

A periodic newsletter to help participants in Hong Kong's financial markets better understand the Codes on Takeovers and Mergers and Share Repurchases

Takeovers Panel's decision in relation to China Gas

Offerors asked to clarify statements on offer price

The Takeovers and Mergers Panel (Panel) has ruled that certain statements made on 26 March 2012 by Fu Chengyu, chairman of China Petroleum & Chemical Corporation (Sinopec) did not constitute a "no increase statement" under Rule 18.3 of the Code on Takeovers and Mergers but were ambiguous and created uncertainty as to whether or not Sinopec and ENN Energy Holdings Limited (ENN, and together with Sinopec, the Offerors) were ruling out the possibility of an increase in the offer price in relation to their pre-conditional voluntary general offers for the shares and options (Offers) of China Gas Holdings Limited (China Gas).

The Panel required the Offerors to issue a clarification announcement, as previously requested by the Executive, and to state specifically whether or not they rule out the possibility of an increase in the offer price. An announcement in compliance with the ruling was issued on 3 April 2012.

Statements Offerors made

On 12 December 2011, the Offerors jointly announced a pre-conditional voluntary general offer for shares and options in China Gas at the offer price of \$3.50 per China Gas share. The making of the Offers is subject to the satisfaction of certain pre-conditions, including, amongst others, various regulatory approvals of mainland China and approval of the shareholders of ENN. The Offers will be conditional on, amongst other things, acceptances being received that would result in the Offerors holding more than 50% of the voting rights of China Gas.

Fu Chengyu, chairman and executive director of Sinopec made certain statements to the media on 26 March 2012. An English translation of the statements as submitted by the legal advisers to the Offerors is as follows:

Highlights

- Takeovers Panel's decision in relation to China Gas Holdings Limited
- Disciplinary action against Capital VC Limited and Yau Chung Hong
- Addition to the Post-Vet List and revision of Practice Note 5
- Quarterly update on the activities of the Takeovers Team for the period ended 31 March 2012

“Regarding the acquisition of China Gas, we and ENN Energy have provided an offer price, which reflects fair value given to China Gas in accordance with market circumstances. As to whether or not there will be an increase to the offer price, we do not have to complete this acquisition just for the sake of completing an acquisition. We cannot overpay by paying a price which is above market. And I believe the price we are offering is a price that has taken into account the market prices.”

On 27 March 2012, the statements were widely reported in the media, with a range of interpretations of their meaning.

On 27 and 28 March 2012, the Executive made repeated requests to the Offerors to issue a clarification announcement as to whether Fu had made any “no increase statement” or to withdraw the statements. The Offerors declined to do so. The matter was then referred to the Panel on 29 March 2012 as there were particularly novel, important or difficult points at issue. The Panel noted that the Offerors had been afforded every opportunity to clarify the statements publicly, but chose not to do so. The Panel expressed its regret that it was even necessary to hear this case. The Panel also emphasised that when the Executive asks a party to an offer to publish a clarification of statements made by its officials, that request should be acceded to without delay unless there are very good reasons to challenge the Executive’s position. The Panel saw no good reasons in the present case for the Executive’s position to be challenged.

Practitioners reminded to co-operate fully with the Executive

The Panel reminded offerors and their advisers of General Principle 6, which requires that “[p]arties involved in offers must take care that statements are not made which may mislead shareholders on the market.”

In particular, the Panel reminded Citigroup Global Markets Asia Limited, the financial adviser to the Offerors, of Note 1 to Rule 9.1, which states that it is the financial advisers who are responsible for guiding their clients with regard to any information released in relation to an offer.

The Panel also specifically reminded practitioners that General Principle 10 requires that “[a]ll parties concerned with transactions subject to the Code are required to co-operate to the fullest extent with the Executive ...”

The full written decision of the Panel can be found in the section “Prospectuses, Takeovers & Mergers” – “Takeovers & Mergers” – “Panel and Executive Decisions / Statements” – “Panel Decisions / Statements” of the SFC Web site.

Disciplinary action against Capital VC and Yau Chung Hong

On 22 May 2012, the Executive publicly censured Capital VC Limited (Capital VC) and Yau Chung Hong in relation to their breach of the mandatory offer obligation requirement in Rule 26.1 of the Takeovers Code. The Executive also imposed a cold shoulder order denying Yau direct or indirect access to the Hong Kong securities markets for 18 months until 22 November 2013.

Capital VC is an investment company under Chapter 21 of the Listing Rules, whose principal business involves investing in listed and unlisted companies in Hong Kong and the mainland China. Yau was an executive director, a substantial shareholder and a member of Capital VC’s investment committee.

On 10 June 2011, Yau and Capital VC increased their collective shareholding in Longlife Group Holdings Limited (Longlife), a GEM board listed company, to 30.19%, thereby triggering a mandatory general offer obligation under Rule 26.1 of the Takeovers Code. Upon becoming aware of the fact that Yau and Capital VC collectively held an interest of 30% or more of Longlife, the Executive asked them to comply with the mandatory general offer requirement and make a general offer for Longlife forthwith. In an announcement issued by Capital VC on 17 August 2011, Yau and Capital VC stated, among other things, that they would not make a general offer for Longlife.

At all material times Yau managed two investment accounts, one for Capital VC and one for his personal investments. He was the sole decision-maker in executing trades in Longlife shares for Capital VC's account and for his own account. He claimed that he had acquired excessive Longlife shares because of wrong calculations. While Yau was aware of the need to keep the collective shareholding of Capital VC and himself in Longlife below 30%, there was no evidence that he had made any serious effort to put in place effective compliance procedures. Yau's actions directly led to the breach of Rule 26.1 of the Takeovers Code.

