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# SFC Issues Takeovers Bulletin On (1) Reminder To Fund Managers Of Dealing Disclosure Obligations Under Rule 22 Of The Takeovers Code (2) List Of Secondary Listed Companies Not Subject To The Codes (3) Public Criticism Of Fidelity Worldwide Investment For Dealing Disclosure Breaches

## Introduction

The latest issue of the Takeovers Bulletin (Issue No.19) published in December 2011 reminds fund managers of the dealing disclosure obligations under Rule 22 of the Code on Takeovers and Mergers (**Takeovers Code**), gives notice of the list of overseas companies with a secondary listing in Hong Kong that are not subject to the Takeovers Code and Share Repurchase Code and highlights a recent panel statement on dealing disclosure breaches.

The [Takeovers Bulletin](http://www.sfc.hk/web/doc/EN/cfd/mergers/takeovers_bulletin/11/dec_11.pdf) ([see archive](dec_11.pdf)) is available under ‘Speeches, Publications & Consultations’-‘Publications’ of the SFC website.

The SFC invites interested parties to submit their feedback and comments to [takeoversbulletin@sfc.hk](mailto:takeoversbulletin@sfc.hk). Intermediaries licensed by the SFC receive the Takeovers Bulletin via their FinNet email accounts. The Takeovers Bulletin can also be received by email after registration for the [Update Email Alert Service](https://www.sfc.hk/sfcUpdateAlert/jsp/EN/update_alert.jsp).

## Articles

## (1) Reminder To Fund Managers Of Dealing Disclosure Obligations Under Rule 22 Of The Takeovers Code

### Introduction

The Securities and Futures Commission (**SFC**) notes that there have been a number of recent breaches of the dealing disclosure obligations under Rule 22 of the Takeovers Code by local and overseas fund managers. In view of this and to raise awareness of the Takeovers Code’s requirements, the SFC has published “[Guidelines to Fund Managers on Dealing Disclosure Obligations under Rule 22 of The Code on Takeovers and Mergers](http://en-rules.sfc.hk/net_file_store/new_rulebooks/h/k/HKSFC3527_3638_VER20.pdf)” (the **Guidelines**) ([see archive](HKSFC3527_3638_VER20.pdf)) which were sent to Hong Kong registered and licensed fund managers in November 2011. The Guidelines summarise the requirements under Rule 22 and suggest practical measures a fund manager, who is an “associate” under the Takeovers Code, might take to help ensure compliance with Rule 22, in terms of identifying relevant companies in an offer period, staff training and maintaining compliance systems. The SFC underlines the importance of timely and accurate disclosure of information by associates and any other parties who may exercise material influence over an offer. It also advises fund managers to remind appropriate persons in their overseas offices, who are likely to deal in the relevant securities of Hong Kong-listed companies, of the dealing disclosure obligations under Rule 22.

### Dealing disclosure obligations

Under Rule 22 of the Takeovers Code, parties to an offer (and their associates) must disclose dealings in relevant securities of the offeree company and the offeror (in the case of a securities exchange offer), conducted for themselves or on behalf of discretionary clients during the offer period. According to Note 4 to Rule 22, relevant securities include:

* securities of the offeree company which are being offered for or which carry voting rights;
* equity share capital of the offeree company and an offeror;
* securities of an offeror which carry the same or substantially the same rights as any to be issued as consideration for the offer;
* securities carrying conversion or subscription rights into any of the foregoing; and
* options and derivatives in respect of any of the foregoing.

An “associate” is defined to include a person who owns or controls at least 5% of any class of relevant securities. A fund manager who manages investment accounts on a discretionary basis is treated as controlling relevant securities so managed (and not the person on whose behalf the securities are managed). Further, where more than one discretionary investment management operation is conducted in the same group, relevant securities controlled by all such operations are treated for the purpose of Rule 22 as those of a single person and must be aggregated (Rule 22.3). A fund manager who is an associate must therefore ensure compliance with the Takeovers Code. Below is a summary of the SFC’s Guidelines.

