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Hong Kong

MERGERS & ACQUISITIONS

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This country-specific Q&A provides an overview of mergers & acquisitions laws and regulations applicable in Hong Kong.

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HONG KONG MERGERS & ACQUISITIONS



1. What are the key rules/laws relevant to M&A and who are the key regulatory authorities?

The Hong Kong Code on Takeovers and Mergers (“**Takeovers Code**”) governs takeovers and mergers affecting public companies in Hong Kong, and companies and real estate investment trusts with a primary listing of their equity securities in Hong Kong.

Under the supervision of the Executive Director of the Hong Kong Securities and Futures Commission (“**SFC**”), violations of the Takeovers Code may result in disciplinary actions or sanctions being taken the Takeovers and Mergers Panel.

Companies whose securities are listed on the Main Board or the Growth Enterprise Market (“**GEM**”) Board, as applicable, of the Stock Exchange of Hong Kong Limited (“**SEHK**”) are subject to **the Rules Governing the Listing of Securities on the SEHK or the Rules Governing the Listing of Securities on GEM of the SEHK, as applicable (collectively, the “Listing Rules”)**. The disclosure and approval procedures for transactions made by the listed firms are outlined in the Listing Rules.

They are enforced by the SEHK, which may impose sanctions, such as private reprimand, public censure, referral to the SFC and other relevant regulatory bodies, exclusion from the market for a stated period or even suspension or cancellation of a company’s listing.

The Companies Ordinance (Chapter 622 of the Laws of Hong Kong) regulates compulsory acquisitions and schemes of arrangement for companies incorporated in Hong Kong (“**Companies Ordinance**”).

A statutory disclosure mechanism is established by the **Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)** (“**SFO**”). In addition, it controls insider trading and other forms of market misconduct pertaining to listed securities and their derivatives, as well as the disclosure of holdings in the stocks of listed businesses.

In addition, M&A activities in certain regulated industries, including banking, insurance, and telecommunications and broadcasting, are also subject to sector-specific regulations by the relevant regulators.

2. What is the current state of the market?

The overall M&A market in Hong Kong remained subdued in 2023. Market sentiment generally remained cautious amidst the complex economic backdrop, geopolitical tensions, and slowing economic growth in China and the APAC region.

In particular, as slowdown in M&A activities continues, private equity sponsors have increasingly resorted to GP-led secondaries transactions to provide exits to their limited partners.

3. Which market sectors have been particularly active recently?

Active sectors include, amongst others, technology, media and telecom (TMT). Business’ pursuit of digital transformation has driven deal making Hong Kong & APAC. The financial services sector has remained a key sector focus in Hong Kong.

4. What do you believe will be the three most significant factors influencing M&A activity over the next 2 years?

- **Deceleration of inflation and reductions in interest rates.** A clearer picture on interests rates and greater visibility regarding the economic outlook is likely to provide buyers with more comfort on valuation.
- **Pressure to exit.** Sellers, especially those under pressure to exit (including from LPs’ demands), are likely to become more realistic about their expectations for valuation.
- **S.-China tensions** may cause foreign businesses to consider carving out their

operations in China, especially those in the more sensitive sectors.

5. What are the key means of effecting the acquisition of a publicly traded company?

The main means of effecting the acquisition of a public company (target) include the following:

- **Mandatory offer.** A mandatory general offer means a bidder is obliged to extend an offer to all of the shareholders of the target to purchase their shares. The Takeovers Code requires a mandatory offer when:
 - a person (together with its concert parties) acquires 30% or more of the voting rights of the target; or
 - a person (together with its concert parties) that holds between 30% and 50% of the voting rights of the target acquires additional voting rights that increase its holding by more than 2% from the lowest percentage holding held by it in the previous 12-month period (“**Creeping Rule**”).
- **Voluntary offer.** A bidder may make a voluntary offer; provided that the outcome of such an offer does not satisfy any of the mandatory offer tests as discussed above. The satisfaction of either test would change a voluntary offer into a mandatory offer.
- **Scheme of arrangement.** A bidder may also purchase 100% of a target by way of a scheme of arrangement. This is commonly used for privatisation of listed companies in Hong Kong.
- **Merger by absorption.** Only applicable to listed companies incorporated in the PRC.

6. What information relating to a target company will be publicly available and to what extent is a target company obliged to disclose diligence related information to a potential acquirer?

Publicly available information on Hong Kong-listed companies includes the following:

- public announcements and circulars about their corporate actions and significant business developments and transactions; and financial reports published on the SEHK’s website and the companies’ websites in

- accordance with the Listing Rules;
- interests and short positions in the shares and debentures of the listed companies held by directors, as well as the interests and short positions in the shares of the listed companies held by substantial shareholders (5% or more); and
- search results that can be obtained through public searches at the relevant government authorities in Hong Kong, including the following:
 - Companies Registry;
 - Land Registry;
 - Trade Marks Registry;
 - Hong Kong courts; and
 - Official Receiver’s Office.

