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**SFC CONSULTATION
ON **PROPOSED**
AMENDMENTS TO
THE CODES ON
TAKEOVERS AND
SHARE BUY-BACKS**

2 AUGUST 2023

Proposed changes involve:

- codification of various Takeovers Executive practices
- cutting the number of paper documents required to be published +
- housekeeping amendments

Consultation closed on 23 June 2023



A WIDER DEFINITION OF “CLOSE RELATIVES”

- Definition of “**close relatives**” is mainly relevant to Classes (2), (6) + (8) of the persons presumed to be acting in concert and Class (3) associates
- Current definition: a person’s spouse, de facto spouse, children, parents + siblings

Proposed definition will add

- a person’s grandparents + grandchildren
- a person’s siblings, a sibling’s spouse or de facto spouse + their children
- the parents + siblings of a person’s spouse or de facto spouse +

+ **clarify** that “children” include natural, adopted + step-children



A WIDER DEFINITION OF “CLOSE RELATIVES” (CONT’D)

- Applicants bear burden of proof of rebutting presumption of acting in concert
- The SFC will not accept arguments that parties are not in regular contact or have not seen each other to rebut the presumption, **unless** there’s corroborative evidence (e.g. litigation between family members evidencing family relationship breakdown)
- Close relatives will be eligible for a waiver from the general offer obligation under Note 6 to Rule 26.1



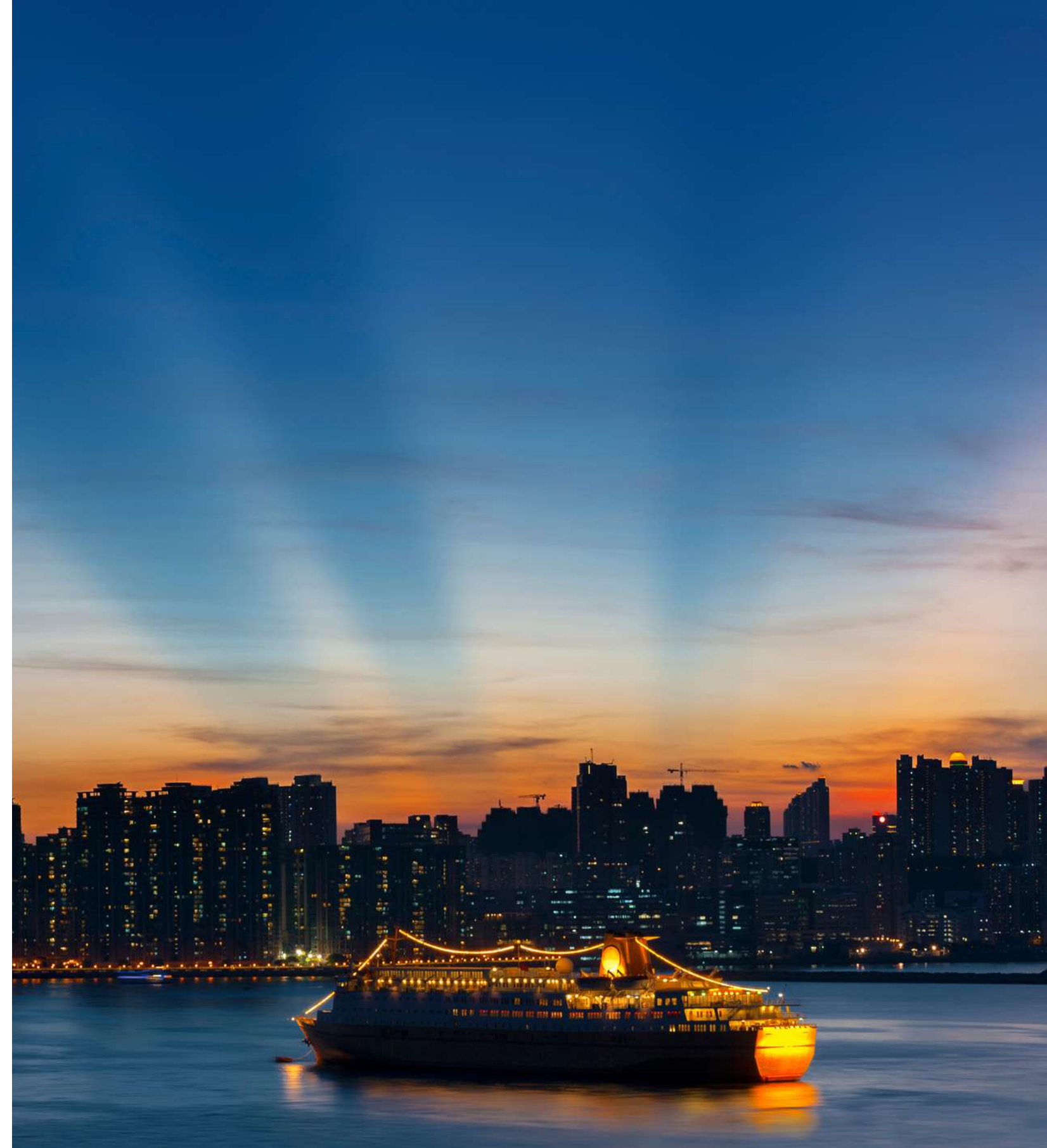
REVISED “VOTING RIGHTS” DEFINITION

- “Control” defined as > 30% or more of a co.’s voting rights
- “Voting rights” = voting rights that are “**currently** exercisable” at a co.’s general meeting
- Are voting rights “currently exercisable” if shares are subject to voting restrictions?
- **Proposed revision of “voting rights” definition** will clarify that voting rights are still exercisable despite voting restrictions
- Acquirer of 30% of a co.’s voting rights must make a Rule 26.1 mandatory general offer even if the voting rights cannot be exercised (e.g. due to an injunction)