Capital VC and its investment committee relied solely on Yau to monitor his and Capital VC's relevant holdings in Longlife. Although both the investment committee and Mr Yau were fully aware of the possible general offer implications of purchases of Longlife shares under the Takeovers Code, they adopted wholly inadequate measures to ensure compliance with applicable regulatory requirements. In these circumstances the Executive believes that Capital VC must also bear responsibility for Mr Yau's action and the consequent breach of the Takeovers Code.

The Executive believes that Yau's and Capital VC's conduct resulted in a serious breach of a fundamental provision of the Takeovers Code, which merited strong disciplinary action. The Executive therefore imposed an 18-month cold shoulder order against Yau and publicly censured both him and Capital VC in relation to their conduct in this matter.

Both Yau and Capital VC accepted that they had breached Rule 26.1 of the Takeovers Code and agreed to the disciplinary action taken against them under section 12.3 of the Introduction to the Takeovers Code.

The Executive wishes to take this opportunity to remind practitioners and parties who wish to take advantage of the securities markets in Hong Kong that in matters relating to takeovers and mergers they should act in accordance with the Takeovers Code. If they do not, they may find by way of sanction, that the facilities of such markets are withheld in order to protect those who participate in Hong Kong's securities markets.

The Executive Statement dated 22 May 2012 can be found in the section "Prospectuses, Takeovers & Mergers" – "Takeovers & Mergers" – "Panel and Executive Decisions / Statements" – "Executive Decisions / Statements" of the SFC website, and the cold shoulder order under "Prospectuses, Takeovers & Mergers" – "Takeovers & Mergers" – "Panel and Executive Decisions / Statements" – "Current Cold Shoulder Orders" of the SFC Web site.

Addition to the Post-Vet List and revision of Practice Note 5

On 25 June 2010, the Executive relaxed the pre-vetting requirement under Rule 12.1 of the Takeovers Code for certain announcements of a routine nature by introducing the Post-Vet List under the Note to Rule 12.1. The Post-Vet List sets out the types of documents that will not be subject to the Executive's prior comment under Rule 12.1. Practice Note 5 provides practical and prescriptive guidance to parties and their advisers in respect of documents that appear in the Post-Vet List.

Since the implementation of the new post-vetting regime the Executive is pleased to note that overall market practitioners have complied with the new requirements without difficulty. The Executive recently decided to add Rule 3.8 announcement to the Post-Vet List, in view of the factual and straight-forward nature of information routinely required to be disclosed under Rule 3.8.

When an offer period begins, Rule 3.8 requires an offeree company to announce, as soon as possible, details of all classes of relevant securities issued by it, together with the number of such securities in issue. An offeror or a potential named offeror must also announce the same details of its relevant securities unless it is stated that the offer is likely to be solely in cash. Rule 3.8 further requires that if any previously announced information changes during an offer period, a revised announcement must be made as soon as possible.

Where the number of relevant securities in issue changes during an offer period as a result of events, such as exercise of share options or warrants, conversion of convertible securities, or their lapse, cancellation or expiry, the Executive would expect the following to be disclosed (i) the event that led to the change in the number of relevant securities; (ii) the number of relevant securities involved (eg, number of relevant securities newly issued or lapsed); and (iii) the up-to-date position of each class of relevant securities immediately following the relevant event.

Given their routine and factual nature, the Executive considers Rule 3.8 announcements that are issued on a stand-alone basis (whether in the form of an initial announcement or subsequent ones) to be appropriate for post-vetting. However, if the relevant announcement contains additional information relating to other material matters or Code provisions, the announcement would not be considered as falling within the Post-Vet List for the purposes of the Note to Rule 12.1. The relevant announcement, therefore, would be required to be submitted to the Executive for comment under Rule 12.1 of the Takeovers Code before its publication. This would be the case in the majority of initial announcements that commence an offer period, issued under Rule 3.7 or Rule 3.5 of the Takeovers Code, which typically include details of relevant securities referred to in Rule 3.8.

In all announcements that fall within the Post-Vet List, parties and their advisers must consult the Executive at the earliest opportunity if there is any doubt as to whether an announcement qualifies for post-vetting (see Note 2 to Rule 12 of the Takeovers Code).

The revised Post-Vet List will now contain the following types of announcements:

- Announcements of the appointment of independent financial advisers under Rule 2.1;
- Announcements of the despatch of circulars under Rule 8 or Rule 25;
- Announcements of delay in the despatch of circulars under Rule 8.2 or Rule 8.4;
- Announcements of the appointment and resignation of directors of the offeree company under Rule 26.4 and Rule 7;
- Announcements of placing and top-up transactions under Note 6 on dispensations from Rule 26; and
- Announcements of numbers of relevant securities in issue under Rule 3.8.

The updated Post-Vet List can be found in the section "Prospectuses, Takeovers & Mergers" – "Takeovers & Mergers" – "Post-Vet List" of the SFC website.

Corresponding changes and other changes to reflect the amendments to the Takeovers Code in March 2012 have been made to Practice Note 5. The updated Practice Note 5 can be found in the section "Prospectuses, Takeovers & Mergers" – "Takeovers & Mergers" – "Practice Notes" of the SFC Web site.

Update on takeovers-related cases

In the three months ended 31 March 2012, the Executive dealt with 14 takeovers-related cases (including privatisations, voluntary and mandatory general offers and off-market and general-offer repurchases) and three whitewashes. The Executive also received 38 ruling applications.

The Takeovers Panel met once during this three-month period on policy-related issues.

The Takeovers Bulletin is available under 'Speeches, Publications & Consultations' – 'Publications' of the SFC website at <http://www.sfc.hk>.

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