There is no statutory obligation on a target company to disclose specific due diligence-related information to a potential acquirer.

7. To what level of detail is due diligence customarily undertaken?

In a hostile bid, a bidder will have to rely on publicly available information discussed in **Q6 above**.

In a friendly transaction, a bidder may ask for additional due diligence information that is not publicly available. This generally includes the following:

- business due diligence;
- financial due diligence;
- legal due diligence, including, but not limited to:
 - material contracts (lease agreements, customer contracts, supplier contracts, employment agreements, partnership agreements, guarantees or loan documentation);
 - licences or permits;
 - specifics of litigation; and
 - intellectual property rights.

8. What are the key decision-making organs of a target company and what approval rights do shareholders have?

A target company’s board of directors is its principal decision-making body, and the directors are required to abide by their statutory fiduciary duties (**see Q9 below**). Shareholders will have right to accept a takeover offer or approve a scheme of arrangement.

9. What are the duties of the directors and controlling shareholders of a target company?

Some general principles of the Takeovers Code include the following:

- rights of control should be exercised in good faith and the oppression of minority or non-controlling shareholders is always unacceptable;
- directors of an offeror and the offeree company must always, in advising their shareholders, act only in their capacity as directors and not have regard to their personal or family shareholdings or to their personal relationships with the companies. They should only consider the shareholders' interests taken as a whole when they are giving advice to
- Directors of the offeree company should give careful consideration before they enter into any commitment with an offeror (or anyone else), which would restrict their freedom to advise their shareholders. Such commitments may give rise to conflicts of interest or result in a breach of the directors' fiduciary duties; and
- at no time after a bona fide offer has been communicated to the board of the offeree company, or after the board of the offeree company has reason to believe that a bona fide offer might be imminent, may the board of the offeree company take any action in relation to the affairs of the company, without the approval of shareholders in general meeting, which could effectively result in any bona fide offer being frustrated or in the shareholders being denied an opportunity to decide on its merits.

In addition, per the Takeovers Code, the target board must establish an independent board committee to make a recommendation, and appoint a competent independent financial adviser to advise it on matters, such as whether the offer is reasonable and fair, and acceptance or voting. The independent financial adviser's written advice (including justifications) shall be disclosed to shareholders by means of the target board circular, in conjunction with the recommendations of the independent board committee on the offer.

10. Do employees/other stakeholders have any specific approval, consultation or other

rights?

There are no legal or regulatory requirements for a target's board to inform or consult its employees about the offer, nor are there statutory consultation rights given to special stakeholders.

11. To what degree is conditionality an accepted market feature on acquisitions?

Mandatory Offer

A mandatory offer can only be conditional on the bidder receiving acceptances that result in it and persons acting in concert with it holding more than 50% of the voting rights in the target.

Voluntary Offer

A voluntary offer must, at the very least, be conditional on the bidder receiving acceptances that result in the bidder and persons acting in concert with it holding more than 50% of the voting rights in the target. Where the bidder intends for the target to remain listed following the takeover, it should ensure the target continues to adhere to the public float requirements.

Additional conditions may be attached to a voluntary offer. Typical conditions include the following:

- regulatory approvals or other third-party consents;
- anti-trust approvals;
- target's shares remain listed on the SEHK; and
- no material adverse change in the business, financial or trading position or prospects of the target.

Typically a financing condition is not included, as the bidder's financial advisor is required to provide a written confirmation to the SFC that it is satisfied that there are sufficient resources available to satisfy acceptance of the offer in full.

12. What steps can an acquirer of a target company take to secure deal exclusivity?

Hong Kong law does not impose automatic exclusivity in negotiations. It is unusual for the board of a Hong Kong public company to grant a meaningful period of exclusivity to a potential bidder in advance of signing a definitive agreement. Providing exclusivity to the bidder prevents other bids from being considered during the exclusivity period, which hinders the directors' ability to

carry out their duties to optimize value for the company. However, in a sell process initiated by the company, directors may be more inclined to provide the bidder exclusivity for a limited period of time to finalise the transaction.

Exclusivity is more prevalent and frequently demanded by bidders in private M&A transactions.

