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SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

Takeovers Bulletin

Highlights

- Treatment of right-of-use assets for Rule 11.1(f)
- Reminder to liquidators on disclosure obligations
- Talks announcement in a competitive situation
- Quarterly update on activities of Takeovers Team

Further guidance on treatment of right-of-use assets for the purposes of Rule 11.1(f)

The Executive has recently been consulted on how certain leased assets should be treated under Rule 11.1(f) of the Takeovers Code.

Under Rule 11.1(f), if the book value of the consolidated property assets of the offeree company exceeds 15% of its consolidated total assets, normally a valuation of the property assets held by the offeree company is required. When the relevant percentage is 50% or above, property assets held by the associated companies of the offeree company should also be valued. The requirements apply similarly to the offeror when its shares are included in the offer consideration.

The purpose of Rule 11.1(f) is to enable shareholders to make an informed assessment of the offer, taking into account the valuations of significant property interests held by the offeree company and the offeror[1] vis-à-vis their book values (for example, whether there is any material revaluation difference).

The valuation requirements are intended to cover both ownership in land and buildings and leasehold interests which give the lessee the substantive risks and rewards of ownership of the leased land or buildings (collectively, "**Relevant Property Interests**"), such as unilateral right(s) to transfer, sublet, mortgage or otherwise dispose of the interests without the consent of the lessor. One example is the long-term land lease granted by the HKSAR Government.

Regarding *other* leasehold interests[2] relating to land or buildings (eg, short-term leases), we recognise that typically a property valuer does not ascribe any commercial value to such interests and therefore it may be misleading to use the book value of these interests as a proxy for their significance for the purpose of Rule 11.1(f).

1 In the case of a securities exchange offer.
2 Under IAS 17 (or its equivalent HKAS17), such other leasehold interests were classified as operating leases, where the leased assets were off-balance sheet and therefore did not form part of a company's assets. In contrast, with IFRS 16 (or its equivalent, HKFRS 16) coming into effect on 1 January 2019, ROU assets need to be recognised in respect of all leases, regardless of whether the underlying interests are determined by a property valuer to have any commercial value.

For the purpose of calculating the percentages referred to in Rule 11.1(f), we would normally permit exclusion of right-of-use (ROU) assets unless the underlying leasehold interests are analogous to ownership in property. This approach is, strictly speaking, a waiver of Rule 11.1(f), and was adopted to uphold the spirit of the rule amidst changes in the financial reporting standard for leases in 2019. Otherwise, there could be an anomaly whereby a company with significant "operating leases" (as defined under IAS[3] 17 or HKAS[4] 17) and insignificant Relevant Property Interests could become obliged to obtain a valuation of its property interests (most of which may be determined to have no value in a property valuation) solely due to the recognition of ROU assets under IFRS[5] 16 (or HKFRS[6] 16).

We notice that calculations submitted by market practitioners in some past cases excluded the ROU assets in question from only "consolidated property assets" without adjusting "consolidated total assets". In a majority of cases, the ROU assets involved were not significant. However, as the purpose of the exclusion is to mitigate the impact of IFRS 16 (or HKFRS 16) on the operation of Rule 11.1(f) and not to make it harder for the percentage thresholds to be reached, the Executive believes that if a company wishes to exclude certain ROU assets on the basis that their value as determined by a property valuer is zero, it would be more appropriate to apply this basis consistently and deduct the book value of the relevant ROU assets from both the numerator and denominator of the percentage calculations accordingly. This calculation method ensures that a company holding significant Relevant Property Interests would not fall outside the scope of Rule 11.1(f) solely because of the recognition of ROU assets. We have revised Practice Note 7 to clarify how the waiver works.

If any parties would like to exclude any assets from the percentage calculations or the valuation requirements under Rule 11.1(f), they should consult the Executive at the outset of their preparation for the relevant offer.

The revised Practice Note 7 can be found in the "Regulatory functions – Corporates – Takeovers and mergers – Practice notes" section of the SFC website.

Reminder to liquidators[7] of offeree companies on disclosure obligations

Rule 3.7 of the Takeovers Code provides that after a potential offeror or the offeree company has announced that talks are taking place or an offer is being contemplated, monthly updates must be made to set out the progress of the talks or the consideration of the possible offer[8].

3 International Accounting Standards.
4 Hong Kong Accounting Standards.
5 International Financial Reporting Standards.
6 Hong Kong Financial Reporting Standards.
7 References to "liquidator(s)" in this Bulletin include references to "provisional liquidator(s)" as well.
8 Until the potential offeror has announced its firm intention to make an offer in accordance with Rule 3.5 of the Takeovers Code or the offer period is closed (whichever is earlier).