SHAREHOLDERS' APPROVAL AND ACCEPTANCE: NOTE TO RULE 2.2(C)

- **Rule 2.2(c)** – requires a shareholders' resolution approving a delisting after a proposed offer to be subject to the offeror being entitled to exercise, and exercising, **rights to compulsorily acquire the remaining shares**
- If the offeree company is incorporated in a jurisdiction without compulsory acquisition rights, SFC will waive the requirement if the 3 conditions in the Note to Rule 2.2 are met
- **Proposed revision of condition (iii)** to expressly include purchases made by the offeror + persons acting in concert in determining whether the 90% of the disinterested shares threshold is met



RULE 2.11

- Rule 2.11 - offeror + its concert parties must have acquired 90% of offeree company's disinterested shares before exercising compulsory acquisition rights
- Rule 2.11 only allows purchases made by an offeror + its concert parties in the **4 months after the posting of the initial offer document**, + acceptances, to count -> 90% threshold
- **Proposed amendment** - purchases made by an offeror + its concert parties from the **date of the announcement of a firm intention to make an offer** until the **end of 4 months after the posting of the initial offer document** will count (with acceptances) -> 90% of the offeree company's disinterested shares threshold



RULES 2.2 AND 2.10

Rule 2.10 - a privatisation by way of scheme of arrangement requires:

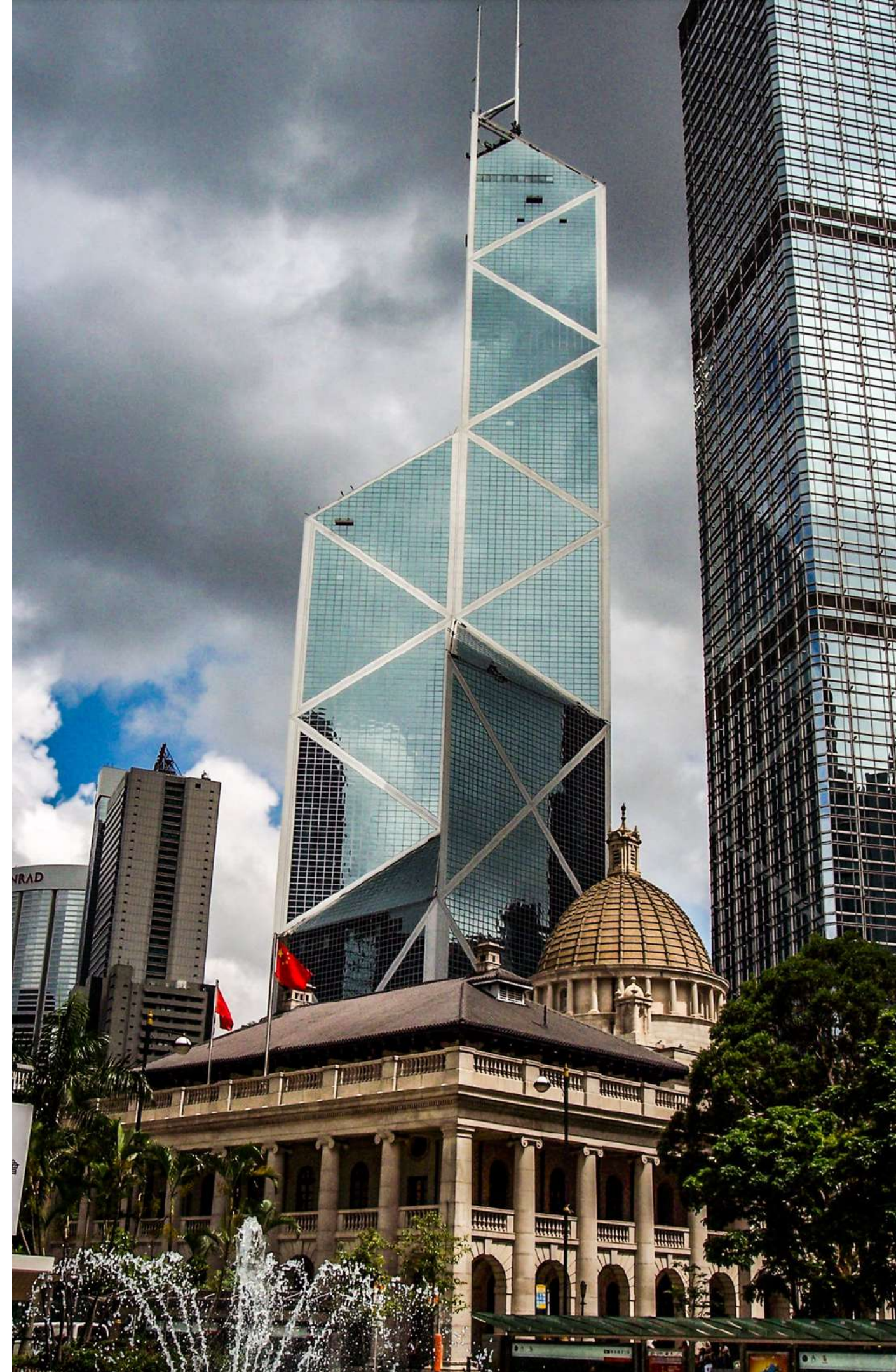
- scheme approval by >75% of votes attached to disinterested shares cast at **a duly convened meeting of the holders of disinterested shares** +
- number of votes cast against the resolution **at that meeting** to be < 10% of votes attached to all disinterested shares
- Different interpretations of required form of shareholders' meetings in HK court judgments (Re. Cosmos Machinery Enterprises Ltd + Re. Chong Hing Bank Limited)