13. What other deal protection and costs coverage mechanisms are most frequently used by acquirers?

It is uncommon for an agreement in connection with a bid to be made between the target and the bidder. In case of takeovers of listed companies by way of scheme of arrangements by consortiums formed among private equity investors and existing shareholders of the target, the target and the bidder may enter into an implementation agreement. Under this agreement, the target typically agrees to: (i) use all reasonable efforts to implement the proposal; (ii) refrain from taking any measures that would effectively hinder the bidder's offer; and/or (iii) not solicit an alternative proposal other than the bidder's.

In addition, a bidder may seek irrevocable commitments from shareholders of the target with significant stakes to accept the offer.

Break fees are permitted but not common in Hong Kong public M&A transactions, and the SFC should be consulted in all cases where a break fee is proposed.

14. Which forms of consideration are most commonly used?

Cash remains more commonly used in Hong Kong, although stock consideration or a combination of cash and stock is also seen in certain transactions. More innovative forms seen in other jurisdictions, such as contingent value rights remain unusual in Hong Kong.

15. At what ownership levels by an acquirer is public disclosure required (whether acquiring a target company as a whole or a minority stake)?

A bidder has a duty under the SFO to disclose their interests in listed company shares if/when, among others, (i) their interest amounts to 5% or more of the voting shares; (ii) their interest increases or decreases; or (iii) the nature of its interest changes.

When working out the total number of shares in which a person is interested, include the following:

- all joint interests;
- interests through equity derivatives;
- any interests held by his spouse and children under the age of 18 years;
- any interests held by controlled companies, trusts and nominees; and
- any interests held under a concert party arrangement.

16. At what stage of negotiation is public disclosure required or customary?

A firm intention to make an offer, along with the terms and other necessary details, should only be announced when the bidder has every reason to believe that it can and will continue to be able to implement the offer.

Before an announcement of a firm intention to make an offer is made, announcements may be made in the following situations:

- the target is the subject of rumour or speculation about a possible offer;
- there is undue movement in its share price or volume of share turnover; and
- negotiations or discussions are about to be extended to include more than a very restricted number of people.

Before the target board is approached, the responsibility for making an announcement will normally lie with the bidder or potential bidder. Following an approach to the target board, the primary responsibility for making an announcement will normally rest with the target board.

17. Is there any maximum time period for negotiations or due diligence?

There are no restrictions on the timing and depth of due diligence in acquisitions under Hong Kong law. The due diligence process is mainly driven by the bidder's requests and the target's cooperation. The duration of the process is negotiable between the involved parties. The bidder can perform initial due diligence on a potential target by looking through publicly available data before requesting for further information from the target.

18. Are there any circumstances where a minimum price may be set for the shares in

a target company?

For a **mandatory offer**, the consideration must not be less than the highest price paid by the bidder or persons acting in concert with it for the target shares during the offer period and for six months before it, unless SFC grants permission. In the event the voting rights were obtained through non-monetary consideration, the offer price must be assessed by an independent valuer.

For a **voluntary offer**, the offer price cannot be more than a 50% discount to the target shares' market price (being the lesser of the closing price of the target's shares on the day before the offer announcement or the previous five days' average closing price).

The offer of the target shareholders cannot be made on less favourable terms if the bidder or any person acting in concert with them has acquired the target shares either three months prior to the start of the offer period, or during the period between the announcement of a proposed or possible offer and the announcement of a firm intention to make an offer.

The bidder shall raise the offer price to the highest price (exclusive of stamp duty and dealing costs) paid for the target shares, if, following the announcement of a firm intention to make an offer and during the offer period, the bidder or any person(s) acting in concert with them purchases target shares above the offer price. Target shareholders who accepted the original offer are entitled to receive the revised price.

19. Is it possible for target companies to provide financial assistance?

Subject to limited exceptions, Hong Kong law prohibits companies incorporated in Hong Kong, or any of their subsidiaries, from providing financial assistance to purchase their own shares.

The Companies Ordinance does not provide a complete definition of financial assistance, but it can take a variety of forms such as loans, gifts, guarantees or waivers. Breach of financial assistance rules could result in committing a criminal offence.

If the target cannot rely on the limited exceptions, it could follow one of the three alternative routes to authorize financial assistance (the "whitewash" procedures). These are providing:

- assistance not exceeding 5% of the paid-up share capital and reserves of the target;
- assistance with unanimous shareholder approval; or

- assistance approved by ordinary resolution (in such case, dissenting shareholders may apply to the court to restrain the giving of assistance).

Prior to providing assistance in each case, the directors must resolve, among other things, that (i) the assistance is in the best interests of the target; and (ii) the terms and conditions under which the assistance is to be provided are reasonable and fair to the target. The directors will need to issue a solvency statement. The parties must strictly adhere to the relevant procedures and guidelines for each route.

20. Which governing law is customarily used on acquisitions?

In public M&A, the law of incorporation of the target typically governs the transaction.