### Identifying Relevant Companies in an Offer Period

The SFC suggests several sources fund managers may use to identify relevant companies in an offer period. The Offer Period Tables under “Prospectuses, Takeovers & Mergers – Offer Period Tables” on the SFC website provide details of current offer periods under the Takeovers Code. Announcements of the commencement of offer periods may be available on the website of the Hong Kong Exchanges and Clearing Limited (**HKEx**). Those announcements may also be found in the News Alert section of the HKEx website. Lastly, fund managers may find information from other sources such as newspaper and financial news services.

### On-going Training of Staff

Staff should be trained in applying relevant provisions of the Takeovers Code. The Guidelines emphasise the importance of understanding the meaning of “associate” and its significance and the requirements of Rule 22 and Schedules I and II to the Takeovers Code. Training should be regular and on-going. [Practice Note 9](http://www.sfc.hk/sfc/doc/EN/cfd/mergers/practice_note/Practice%20Note%2009_EN_020408%20(revised%20on%2030%209%2010).pdf) ([see archive](PN9.pdf)) explains the exempt system for connected fund managers and principal traders.

Lastly, compliance personnel should keep themselves updated on recent changes to the Takeovers Code. The SFC suggests that it may be helpful to subscribe to the Update Alert service on the SFC website to receive takeovers-related notifications such as Takeovers Bulletins and market consultations on amendments to the Takeovers Code.

### Proper Compliance Systems

The Guidelines suggest that fund managers maintain adequate and proper compliance systems to discharge fully their Takeovers Code obligations.

## (2) List Of Secondary Listed Companies Not Subject To The Codes (Posted On The SFC Website)

The Takeovers Bulletin gives notice that a list (updated from time to time) of the names of overseas companies with secondary listings in Hong Kong, to which the Codes on Takeovers and Mergers and Share Repurchases (**Codes**) do not apply, is available on the Takeovers & Mergers section of the [SFC website](http://www.sfc.hk/web/EN/regulatory-functions/listings-and-takeovers/takeovers-and-mergers/secondary-listed-companies-not-subject-to-the-codes.html) ([see archive](SFC_list.pdf)) and the [HKEx website](http://www.hkex.com.hk/eng/rulesreg/listrules/listsptop/listoc/sec_li.htm) ([see archive](HKEx_list.pdf)). While the Codes apply to all companies with a primary listing in Hong Kong, where the listing is a secondary listing, the Codes apply only where the company is a “public company in Hong Kong” within the meaning of the Codes. The SFC has given a number of confirmations to overseas companies that they will not be considered public companies to which the Codes apply after their secondary listing in Hong Kong.

As at 1 December 2011, the following companies with a secondary listing in Hong Kong are not subject to the Codes:

**Secondary Listed Issuers**

**Stock Code**

**Primary Markets**

CapitaMalls Asia Limited

6813

Singapore Exchange

Coach, Inc.

6388

New York Stock Exchange

Glencore International plc

805

London Stock Exchange

Kazakhmys PLC

847

London Stock Exchange and Kazakhstan Stock Exchange

Manulife Financial Corporation

945

Toronto Stock Exchange

Midas Holdings Ltd

1021

Singapore Exchange

SBI Holdings, Inc

6488

Tokyo Stock Exchange and Osaka Securities Exchange

SouthGobi Resources Ltd

1878

Tokyo Stock Exchange

Vale S.A.

6210/6230

BM&FBOVESPA and New York Stock Exchange

Hong Kong shareholders who invest in secondary-listed companies to which the Codes do not apply, will not have the benefit of the protection provided by the Codes.

### Public company in Hong Kong

In order to determine whether a company is a public company in Hong Kong, Section 4.2 of the Introduction to the Codes states that the Executive will consider all the circumstances and apply an economic or commercial test that will take into account primarily the number of Hong Kong shareholders and the extent of share trading in Hong Kong, and any other factors including as follows:

1. location of its head office and place of central management;
2. location of its business and assets, including such factors as registration under companies legislation and tax status; and
3. the existence or absence of protection available to Hong Kong shareholders given by any statute or code regulating takeovers, mergers and share repurchases outside Hong Kong.