RULES 2.2 AND 2.10 (CONT'D)

Proposed revision of Rules 2.10 + 2.2 to:

- refer to approval by > 75% of votes attaching to disinterested shares **cast either in person or by proxy at a duly convened meeting of “shareholders”** (rather than of “disinterested shareholders”) +
- add **new Note 8 to Rule 2** that a duly convened meeting of shareholders” (for the purposes of Rules 2.10 + 2.2) refers to a shareholders’ meeting duly convened ***in accordance with the offeree company’s constitutional documents and the company law of its place of incorporation***



IRREVOCABLE COMMITMENTS

Proposed amendments so that:

- offeror does not have to consult the Executive before approaching a shareholder with a **material interest** (>5% of offeree co's voting rights)
- offeror only has to consult the Executive before approaching shareholders **without a material interest** in the offeree
- offeror **cannot approach** more than **6 shareholders** (whether holding a material interest or not)



THE CHAIN PRINCIPLE

- Chain principle applies where a mandatory general offer obligation for a **2nd company. (a chain principle offer)** results from acquisition of control of **1st company.** because the 1st company controls 2nd company.
- 2 tests to determine if a “chain principle offer” is required - **Substantiality Test** + **Purpose Test** (Rule 26.1, Note 8)

Proposed amendments:

- Substantiality Test to require comparison of market capitalisation
- Look at ≥ 3 most recent financial periods to calculate if Substantiality Test produces an anomalous result
- Update PN 19 guidance on Substantiality Test



DEFINITION OF “OFFER PERIOD”

- PN 24 (Nov 2022) guidance on start of offer period when receivers or liquidators are appointed
- Once started, offer period ends only on occurrence of event in the “offer period” definition:
 - where the offer closes for acceptances, lapses, is withdrawn, or will not proceed **or**
 - where the offer allows election of alternative forms of consideration, the last date for making that election
- Executive has no explicit authority to end an offer period
- **Proposed amendment** will give Executive explicit power to terminate an offer period





LAST POSSIBLE DAY FOR DAY 60 IN PRIVATISATIONS + TAKE-PRIVATE TRANSACTIONS

- Under Rule 15.5(ii) - offeree board can consent to final day for an offer to become unconditional as to acceptances being extended **beyond the 60th day** after posting the composite document
- **Proposed amendment** will prohibit 'Day 60' from being extended beyond **4 months** after the date of the offer document

PUT UP OR SHUT UP ORDERS

- Put Up or Shut Up orders: issued by Executive (on application by offeree company.) + require the offeror to announce a firm intention to make an offer by a set deadline (**put up**) or that it will not proceed with an offer (**shut up**)
- Currently no express provision for Executive to issue Put Up or Shut Up Orders
- The proposed new Rule 3.9 will empower Executive to impose Put Up or Shut Up orders in exceptional circumstances

Executive to consider: current offer period duration; reason(s) for offeror's delay in issuing firm intention announcement; proposed offer timetable (if any); offer period's adverse effects on offeree company + conduct of parties to the offer

Rule 3.9 will also apply to Share Buy-Backs



SETTLEMENT OF CONSIDERATION + SHARE CERTIFICATE RETURN

Rule 20.1 - consideration for an offer must be paid within 7 business days from the later of:

- the date the offer becomes, or is declared, unconditional +
- the date of receipt of a duly completed acceptance

On offer lapse or withdrawal - share certificates must be returned within 10 days of offer's withdrawal or lapse (Rule 20.2)

Proposed amendment to Rule 20.2: On offer lapse or withdrawal - share certificates must be returned **no later than 7 business days after** offer's withdrawal or lapse



SHARE CERTIFICATE RETURN: SUCCESSFUL OFFERS

On successful offers (including partial offers) + **share buy-backs by general offer** - share certificates for **untaken shares + untendered shares** must be posted to or made ready for collection by accepting shareholders, **at the same time as the payment of consideration + no later than 7 business days** after later of:

- the date the offer becomes, or is declared, unconditional +
- the date of receipt of a duly completed acceptance

Untaken shares = shares tendered for acceptance but not taken up by offeror: **Untendered shares** = shares not tendered for acceptance represented by a share certificate also representing shares tendered for acceptance

Partial offer deadline for share certificate return: 7 business days after partial offer's close





SHARE CERTIFICATE RETURN: UNSUCCESSFUL OFFERS

- On offer withdrawal or lapse - offeror must, as soon as possible + **no later than 7 business days** after the offer withdrawal or lapse, return the share certificates lodged to offeree co.'s shareholders who accepted the offer
- Same timing applies to accepting shareholders who withdraw acceptance after 21 days from the first closing date of the offer, if the offer has not become unconditional as to acceptances