Where an offeree company becomes the subject of a winding-up petition after a Rule 3.7 announcement, it[9] remains obliged[10] to comply with the Takeovers Code and keep the market informed of the possible offer by way of an announcement on the Hong Kong Exchanges and Clearing Limited's website[11], such as when a formal winding up order was granted and whether talks with the potential offeror are continuing.

The responsibility to ensure the offeree company's compliance with the Takeovers Code shall rest with its liquidator as soon as it is appointed to take control of the offeree company's affairs and assets in place of directors. Liquidators are reminded to submit draft monthly updates or other offer-related documents to the Executive for comment before publication.

To ensure accuracy of the "offer periods" information on the SFC website, timely input from liquidators of the offeree company and the offeror is of vital importance.

As always, the Executive should be consulted at the earliest opportunity if there is any doubt about the application of the Takeovers Code. Depending on the circumstances, liquidators of the offeree company and the potential offeror may need to seek help from financial and legal advisers as well.

Talks announcement in a competitive situation

In a competitive situation, where an offeror has issued a firm intention announcement under Rule 3.5 of the Takeovers Code, it is possible that the competitor is still contemplating whether or not to make an offer. To the extent the possible competing offer is already announced in a Rule 3.7 talks announcement, shareholders would reasonably wish to take into account the intention of the potential competing offeror (including the terms of its offer) in making decisions with regard to their shares in the offeree company. Such information is particularly relevant when the first offeror has already issued its offer document and shareholders are being invited to accept the offer before the closing date.

One of the principal objectives of the Takeovers Code is to provide an orderly framework within which takeovers are conducted[13]. It is important that shareholders be given sufficient information and time to reach an informed decision on an offer[14].

Under Rule 3.9 of the Takeovers Code, the offeree company may request the Executive to set a time limit for a potential competing offeror to clarify its intention. The Executive may also exercise its power to impose such a time limit on the potential competing offeror, if it considers it appropriate to do so, even when a request has not yet been made by the offeree company.

9 The responsibility for making an announcement about a possible offer may also rest with the potential offeror in certain circumstances. See Rule 3.1 of the Takeovers Code for details.
10 Provided that the offeree company remains primarily listed in Hong Kong or is otherwise a public company in Hong Kong.
11 Or on the SFC website if the offeree company is an unlisted public company.
12 Please email to takeovers@sfc.hk.
13 For example, the Takeovers Code sets out a standard timetable following a Rule 3.5 announcement, comprising a window of up to 35 days for posting the formal offer document to offeree company shareholders (Rule 8.2), a further 60 days within which the offer must become or be declared unconditional as to acceptances (Rule 15.5), and a further 21 days within which all other conditions to the offer must be fulfilled (Rule 15.7).
14 See General Principle 5.

In reaching a decision on whether and how long a time limit should be imposed on a potential competing offeror to announce either a firm intention to make an offer in accordance with Rule 3.5 or that it does not intend to make an offer, the Executive will take into account all relevant factors[15] including:

(a) the current duration of the offer period[16];

(b) the reason(s) for the potential competing offeror's delay in issuing a firm intention announcement;

(c) the proposed offer timetable (if any);

(d) any adverse effects that the offer period has had on the offeree company; and

(e) the conduct of the parties to the offer.

As explained in Issues No. 37 (June 2016) and No. 53 (June 2020) of the *Takeovers Bulletin*, as long as the parties involved in a possible offer keep the matter confidential, normally there should not be a need to issue a "talks" announcement prior to a Rule 3.5 announcement[17]. We would like to remind any potential offeror, offeree company and their advisers that they must take reasonable steps to prevent leakage of information when discussions are still preliminary and the relevant offer may or may not materialise[18].

Quarterly update on the activities of Takeovers Team

From January to March 2025, we received 19 takeovers-related cases (including privatisations, voluntary and mandatory general offers, and off-market and general-offer share buy-backs), five whitewashes and 71 ruling applications.

Useful links

- The Codes on Takeovers and Mergers and Share Buy-backs
- Practice notes
- Decisions and statements
- Previous *Takeovers Bulletins*

15 See Note to Rule 3.9 of the Takeovers Code.
16 For example, the duration for which it has been announced that the potential competing offeror is contemplating an offer, the date on which the first offer is expected to be closed as disclosed in the relevant offer document and the final day to which the closing date for the first offer may be extended under Rule 15.5 of the Takeovers Code.
17 To the extent permitted under applicable laws and regulations (such as the safe harbour provisions under Part XIVA of the Securities and Futures Ordinance).
18 Rule 1.4 of the Takeovers Code.

All issues of the *Takeovers Bulletin* are available under 'Published resources – Newsletters – Takeovers Bulletin' on the SFC website at www.sfc.hk.

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