The application of the Codes to companies with a secondary listing in Hong Kong was discussed in the article “The Codes do not apply to all listed companies in Hong Kong” in the [September 2010 issue](http://www.sfc.hk/sfc/doc/EN/cfd/mergers/takeovers_bulletin/10/sep_10.pdf) ([see archive](sep_10.pdf)) of the Takeovers Bulletin (Issue no. 14). As a starting point, the Executive will consider the number of public shareholders and the extent of share trading in Hong Kong. These factors are however considered in the context of the size of the relevant company and the relative proportion of its shareholders and share trading activity in Hong Kong. Where the proportion is very small, the Executive does not believe that it should assert jurisdiction. If it is not very small, the Executive will consider the other factors at (a) to (c) above. As regards factors (a) and (b) (generally referred to as the “centre of gravity” of the company), the general principle is that the closer the proximity of the management and the business/assets to Hong Kong, the more likely that protection under the Codes should be afforded.

A company with a ‘secondary listing’ in Hong Kong, by definition, will also have a primary listing in an overseas jurisdiction and the Executive will take into account whether alternative protection is available to Hong Kong investors under factor (c). The Executive adopts a practical approach to see if the protection available to Hong Kong investors under the overseas jurisdiction regulating takeovers, mergers and share repurchases is broadly comparable to the Codes. The Codes have not set down a qualitative test or a test of equivalence as the application of such tests to takeover regimes of different jurisdictions would be problematic and cumbersome in practice.

In addition to referring to the list on the SFC website, investors can read the prospectus and listing documents of a secondary-listed company on its corporate website or the HKEx news website to check whether it is subject to the Codes.

Further information is available in the article “[Non-application of the Takeovers Code](http://www.hkiec.hk/web/en/investment/understanding-products/stock/corporate-action/takeovers-code-non-application.html)” ([see archive](nonapp.pdf)) on the SFC’s investor education website.

## (3) Fidelity Worldwide Investment Publicly Criticised For Dealing Disclosure Breaches

### Background

On 7 November 2011, pursuant to section 12.3 of the Introduction to the Takeovers Code, the Executive publicly criticised FIL Investment Management (Hong Kong) Ltd (trading under the brand name Fidelity Worldwide Investment in Hong Kong) for dealing disclosure breaches under Rule 22 of the Takeovers Code. A copy of the [Executive’s statement](http://www.sfc.hk/sfc/doc/EN/cfd/mergers/panel/04%20-%20Notice%20of%20criticism%20-%20111101%20(Eng).pdf) ([see archive](Executive_statement.pdf)) is available on the SFC website.

The breaches were the result of Fidelity Worldwide Investment’s non-disclosure of dealings in the shares of Little Sheep Group Limited (**Little Sheep**). The dealings (**Dealings**) involved the execution of 29 trades in shares of Little Sheep between 23 May 2011 and 1 June 2011 that increased the shareholding of Fidelity Worldwide Investment from 8.20% to 8.21%. These dealings occurred after the commencement of an offer period for Little Sheep on 26 April 2011 when it announced that it had received an approach from a substantial shareholder, Yum! Brands, Inc. (**Yum**) regarding a possible offer to acquire the outstanding capital of Little Sheep (the **Rule 3.7 Announcement**) and a subsequent announcement by Little Sheep and Yum on 13 May 2011 of a proposal for the privatisation of Little Sheep by way of a scheme of arrangement (the **Rule 3.5 Announcement**). Both the Rule 3.7 and Rule 3.5 Announcements contained a warning to associates of Little Sheep to disclose their dealings in Little Sheep in accordance with Rule 22 of the Takeovers Code.

### Criticisms

Fidelity Worldwide Investment breached Rule 22 of the Takeovers Code based on the following provisions:

#### Disclosure obligation under Rule 22.3

Under Rule 22.3 of the Takeovers Code, if a person manages investment accounts on a discretionary basis, the relevant securities managed will be treated, for the purpose of Rule 22, as controlled by that person and not by the person on whose behalf the relevant securities are managed.