PROPOSED CHANGES TO TAKEOVERS CODE'S TIMING REQUIREMENTS

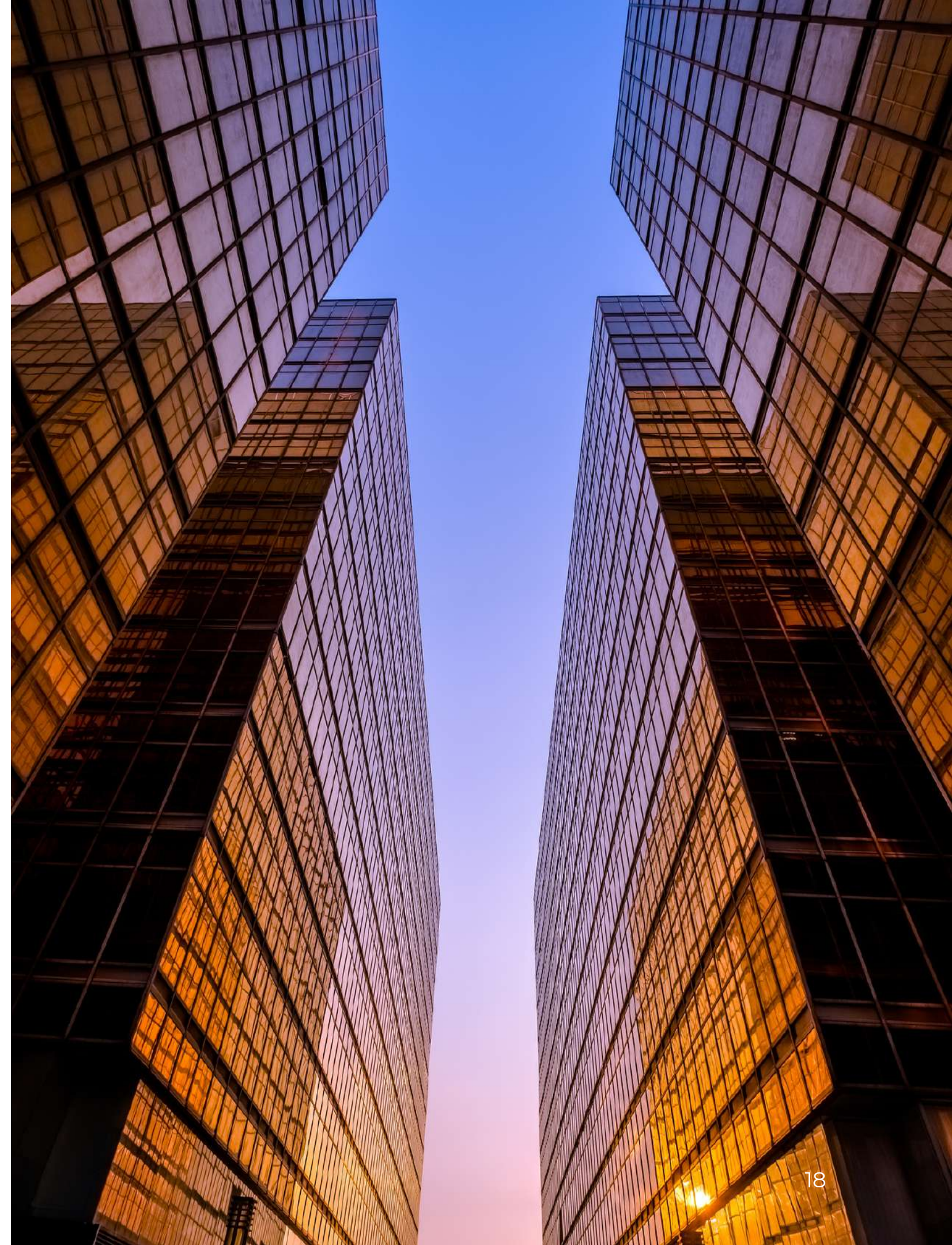
General housekeeping amendment: Day 1 = **the day after the event**

Offeree Directors' Resignation

Rule 7 amendment: offeree co. director's resignation cannot take effect until **after later of publication of:**

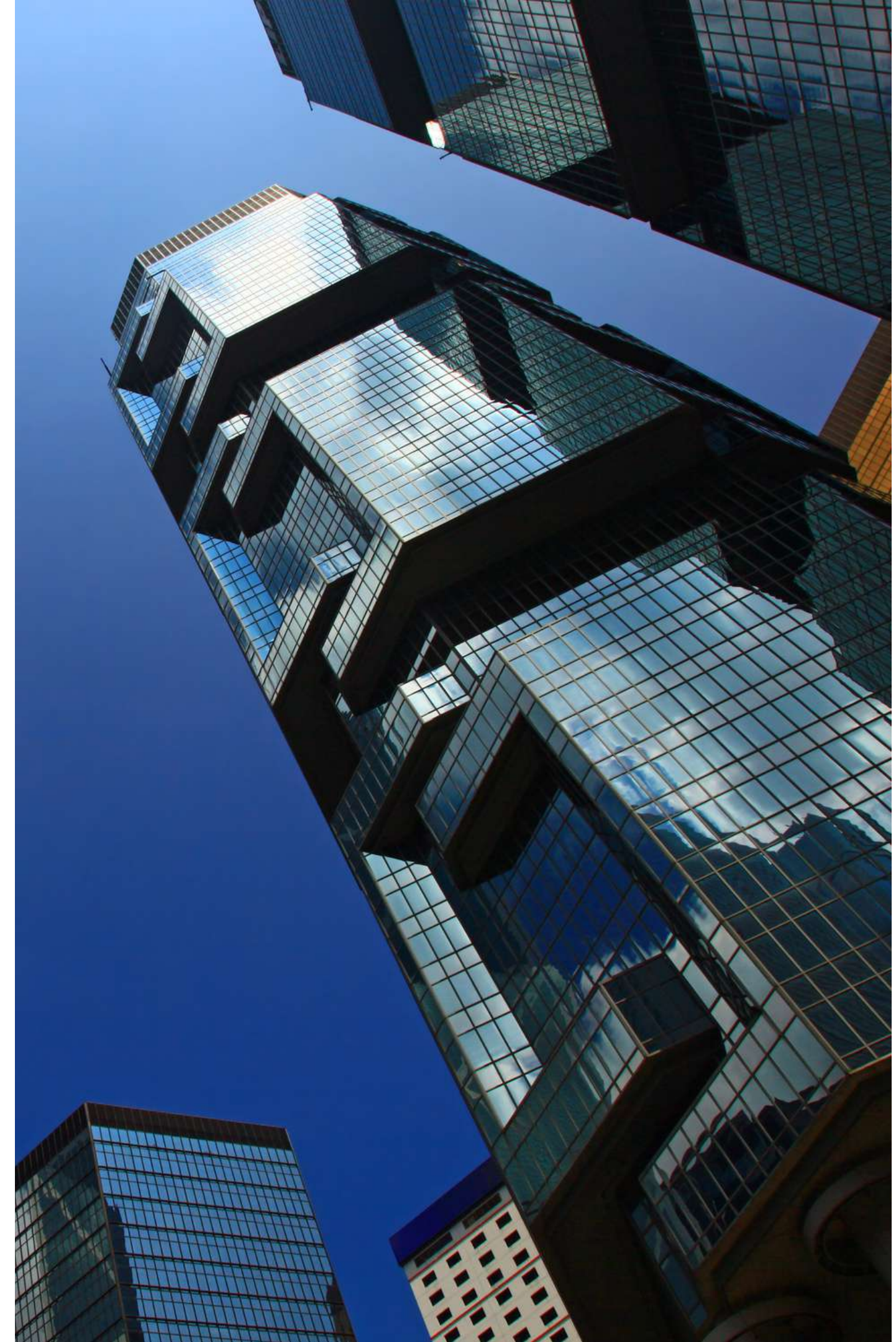
- closing announcement on the offer's first closing date +
- an announcement that the offer has become or been declared unconditional

