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CLIENT ALERT

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PRIVATISATION: RECENT DEVELOPMENTS AND OPPORTUNITIES

The last few years have seen a flurry of privatisations of Hong Kong listed companies, with a significant portion of them being conducted by way of scheme of arrangements. In this briefing, we highlight two recent legal developments relating to privatisation schemes of Hong Kong-listed companies. The first is the **upcoming abolishment of the headcount test for members' scheme of arrangements of Cayman-incorporated companies** – once in force, this will lower the hurdle and remove a layer of uncertainty for controlling shareholders wishing to privatise listed Cayman-incorporated companies. The second development flows from **a Hong Kong High Court judgment which will affect how parties should deal with concert parties' votes on a privatisation scheme**.

Headcount test for privatisation of Cayman-incorporated companies

For a target incorporated in the Cayman Islands, the relevant companies law requires a majority in number of shareholders (i.e. the headcount test) representing at least 75% in value of the members (or class of members) present and voting to approve the scheme.

Historically, there have been instances of privatisations being thwarted due to not meeting the headcount test threshold. It is also sometimes seen as a hurdle that prevents offers from being launched in the first place. Examples of failed privatisations linked to the headcount test include **New World China Land Limited** and **Glorious Property Holdings Limited**. In a landscape where the bulk of listed shares are held by a nominee entity (i.e. HKSCC Nominees Ltd in Hong Kong), the test has also resulted in a degree of uncertainty over how "heads" are counted.

A bill has been gazetted in the Cayman Islands to remove the headcount test for members' scheme of arrangements[1]. We understand this is likely to become effective by **the end of March 2022**.

Under Rule 31.1 of the Hong Kong Takeovers Code, offerors who have failed a privatisation will generally not be able to make another offer for the target for at least 12 months from the withdrawal or lapse of the offer. Offerors should bear this in mind when reinitiating their privatisation offers. Nonetheless, once in force, we expect this change to ignite activity in privatisations of Hong Kong-listed Cayman-incorporated companies, especially if share prices of Hong Kong stocks remain subdued in the coming months.

Hong Kong High Court judgment on voting by offeror concert parties

Rule 2.10 of the Hong Kong Takeovers Code provides that a privatisation scheme may only be implemented if, in addition to satisfying any company law requirements, broadly: (a) it receives 75% approval from disinterested shareholders present and voting at a shareholder meeting in person or by proxy; and (b) the number of votes cast against the scheme is not more than 10% of the votes attaching to all disinterested shares[2].

[1] The new clause will state: "If seventy-five per cent in value of the members or class of members, as the case may be, present and voting either in person or by proxy at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the Court, be binding on all the members or class of members, as the case may be, and also on the company or, where a company is in the course of being wound up, on the liquidator and contributories of the company".

[2] "Disinterested shares" means shares other than those owned by the offeror or its concert parties.

In the recent case of *Re Chong Hing Bank*[3], the High Court of Hong Kong considered the effect of Rule 2.10, in particular whether it means that:

(a) offeror concert parties are prohibited from attending and voting at the court-convened shareholder meeting to consider the scheme (the "**Court Meeting**") (the "**Prohibition View**"); or

(b) offeror concert parties are not prohibited from attending and voting at the Court Meeting but their votes must be disregarded for the purpose of determining whether the voting requirements in Rule 2.10 have been satisfied (the "**Non-Prohibition View**").

The Court ruled that the Prohibition View is the correct view[4].

In light of the Court's decision, to minimise the risk of running into difficulty in future scheme privatisations of Hong Kong incorporated companies, it would be advisable for offerors to:

(i) ensure that offeror concert parties who will be subject to the scheme irrevocably undertake to the offeror and the target company (and the court, if requested to do so) that they will not attend or vote at the Court Meeting, and that they agree to be bound by the scheme; and

(ii) carefully consider any statement in the scheme document and notice of the Court Meeting regarding the attendance, voting and irrevocable undertaking by such concert parties to ensure that they are accurate in light of the Court's decision.

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[3] *Re Chong Hing Bank Ltd* [2021] HKCFI 3091

[4] This is contrary to the High Court's view in *Re Cosmos Machinery Enterprises Limited* [2021] HKCFI 2088 that the Non-Prohibition View is the correct position. However, such view was regarded by the High Court in *Re Chong Hing Bank Ltd* as *obiter* and therefore non-binding.

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