour noted that there is a general legal principle that persons “exercising public authority” are duty bound to promote, and not “undermine the public policies” behind the authority. Her Honour said that this principle applies to any decision maker which frustrates the public policy of a statute, irrespective of whether that statute is the source of power for that decision maker.

TVB's case was that the Ruling was an attempt to circumvent the scale-back provision, and thus the Hong Kong Takeovers Panel acted *ultra vires* and for an improper purpose, and erred in law by missing the true effect of the statutory regime under the Broadcasting Ordinance.

The Securities and Futures Commission's (SFC) position was that any decision to grant a whitewash waiver was not governed by the Broadcasting Ordinance, and that there was no requirement in the Broadcasting Ordinance or other legislation for a whitewash waiver to be put to a vote at a shareholders' general meeting. Instead, the Takeovers Code prescribed the grant of a whitewash waiver subject to shareholders' approval in general meeting. Whether a whitewash waiver should be granted is within the jurisdiction of the Hong Kong Takeovers Panel, which derives its powers from the Codes and not the Broadcasting Ordinance. It was contended by the SFC that the scale-back provision in the Broadcasting Ordinance has a limited application in that it applies only to questions or matters to be determined by a poll at any general meeting of the licensee. Further, the scale-back provision has no application when the Hong Kong Takeovers Panel determines as a condition for the grant of the Whitewash Waiver that it should comply with the wishes of all TVB's shareholders (regardless of residency) on the Whitewash Waiver without requiring the matter to be put to a vote at a general meeting. The recount of the votes on the Share Buy-Back Offer (without the scale-back provision) is a method of determining shareholders' view without a shareholders' meeting. The Majority Vote Condition does not require any corporate act by TVB that triggers the scale-back provision.

The Hon Justice Wong focused on “the supremacy of the scale-back provision”, which derives from the language of the Broadcasting Ordinance, which expressly states that the provision applies notwithstanding anything found in the licensee's articles of association or “any provision of any law”.

According to Her Honour, the purpose of restrictions on ownership and voting control under the Broadcasting Ordinance is to ensure that licensees' decisions (both at board and shareholders' meetings) are made and approved by a majority of persons ordinarily resident in Hong Kong.

She noted that paragraph 1.3 of the Introduction to the Codes provides that the Codes do not have the force of law, but represent a consensus of opinion of those who participate in Hong Kong's financial markets and the SFC regarding standards of commercial conduct and behaviour considered acceptable for takeovers, mergers and share repurchases.

Counsel for the SFC submitted that there is no requirement by law for the Hong Kong Takeovers Panel to put the Whitewash Waiver to TVB's shareholders for a vote at a general meeting. However, Her Honour stated that the scale-back provision applies "where any question or matter is to be determined by a poll at any general meeting of the licensee", and does not only apply where the matter to be put to shareholders is required by law.

Her Honour said that the question to be determined is whether the Hong Kong Takeovers Panel in its Ruling put the Whitewash Waiver to a determination by TVB's shareholders at the EGM. In answering this question, Her Honour emphasised that the Court should have regard to the substance and reality of the matter, and not merely form.

Following the Hong Kong Takeovers Panel's Ruling, the issue as to whether to grant the Whitewash Waiver reverts back to the Takeovers Executive who would grant the waiver after the EGM taking into consideration the amount of support for the Share Buy-Back Offer.

The Majority Vote Condition involves a recount of the votes on the Share Buy-Back Offer without employing the scale-back provision. This raises the issue whether this condition effectively puts the Whitewash Waiver to a determination by a poll at the EGM, thereby triggering the scale-back provision.

TVB's shareholders are to vote supposedly only on the Share Buy-Back Offer at the EGM, with the Whitewash Waiver not being put to a vote. However, shareholders voting on the offer would know that their votes would be recounted in relation to the Whitewash Waiver, and thus they would be expected to vote in a manner that reflects their views on the Whitewash Waiver.

Critical to the judgment was The Hon Justice Wong's opinion that the Hong Kong Takeovers Panel's requirement of a recount of the votes on the Share Buy-Back Offer for the purpose of granting the Whitewash Waiver was in substance and in effect directing a vote on the waiver. The Majority Vote Condition in substance and in effect required a vote by TVB's independent shareholders on the Whitewash Waiver, but without the application of the scale-back provision. The dis-application of the scale-back provision was not permitted under the Broadcasting Ordinance.

Her Honour thus found that the Hong Kong Takeovers Panel in including the Majority Vote Condition for the grant of the Whitewash Waiver, misconstrued the true meaning and effect of the scale-back provision and disregarded and attempted to circumvent the provision, and the Ruling was *ultra vires*.

TVB made out the first three grounds, and thus Her Honour stated that it is unnecessary to address the other grounds for judicial review.

Finally, the Court addressed the submission of Counsel for the SFC that although the Hong Kong Takeovers Panel's decisions are subject to judicial review, it is well recognised that the courts should only interfere in very limited circumstances. However, the authorities relied on by Counsel for the SFC did not have any application to the present issue involving the operation of a general law which, if triggered, has priority over the Codes.

## Disposition

Her Honour issued the following orders:

- Grant TVB leave to apply for judicial review of the Ruling.
- Allow TVB's application for the judicial review of the Ruling.
- Make an order of *certiorari* to bring up and quash the Ruling.
- Make a declaration that the scale-back provision in section 19 of Schedule 1 to the Broadcasting Ordinance is applicable to the shareholders' approval of the Whitewash Waiver.
- Remit back to the Takeovers Executive the question of whether to grant a whitewash waiver to TVB.
- Make an order *nisi* that the SFC should pay TVB's costs of these proceedings, to be taxed on a party and party basis if not agreed.

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