On takeover offers involving a whitewash waiver, offeree co. director's resignation cannot take effect until after **publication of the results announcement** from the shareholders' meeting to approve the whitewash waiver



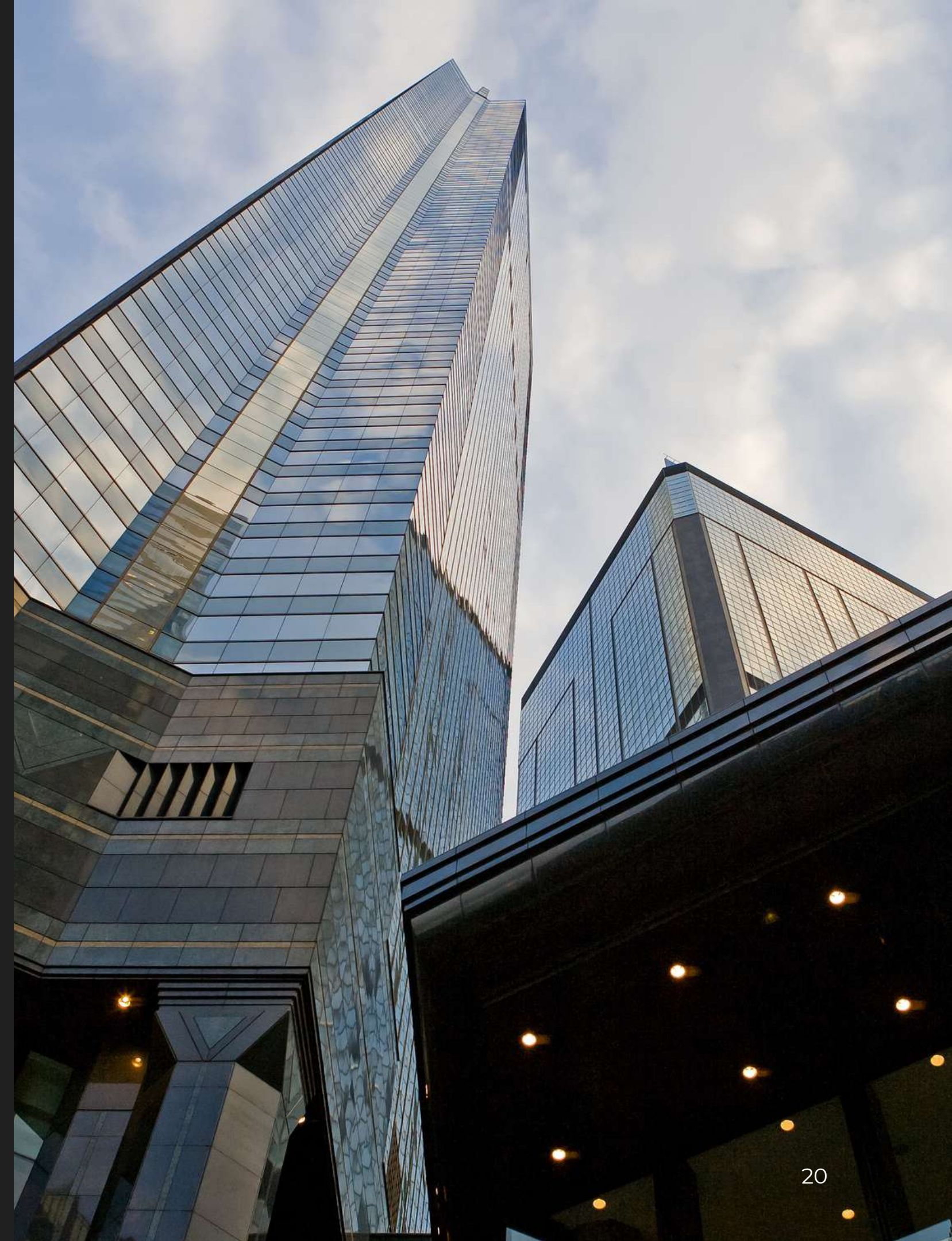
RULE 15.7

- Rule 15.7 - all conditions must be met or offer will lapse 21 days after the later of the first closing date + the date the offer becomes or is declared unconditional
- On privatisations by scheme of arrangement - scheme's effective date cannot be > 21 days after date of court meeting, without Executive's consent
- Executive currently grants waivers where timing cannot be met due to court's timetable
- **Proposed new Note** to Rule 15.7 – will remove need for Executive consent where a scheme's effective date occurs > 21 days after court meeting because of the court's timetable