In private transactions, Hong Kong, New York and English law are all commonly seen.

21. What public-facing documentation must a buyer produce in connection with the acquisition of a listed company?

The Takeovers Code requires a bidder to post an offer document within 21 days of the date of the announcement of the terms of the offer. The offer document must contain information specified in the Takeovers Code to enable the target's shareholders to reach a properly informed decision. Such information includes the following:

- details of the offer and accompanying conditions;
- the bidder's future plans for the target and its employees;
- whether the bidder intends to avail itself of any powers of compulsory acquisition; and
- share ownership and dealing disclosures.

The target board must respond to the offer in a circular (or response document) to its shareholders within 14 days of the offer document being posted. The target board circular must also contain information specified in the Takeovers Code including the following:

- the recommendations of the target board and advice to shareholders about the acceptance of the offer;
- advice of an independent financial adviser;
- share ownership and dealing disclosures; and
- financial information and details of the

target's material contracts.

In the case of a recommended bid, the offer document will typically be a composite document prepared by both the bidder and the target setting out all the information required in the offer document and the target board circular.

In the case of a hostile bid, the offer document and the target board circular will normally be issued separately.

22. What formalities are required in order to document a transfer of shares, including any local transfer taxes or duties?

Hong Kong share transfer documents include the following:

- bought and sold notes;
- instrument of transfer;
- resolutions of the board of directors of the target; and
- supporting documents required for stamp duty purposes.

23. Are hostile acquisitions a common feature?

Although permitted, hostile bids are not common in Hong Kong because a vast number of public companies in Hong Kong are controlled by shareholders with significant or controlling stakes (sometimes including a major stake held by a founding family), which may reduce the likelihood of successful hostile bids.

24. What protections do directors of a target company have against a hostile approach?

A general principle of the Takeovers Code states that without shareholders' approval, a target's board cannot take any action that could effectively frustrate any bona fide offer or deny shareholders an opportunity to decide on an offer's merit.

Other than expressing its views for opposing a hostile bid in the target board circular, a target's board has limited options in opposing a hostile bid. Typically a hostile bid fails not because of the target's defensive measures but because of public shareholders' dissatisfaction with the offer price.

25. Are there circumstances where a buyer may have to make a mandatory or compulsory offer for a target company?

As mentioned in **Q5** above, the Takeovers Code requires a mandatory offer to be made to all shareholders of the target when:

- a person acquires voting rights of the target thereby increasing his holding (alone or together with the holding of persons acting in concert with them) of voting rights to 30% or more of the voting rights of the target; and
- a person (alone or together with persons acting in concert with them) hold(s) between 30% and 50% of the voting rights of the target and that person (or any one or more of the persons acting in concert with it) acquire(s) additional voting rights of more than 2% from their lowest percentage holding in the previous 12-month period. (This is known as the "creeper rule.")

The above rules do not apply if a waiver is granted by the SFC. For example, the SFC will normally grant such waiver when a company issues new securities as consideration for an acquisition, or a cash subscription, or taking a strip dividend, if the waiver and the transaction are separately approved by 75% and 50% of the independent vote at a shareholders' meeting.

26. If an acquirer does not obtain full control of a target company, what rights do minority shareholders enjoy?

Following a takeover offer, minority shareholders who stay invested in the target have a limited set of rights. The minority shareholder will continue to have the rights and protections granted by the Listing Rules; provided that the target hasn't been delisted.

In addition, under the Companies Ordinance (for a Hong Kong-incorporated company):

- a minority shareholder that has not accepted a takeover offer before the end of the offer period can require the offeror to acquire its shares, if the offeror has (by virtue of acceptances of the takeover offer) acquired, or contracted unconditionally to acquire, some but not all of the shares to which the offer relates, and at any time before the end of the offer period, the shares controlled by the offeror represent at least 90% of the shares in the target; and

- a minority shareholder can apply to the court for relief where it considers that the company's affairs are being or have been conducted in a manner that is unfairly prejudicial to its interests.

27. Is a mechanism available to compulsorily acquire minority stakes?

The availability of compulsory acquisition rights is contingent upon the laws of the jurisdiction in which the target is incorporated. Among the common jurisdictions

of incorporation for Hong Kong-listed companies, the laws of the Cayman Islands, Bermuda and Hong Kong provide for compulsory acquisition rights.

Under the Takeovers Code, compulsory acquisition rights may only be exercised if, in addition to satisfying any requirements imposed by law, acceptances of the offer and purchases made by the bidder and persons acting in concert with them during the period of four months after posting the initial offer document total 90% of the disinterested shares. Once the compulsory acquisition is completed, an application will be submitted to withdraw the listing of the shares of the target from the SEHK.

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