29 October 2008

General offer trigger point and creeper under Takeovers Code upheld

The Securities and Futures Commission (SFC) has noted recent suggestions from some market participants that, in light of current market conditions, the 30% general offer trigger point and 2% creeper under the Takeovers Code should be relaxed temporarily. It has been suggested that relaxation of the relevant provisions would allow companies and their major or controlling shareholders to exhibit their confidence in the prospects of the company without incurring a mandatory takeover offer.

Rule 26.1 of the Takeovers Code provides that a person and his concert parties will incur a general offer obligation if they acquire voting rights that will increase their holdings to 30% or more of a company. For those who are holding voting rights between 30% and 50%, a general offer will be required if they acquire more than 2% in 12 months.

The cornerstone of Rule 26.1 is the affordability of fair treatment for shareholders. The underlying principle is that: if control of a company changes, a general offer to all other shareholders is normally required. The general offer trigger and creeper thresholds were reduced from 35% and 5% to 30% and 2% on 19 October 2001 respectively following extensive market consultation. The reductions were driven by market expectations of an alignment of the Hong Kong regulations with those adopted in other leading markets including the United Kingdom. The United Kingdom regulations are indeed stricter as they do not have a creeper provision.

The Takeovers Code does not have the force of law. It represents a consensus of opinion of those who participate in Hong Kong's financial markets and the SFC regarding standards of commercial conduct and behaviour considered acceptable for takeovers, mergers and share repurchases.

The Takeovers Panel has met at the request of the Takeovers Executive to give its view on whether, and if so to what extent, the trigger and creeper provisions in the Takeovers Code should be relaxed in light of current market conditions. The Takeovers Panel consists of 27 members drawn from the financial and investment community.

The Takeovers Panel by a substantial majority was opposed to any relaxation of the provisions of the relevant rules for the following reasons:

1. the proposals ran counter to General Principle 1 of the Takeovers Code which requires equality of treatment for all shareholders; this is an absolutely fundamental principle underpinning the regulation of takeovers and mergers in Hong Kong;
2. no jurisdiction that had a similar regulatory framework as Hong Kong had proposed temporary waivers of important provisions of their takeovers regulations in response to recent market conditions;
3. the proposals, were they to be implemented, would likely reflect poorly on Hong Kong as an international financial centre. In this regard, it is noted that the temporary waiver of the 35% trigger and 5% creeper in 1987 was subject to criticism;

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4. while the stock market had experienced substantial declines in prices, there was no suggestion that it was not functioning properly;
5. the proposals were opportunistic in that they appeared to be motivated more by the interests of major or controlling shareholders than the market as a whole;
6. they would be seen as favouring big business interests at the expense of other stock market participants and, in fact, may work against their interests; and
7. there was no evidence to indicate that support for the proposals was widespread or that the proposals would boost confidence in the market for the shares of particular companies or the market as a whole.

The Takeovers Panel also noted that off-market company share repurchases, share repurchases by general offer and partial offers that are conducted in compliance with the current provisions of the Takeovers and Share Repurchase Codes, could all be employed to increase a major or controlling shareholder's interest without triggering a mandatory takeover offer. Market participants are reminded that there is a mechanism in the Takeovers Code for shareholders' approval of any partial offers, which could result in the offeror holding 30% or more of the voting rights in the company. These existing provisions of the Takeovers Code allow companies and their major or controlling shareholders to exhibit their confidence in the prospects of the company in a manner that does not violate the fundamental principle of fair treatment of shareholders or give rise to the possible adverse consequences, as described above, and does not require any temporary waiver of important provisions of the Takeovers Code.

End

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