OFFER PRICE DISCLOSURE PROHIBITED IN RULE 3.7 'TALKS ANNOUNCEMENTS'

- Strict approach to “**talks announcements**” to prevent use to condition the market + mitigate risk of impact on offeree’s trading price
- When issued, “talks announcement” should:
 - be short + only disclose that talks are taking place
 - not disclose indicative offer price or form of consideration
- New Note 4 - disclosure of indicative offer price is **not normally permitted** before announcement of a firm intention to make an offer, unless **exceptional circumstances** exist (eg. need to clarify an incorrect market rumour or offer price disclosure required under overseas regulations. Disclosed offer price will be the floor price for a subsequent offer
- New Note 3 - offeror will be bound by terms announced before firm intention announcement, unless right not to be bound is specifically reserved



DEDUCTING DIVIDENDS FROM THE OFFER PRICE

2019 Takeovers and Mergers Panel decision: Offeror could not deduct the final dividend from offer price in a mandatory general offer, if it had not reserved the right to do so

Proposed amendments to Rule 23.1 Note 11 + Rule 26.3 Note 3

- offeror cannot deduct amount of a dividend or other distribution subsequently paid or payable to offeree co.'s shareholders by offeree **from offer price**, unless it has **specifically reserved its right to do so in an announcement**
- where a dividend or other distribution is subject to withholding tax or other deductions, offer consideration should be reduced by the **gross amount** received or receivable by offeree co.'s shareholders



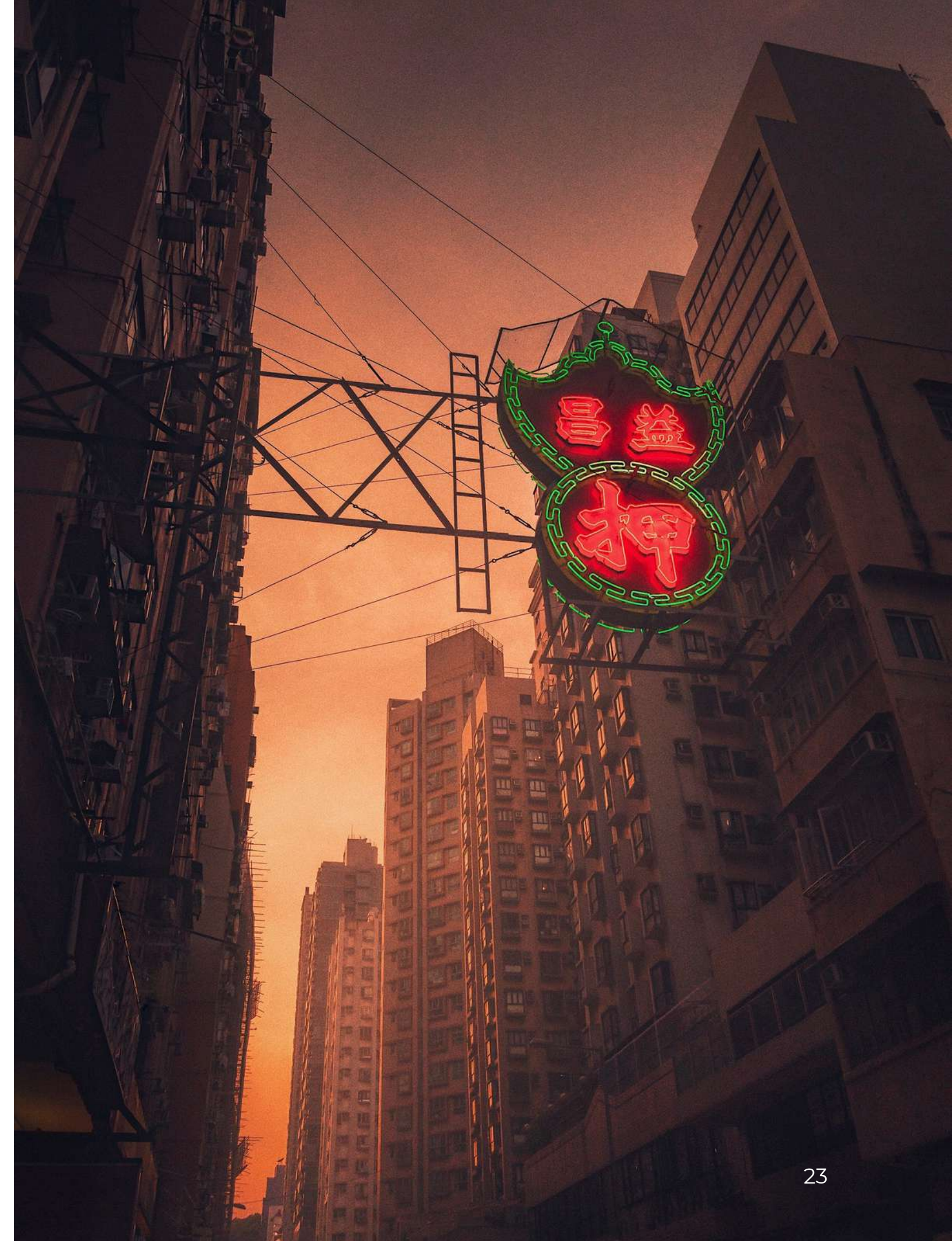
OFFER PERIODS FOR PARTIAL OFFERS

- Rule 28.5 - a partial offer must be conditional on obtaining approval of 50% of all independent shareholders if an offer may result in offeror holding > 30%
- That approval must be obtained on or prior to final closing day + no further offer period extension allowed after approval condition is met
- **Proposed amendment to Rule 28.4** - if, on a closing day, acceptances received > no. of shares stated in offer document (under Rule 28.7), offeror must declare partial offer unconditional as to acceptances + extend the final closing day to 14th day after that (but cannot further extend the final closing day)



