Revised Practice Note 1 (PN1) – Partial offers

Although partial offers are relatively rare in Hong Kong the Takeovers Executive has received a number of enquiries about the application of Rule 28 of the Takeovers Code and would like to clarify its application in certain areas.

A partial offer is an offer to shareholders to buy a specified number (but not all) of shares which carry voting rights of a company not already held by the offeror and its concert parties. In addition to the General Principles and Rules of the Takeovers Code a partial offer is specifically governed by Rule 28 of the Takeovers Code.

A partial offer may be made in the following two ways:

■ **Share register method** – This is where an offer is made for a specific proportion of each shareholder's shares that are registered in his name on the record date. In this instance an accepting shareholder is assured that a minimum number of the shares held by him on the record date will be accepted by the offeror if the offer becomes unconditional.

For example, if an offeror holding no shares offers to buy 40% of the offeree company's shares an accepting shareholder holding 100 shares on the pre-determined record date may tender 40 shares (i.e. 40% of his holding) or less and be assured that, if the offer completes, all of those shares will be taken up by the offeror. The shareholder is therefore free to hold on to or sell his remaining 60 or more shares. Alternatively, in anticipation of some shareholders not accepting the offer, the shareholder may tender some or all of his remaining shares as excess applications for the offeror to take up and reach his target of 40%.

Limitations of the share register method

Under the share register method, a record date to ascertain assured acceptances, and where relevant entitlements to vote (see Rule 28.5), must be announced along with the terms of the partial offer in the announcement of a firm intention to make the partial offer (issued under Rule 3.5 of the Takeovers Code).

Typically the record date is set at 4:00 pm on the same date as the "first closing date" of an offer which must be at least 21 days (and normally not more than 60 days) from the date on which the offer document is posted to shareholders (Rule 15 of the Takeovers Code). It follows that only those shares voted and/or tendered by shareholders whose names appear on the share register at 4:00

pm on the record date would be counted for acceptances and fulfilment of the voting requirement under Rule 28.5. The offeror may not move the record date from the first closing day to a later date in the hope that it would improve voting results and/or acceptance levels. The reason for this is that the change of record date would give rise to various double counting issues in respect of both acceptance and where relevant voting levels which would lead to unacceptable uncertainty and confusion.

■ **Common pool method** – The "common pool method" is where the number of shares taken up by the offeror from each shareholder is determined by the total number of shares tendered for acceptance (the pool).

For example in an offer to buy 40% of the offeree company's shares (again by an offeror holding no shares) where the offeree company has 100 million issued shares, 40% would represent 40 million shares. If all shareholders tender all their shares in acceptance the offeror must take up 40% of each shareholder's tendered shares. However, if for example, the offeror receives a total of 50 million shares tendered for acceptance, 80% (i.e. 40 million ÷ 50 million) of the shares tendered for acceptance by each shareholder must be taken up by the offeror ensuring that all accepting shareholders share the offer on an equal basis. There is no record date nor reference to the share register. Provision for excess applications is not required.

In general the Executive views both types of offer mechanism as acceptable for Takeovers Code purposes because in both cases shareholders are treated equally and are fully informed of the mechanism and terms of the partial offer. Given the drafting of Rule 28.8 the Executive may, depending on the circumstances of the case, grant a waiver from strict compliance with that Rule in the case of common pool partial offers. As with all transactions under the Codes there is an overriding concern that shareholders are treated equally.

In all partial offers the Executive should be consulted at the earliest opportunity.

Odd lots

One consequence of accepting a partial offer is that shareholders may be left holding odd lots of shares which can be difficult to sell or only be sold at a lower price than the market price or involve greater transaction costs per share to sell than board lots of shares. In these circumstances a designated broker may be appointed to match sales and purchases of odd lot holdings. The designated broker may not, however, itself make an offer to buy the odd lots from shareholders. The reason for this is that if odd lot holders were to receive an offer for their shares and this offer was not extended to all other shareholders this would amount to unequal treatment of shareholders in breach of General Principle 1 and Rule 28.3 (as the designated broker is likely to be acting in concert with the offeror) of the Takeovers Code. In cases of doubt the Executive should be consulted.

Executive's consent for partial offers

As a matter of practice the Executive normally grants consent under Rule 28.1 to partial offers which could result in an offeror holding 30% or more of the voting rights attaching to the shares in a company provided that the partial offer is conditional on approval of independent (i.e. not the offeror or its concert parties) shareholders holding over 50% of the voting rights and subject to compliance with other relevant provisions of the Codes. The approval process is signified by means of a separate tick box on the acceptance form which states the number of shares in respect of which the offer is approved.

No extension of final closing date for partial offers

Under Rule 20.1(b), accepting shareholders in a partial offer will be paid as soon as possible but in any event within 7 business days following the close of the partial offer. To avoid the situation where accepting shareholders' receipt of consideration for their shares is delayed as a result of extending the final closing date, Rule 28.4 provides that for partial offers, once acceptances exceed the number of shares stated and the offeror declares the partial offer unconditional, the final closing date must be the 14th day thereafter and cannot be further extended.

Furthermore, it would not be fair to accepting shareholders to allow an extension of the final closing date as any extension would dilute or affect the ultimate number of shares that the accepting shareholders are entitled to sell through the partial offer.

Shareholder approval for partial offers for 30% or more

Rule 28.5 of the Takeovers Code provides that any partial offer which could result in the offeror holding 30% or more of the shares which carry voting rights of a company must normally be conditional on the approval of the offer, by independent shareholders holding over 50% of the shares (i.e. this is calculated by reference to the total issued shares of the company and not limited to shares held by shareholders attending the meeting). The reason for this is to ensure that over 50% of the independent shareholders approve the offeror's proposal to acquire 'control' by means of a partial offer (which can be regarded as an exception of the requirement to make a mandatory offer under Rule 26.1 of the Takeovers Code). A shareholder who wishes to approve the offer must tick the separate box on the acceptance form and indicate the number of shares in respect of which the offer is approved. The approval process is viewed as separate from the acceptance process and therefore it is possible to have a shareholder who accepts a partial offer but does not approve it or who does not accept the offer but approves it.

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