

Practice Note 2 (PN 2) – Issues relating to profit forecasts under Rule 10

Rule 10 of the Takeovers Code governs the treatment of profit forecasts and other financial information in the context of an offer or a possible offer. Where a document to shareholders includes information that constitutes a profit forecast under Rule 10 of the Takeovers Code, then the party issuing the forecast must obtain and publish an accountant's report and financial adviser's report on the forecast in accordance with Rule 10.4.

The purpose of this Practice Note is to clarify (i) the meaning of "reporting on" under Rule 10 of the Takeovers Code, (ii) the circumstances where Rule 10.4 may be relaxed; and (iii) the application of Rule 10.9 to unaudited quarterly results published by companies with dual listings.

I. Meaning of "reporting on" under Rule 10 of the Takeovers Code

Rule 10.1 and Note 1(c) to Rules 10.1 and 10.2 and Rule 10.4 of the Takeovers Code are relevant.

Reporting on a profit forecast involves (i) the financial advisers reviewing and discussing the assumptions with their client in order to satisfy themselves that the forecast has been made with due care and consideration; and (ii) the auditors or accountants satisfying themselves that the forecast, so far as the accounting policies and calculations are concerned, has been properly compiled on the basis of the assumptions made. Financial advisers and the auditors/accountants are not normally required to provide written confirmations to the Executive in relation to the above matters. In both cases it is normally sufficient for the relevant written confirmations, which form part of the report referred to in Rule 10.4 of the Takeovers Code, to be published in the document addressed to shareholders containing the profit forecast. If the profit forecast is made in an announcement, then the reports must be lodged with the Executive before the announcement is published and such reports must be published in the next document issued by the company to shareholders.

There may be occasions, particularly when an estimate relates to a period already ended, when no assumptions are required as

provided under Note 2(c) to Rules 10.1 and 10.2 of the Takeovers Code. For the avoidance of doubt, an estimate of profit for a period which has already expired should be treated as a profit forecast under Rule 10.6 (b). In these circumstances, instead of reviewing the assumptions, the financial advisers and auditors/accountants should review and report on the bases of the profit estimates.

II. Circumstances where Rule 10.4 may be relaxed

- (a) Financial projections published under the laws and regulations of an overseas jurisdiction

During the course of a Code-related transaction, an offeree company (or an offeror in the case of a securities exchange offer) may be required under the laws and regulations of an overseas jurisdiction to include certain financial projections in documents that are sent to shareholders containing details of the transaction. Such financial projections would normally be regarded as profit forecasts under Rule 10 of the Takeovers Code and would therefore need to be 'reported on' by both the offeree company's financial advisers and its accountants or auditors in accordance with Rule 10.4.

Notwithstanding this if the only reason for publishing the profit forecasts is that it is required by the laws and regulations of certain overseas jurisdictions (and is not otherwise proposed to be published by the offeree company) and the parties have encountered genuine practical difficulties (time-wise or otherwise) in meeting the reporting requirements set out in Rule 10.4, the Executive will normally be prepared to permit publication of the forecasts without full compliance with Rule 10. In this instance the profit forecasts must be accompanied by an appropriate warning that they do not meet the standard required by Rule 10 and that shareholders and potential investors should exercise caution in placing reliance on such forecasts in assessing the merits and demerits of the transaction. The Executive will also normally require the forecasts to be reported on as soon as reasonably practicable and the relevant reports to be contained in the next document to be sent to shareholders. This may require the issue of a supplemental document to shareholders if an offer document or whitewash document has already been sent out. In determining what constitutes "practical difficulties", the Executive will take into account the specific facts and circumstances of each case.

(b) Profit warning or positive profit alert announcements

During an offer period an offeree company may see the need to issue a profit warning or positive profit alert announcement pursuant to the Listing Rules and the inside information provisions under Part XIVA of the Securities and Futures Ordinance which took effect from 1 January 2013. The profit warning or positive profit alert announcements would normally be regarded as profit forecasts under Rule 10 of the Takeovers Code and would therefore need to be 'reported on' by both the offeree company's financial advisers and its accountants or auditors in accordance with Rule 10.4.

Often profit warning or positive profit alert announcements are issued almost immediately after the directors of the listed issuer come into possession of the relevant inside information. Given the time constraints faced by listed issuers when issuing these announcements, the Executive adopts a similar approach as described in subparagraph (a) above. In all cases involving this issue the Executive should be consulted at the earliest opportunity.

III. Unaudited quarterly results published by companies with dual listings

Companies with dual listings of their shares may publish unaudited quarterly results pursuant to a requirement under the relevant laws or regulations of the overseas jurisdiction during an offer period.

Rule 10.9 requires any unaudited profit figures published during an offer period to be reported on except with the consent of the Executive or in the following instances:

- (i) unaudited statements of annual or interim results which have already been published;
- (ii) unaudited statements of annual results which comply with the requirements for preliminary profits statements as set out in the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules");
- (iii) unaudited statements of interim results which comply with the requirements for half-yearly reports as set out in the Listing Rules in cases where the board of the offeree

company has not publicly advised its shareholders not to accept an offer;

- (iv) unaudited statements of interim results by offeror which comply with the requirements for half-yearly reports as set out in the Listing Rules, whether or not the offer has been publicly recommended by the board of the offeree company but provided the offer could not result in the issue of securities which would represent 10% or more of the enlarged voting share capital of the offeror

The Note to Rule 10.9 extends the exemptions from the reporting requirements to unaudited quarterly results of companies listed on the Growth Enterprise Market of the Stock Exchange (“GEM”).

The exemptions for companies listed on The Stock Exchange of Hong Kong Ltd (“Stock Exchange”) (either on the Main Board or GEM) from the reporting requirements contained in Rule 10.9 are appropriate as:

- (i) the relevant unaudited interim and quarterly figures and preliminary announcements of results are required to be published and prepared to the standards required by the respective applicable Listing Rules¹; and
- (ii) the unaudited figures must be included in a full-year audit in due course.

The Executive believes that if a company has a dual listing and is required by the relevant laws or regulations of the overseas jurisdiction to publish unaudited quarterly results the exemption from the reporting requirements in Rule 10.9 should also apply.

In relevant cases where a company with a dual listing wishes to take advantage of the exemptions from the reporting requirements in Rule 10.9 the Executive must be consulted at the earliest opportunity. Where appropriate the Executive may require the relevant party to apply for a formal ruling under section 8 of the Introduction to the Codes.

¹ See Appendix 16 to the Main Board Listing Rules and Chapter 18 of the GEM Board Listing Rules.

Rule 10.9 also provides that the Executive should be consulted in advance if a company is not listed on the Stock Exchange but wishes to take advantage of the exemptions under this Rule.

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