OFFER PERIODS FOR PARTIAL OFFERS

- If the acceptance condition is met **before 1st closing day**, offeror must declare partial offer unconditional as to acceptances on day the acceptance condition is met + offer must remain open for acceptances for at least a further **14 days**
- If acceptance condition met **after 1st closing day** during an extended offer period - offeror must declare partial offer unconditional as to acceptances on day the acceptance condition is met + the final closing date **cannot be extended beyond the 14th day after that**



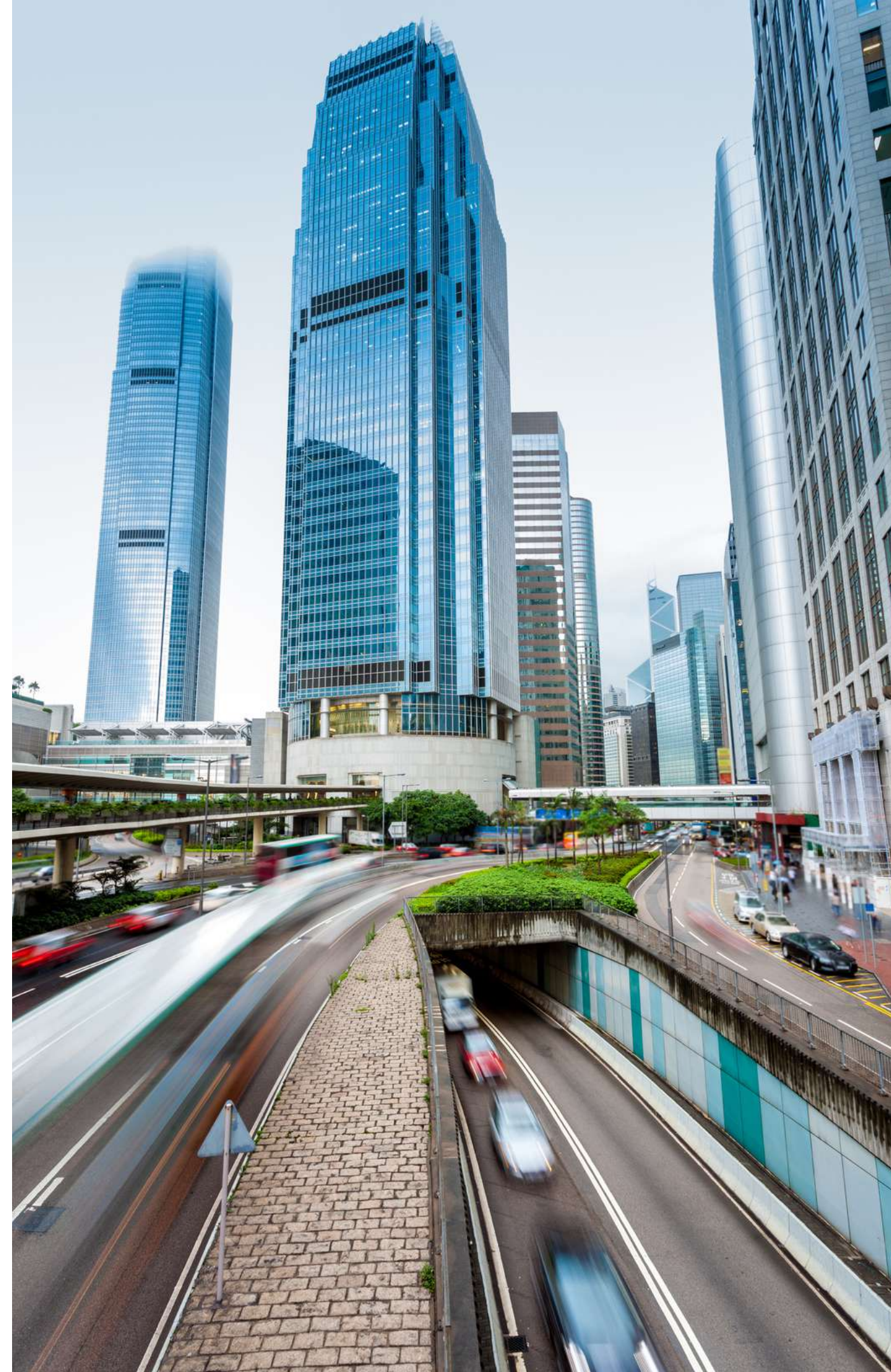
RULE 28.10 PARTIAL OFFERS: COMPARABLE OFFER FOR CONVERTIBLE SECURITIES, WARRANTS ETC.



