

Practice Note 7 (PN7) – Treatment of certain assets for the purpose of Rule 11.1(f)

Rule 11 of the Takeovers Code deals with asset valuations. Rule 11 provides that when valuations of assets are given in connection with an offer, details of the valuations must be included in the relevant document and should be properly supported by the opinion of a suitably qualified independent valuer. This helps to ensure that shareholders are provided with sufficient information to reach an informed decision on an offer as required by General Principle 5 of the Codes.

Some aspects of Rule 11 are unique to Hong Kong insofar as it imposes an obligation on a company to obtain an asset valuation in certain circumstances. There is no such requirement in the UK Takeover Code. The obligation to require an asset valuation under Rule 11 arises under Rule 11.1(f) which provides that "... a valuation of properties will be required in the case of an offer for a company with significant property interests and, in the case of a securities exchange offer, where the offeror company has significant property interests" (emphasis added). This requirement was introduced into the Codes to reflect the relatively high concentration and volatility of property companies listed in Hong Kong at the time.

Rule 11.1(f) provides further guidance on the meaning of "significant property interests":

"As a general guide, this should be taken to refer to a company or group of companies, the book value of whose property assets or consolidated property assets, respectively, exceeds 15% of the book value of total assets or total group assets, as the case may be" (emphasis added).

Recently some market practitioners have voiced concerns that strict compliance with Rule 11.1(f) may in some circumstances be unduly burdensome. These practitioners have suggested that certain assets should not be regarded as property assets for the purpose of calculating the 15% threshold even though they may be listed on a company's balance sheet as "buildings" or "plant and buildings". For example, it has been suggested that account should not be taken of properties of a mining company which are used

for smelting or storage purposes or infrastructure such as roads at the mining sites.

The Executive agrees that in some circumstances the strict application of Rule 11.1(f) may be unduly burdensome and should be decided on a case-by-case basis. If parties or their advisers are in doubt as to whether certain assets should be taken into account for the purpose of calculating the 15% threshold, they should consult the Executive at the outset of the transaction. The Executive may request to see a list of the assets including a detailed description of their nature, location, size, book value and any other characteristics or relevant information which would assist in its consideration of the matter.

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