Thus although Fidelity Worldwide Investment’s dealings in shares of Little Sheep were not proprietary positions held by it and were conducted on behalf of funds managed by the group, Fidelity Worldwide Investments (and not its clients), was treated as interested in the Little Sheep shares. Hence, non-disclosure of the relevant Dealings by Fidelity Worldwide Investment to the Executive breached the Rule 22 disclosure obligations.

#### Disclosure obligation under Rule 22.1(b)

For the purpose of Rule 22.1(b) of the Takeovers Code, dealings in relevant securities by an offeror or the offeree company, and by any associates, for the account of discretionary investment clients during an offer period must be publicly disclosed in accordance with Notes 5, 6 and 7 to Rule 22 of the Takeovers Code. As defined by the Takeovers Code, an “associate” includes a person who owns or controls 5% or more of any class of relevant securities issued by an offeror or the offeree company, including a person who as a result of any transaction owns or controls 5% or more.

Immediately prior to the commencement of the offer period for Little Sheep on 26 April, Fidelity Worldwide Investment held 8.20% of the issued share capital of Little Sheep. Since Fidelity Worldwide Investment held over 5% of the issued share capital of Little Sheep at all relevant times, it was an associate of Little Sheep and was required under Rule 22 of the Takeovers Code to disclose publicly its dealings in Little Sheep during the offer period. Hence, non-disclosure of the relevant Dealings to the Executive constituted a breach of the Rule 22 disclosure obligations.

### Remedial Actions taken by Fidelity Worldwide Investment

Fidelity Worldwide Investment self-reported to the Executive on 10 June 2011 that it had not made the required disclosures in respect of the Dealings in accordance with Rule 22 of the Takeovers Code.

It then implemented a number of enhanced measures to ensure future compliance with its Rule 22 disclosure obligations including:

1. the provision of training to staff members of the Asia regulatory reporting team to reinforce the daily checking and reporting process;
2. the addition of the following webpages/searches to its daily monitoring procedures:
   1. “Offer Period Tables” webpage on the SFC’s website;
   2. the announcements page on the Stock Exchange’s website; and
   3. query function of Bloomberg to assist in identifying takeover offers;
3. the hiring of an additional staff member to assist in the daily monitoring process;
4. subscription to relevant alerts from the SFC, the Stock Exchange and the Takeovers Bulletin to assist in monitoring takeovers in Hong Kong; and
5. enhancement of the compliance assurance process which was independently reviewed by external counsel.

Fidelity Worldwide Investment also duly complied with the disclosure obligations under Rule 22 of the Takeovers Code in respect of dealings in Little Sheep shares.

### Implications of Fidelity Worldwide Investment’s failure to comply with Rule 22 of the Takeovers Code

The Executive noted in its statement that the disclosure obligations under Rule 22 of the Takeovers Code are intentionally more onerous than those under Part XV of the Securities and Future Ordinance in that:

1. Rule 22 requires filing to be made by 10:00 am on the business day following the dealing;
2. There are no de minimis thresholds; and
3. Rule 22 requires the disclosure of prices paid or received for each underlying trade whilst the Securities and Future Ordinance only requires the disclosure of the highest and the average price paid or received.

The Executive also considers that the high degree of transparency required under the Takeovers Code is essential to the efficient functioning of the market in an offeree company’s shares during the critical period of an offer. This is in line with General Principle 6 of the Takeovers Code which provides that:

"All persons concerned with offers should make full and prompt disclosure of all relevant information and take every precaution to avoid the creation or continuance of a false market. Parties involved in offers must take care that statements are not made which may mislead shareholders or the market."

The Executive found that Fidelity Worldwide Investment’s failure, as an associate, to make timely disclosure of details of its dealings in the shares of Little Sheep during the offer period constituted a material breach of General Principle 6 as well as Rule 22 of the Takeovers Code.

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