- Codes lack explicit requirements for Rule 13 offers for convertible securities, options, warrants etc. on partial offers
- Proposed new Rule 28.10 - when an offer could result in an offeror holding > 30% of offeree co.'s voting rights + offeree co. has convertible securities, warrants, options, or subscription rights outstanding, offeror **must make appropriate offer or proposal to holders of these securities** (Rule 13 requirements will apply)

PARTIAL OFFERS: TICK-BOX APPROVAL REQUIREMENT

- Rule 28.5 “tick-box” approval condition requires offers to be conditional on majority approval of offeree’s independent shareholders, but this can be waived if an independent shareholder with > 50% of independent voting rights approves the partial offer
- **Proposed Rule 28.5 amendment to** clarify that “tick-box” approval condition **does not apply to partial offers** (i.e. offers within Rule 28.1(a) or (b))



ACCEPTANCE + APPROVAL OF PARTIAL OFFERS BY EXEMPT PRINCIPAL TRADERS

- Rule 35.4 prohibits exempt principal traders connected with an offeror or offeree co. from voting on an offer
- New Note 3 to Rule 28 will clarify that partial offers are subject to Rules 35.3 + Rule 35.4 - i.e.
 - exempt principal traders connected to an offeror or offeree must not vote on partial offers +
 - shares held by exempt principal traders connected to an offeror cannot be assented to an offer, until offer becomes or is declared unconditional as to acceptances



GREEN INITIATIVES: ELECTRONIC DOCUMENT DISSEMINATION

- New Rule 8.7 to give offeror + offeree co.'s option of sending code documents electronically
- PN20 to be revised to remove requirement for hard copy submission
- However, document sent in breach of applicable laws and regulations + constitutional documents will **not** be treated as having been sent or dispatched under Rule 8.7

Language Preference

- Rule 8.6 - documents to be printed and dispatched in Chinese + English
- Proposed new Note 2 to Rule 8.6 will allow issuers to send physical documents in English or Chinese, provided arrangements exist to ascertain recipients' language preference



ANNOUNCEMENTS OF UNLISTED OFFEREEES

- Proposed removal of Rule 12.2 requirement for unlisted offeree companies to publish announcements in leading English + Chinese newspapers (but will still need to send electronic versions to Executive for publication on SFC website)
- All submissions (including draft documents, ruling applications, financial resources confirmations, no material change confirmations + other reports, letters and confirmations required by the Codes + PN 20) must be made **by email to cfmailbox@sfc.hk**
- Rule 12.1 to be revised to require all documents to be filed electronically



DERIVATIVE DEFINITION

Definition of "**derivative**" to be revised to make clear that:

- Codes do not restrict dealings in, or require disclosure of, derivatives which are not connected with an offer or potential offer
- Revised Note will state that a derivative referenced to a basket or index including relevant securities will **not normally be regarded as connected with an offer** if, at the time of dealing, the relevant securities in the basket or index represent:
 - < 1% of the class in issue +
 - < 20% of the value of securities in the basket or index



ON-MARKET SHARE BUY-BACKS DEFINITION

- Off-market share buy-backs require approval of 75% of co.'s independent shareholders
- Proposed clarification that, for HKEX-listed shares, “**on-market share buy-back**” means a share buy-back:
 - by an HKEX-listed co. made through facilities of HKEx’s automatic order matching system or the equivalent order matching system of a recognised exchange
 - in which the co. buying back its shares + its directors are **not involved** (directly or indirectly) in the selection or identification of the share sellers



SPECIAL DEAL DISCLOSURE IN FIRM INTENTION ANNOUNCEMENTS

- Proposed prescribed disclosure under Rule 3.5 requiring vendor, offeror + offeree co.s to disclose details of **special deals** or an **appropriate negative statement** in announcements of a firm intention to make an offer and shareholders' documents
- **Proposed Note 14 to Rule 22** will remove requirement for **offeror's class (6) associates** to disclose dealings in offeree's relevant securities during **a cash offer**



FRUSTRATING ACTIONS

Proposed amendments will:

- clarify that Rule 4 list of frustrating actions is **non-exhaustive**
- state that Rule 4 requirements do **not normally** apply to prior contractual obligations to take an action (but poison pill arrangements likely to constitute frustrating actions)

Offeror's consent

- Note 1 to Rule 4 - shareholders' approval is not required if offeror consents to corporate action
- **Proposed amendment** - once offeror consents, no further Executive waiver is needed
- Where an announcement is made, sufficient to include a statement confirming that offeror's consent has been obtained
- If no announcement, offeror's consent to the corporate action must be lodged with Executive



DISCLOSURE OF MARKET PRICES OF OFFEREE + OFFEROR SECURITIES



- Para 10 of Schedule I sets out disclosure requirements re. closing price of offeree's securities + offeror's securities (if offer consideration includes offeror securities)
- **Proposed new Note to para 10** - if share trading is suspended during a trading day, closing price on the last full trading day + trading price immediately before the suspension, must be disclosed

APPLICATION OF RULE 31.1 TO WHITEWASH TRANSACTIONS

- Where an offer is withdrawn or lapses, Rule 31.1 prevents offeror + its concert parties from making further offer for offeree within **12 months** from date of previous offer's withdrawal or lapse
- If transaction is conditional on no general offer obligation being incurred, Rule 31.1 applies unless the right to waive that condition is reserved or, if the right to waive the condition is reserved, the waiver is not exercised
- **Proposed amendment** will apply Rule 31.1 to whitewash transactions: so no further offer allowed within **12 months of a whitewash waiver**
- Revised Note 4 will not prevent back-to-back non-waivable whitewash transactions



RULE 3.8 APPLICATION TO SHARE BUY-BACKS BY WAY OF GENERAL OFFER

- Proposed amendment to **Rule 5.1(c)** of Share Buy-backs Code will apply Rule 3.8 requirement for offerors + offerees to announce details of relevant securities to share buy-backs by way of general offer
- Rationale: to enable investors to determine if they are class (6) associates who need to comply with Rule 22 requirement to disclose dealings in relevant securities during offer periods



HOUSEKEEPING AMENDMENTS

- Proposed amendment to paragraph 2(a) of Schedule VI so that the grant of a Rule 26 whitewash waiver will be conditional on there having been no disqualifying transactions
- Will remove the limitation to disqualifying transactions in the period from 6 months before the announcement of whitewash proposals up to the date of the shareholders' meeting

