

A periodic newsletter to help participants in Hong Kong's financial markets better understand the Codes on Takeovers and Mergers and Share Repurchases

Takeovers Panel rules chain principle offer triggered for Greenheart

On 17 January 2013, the Takeovers and Mergers Panel (Takeovers Panel) ruled that an obligation under the Takeovers Code to make a chain principle offer for Greenheart Group Limited (Greenheart) would be triggered if Sino-Forest Corporation (Sino-Forest) proceeded with the transfer of substantially all the assets of Sino-Forest, which included an indirect shareholding of 63.6% in Greenheart, to a new company wholly-owned by Sino-Forest's creditors. The Takeovers Panel also decided that a waiver of any such mandatory offer obligation would not be available.

Background

The matter related to a proposed restructuring of Sino Forest which was in severe financial difficulty.

Sino-Forest is a company whose shares were previously listed on the Toronto Stock Exchange. Following a report in June 2011 by Muddy Waters L.L.C., Sino-Forest experienced severe financial difficulties with the result that it defaulted on certain of its obligations under certain notes it had issued.

In March 2012 Sino-Forest filed a motion under the Canadian Companies' Creditors Arrangement Act (the CCAA) seeking the protection of the Ontario Court to rearrange its affairs.

Following the unsuccessful sale of its assets (including its 63.6% interest in Greenheart) at an appropriate price, it was proposed that Sino-Forest would transfer its assets to a new company or a wholly-owned subsidiary of it (collectively New Holdco) which would be owned by Sino-Forest's creditors as a compromise for its debts. These arrangements were supported by the ad hoc committee, comprising holders of a significant amount of notes issued by Sino-Forest (the Ad Hoc Committee) and subsequently by noteholders holding an aggregate of some 72% of the outstanding notes (the Restructuring Plan). Sino-Forest proceeded to file the Restructuring Plan with the Ontario Court and by 10 December 2012, it had been approved by both the Ontario Court and noteholders.

Highlights

- Takeovers Panel rules chain principle offer triggered for Greenheart
- Appointments and reappointments to the Takeovers Panel and related committees
- Quarterly update on the activities of the Takeovers Team

One of the assets to be transferred from Sino-Forest to New Holdco was the entire issued share capital of Sino-Capital Global Inc. (SCGI) which held shares representing some 63.6% of the voting rights of Greenheart, and some other businesses, being primarily a business owned by another subsidiary, Homix Limited, engaged in wood manufacturing.

The Ad Hoc Committee applied to the Executive for a ruling on whether a chain principle offer for Greenheart would be triggered under Note 8 to Rule 26.1 of the Takeovers Code as a result of the Restructuring Plan. At the request of the advisers of the Ad Hoc Committee, the application was referred to the Takeovers Panel.

Whether a chain principle offer will be triggered

The advisers to the Ad Hoc Committee argued that the proposed transfer of SCGI with its controlling interest in Greenheart is one element in the Restructuring Plan and should not be seen separately from it. It was suggested that SCGI was also not a core element of the Restructuring Plan, given its value relative to the total assets of the Sino-Forest Group to be transferred under the Restructuring Plan. However, the Takeovers Panel agreed with the Takeovers Executive's interpretation of Note 8 to Rule 26.1 in that it simply looks at a transaction, whether it is an element of a larger one or not, in which change in the statutory control of one company results in the acquisition or consolidation of control, as defined in the Takeovers Code, of a second company.

While it was undoubtedly part of a larger series of inter-conditional transactions, New Holdco proposed to acquire statutory control of SCGI and this company held a controlling interest in Greenheart. In any circumstances when the control of a company which is subject to the provisions of the Takeovers Code is to be acquired, consideration must be given to the possibility of a mandatory offer obligation arising. This is fundamental to the Takeovers Code, of which General Principles 1 and 2 and Rule 26.1 are at its heart.

The Takeovers Panel considered that Note 8 to Rule 26.1 does not differentiate one kind of transaction from another on the basis of the circumstances that caused it to be entered into. It applies equally to a debt restructuring as to any other commercial arrangement which comes within its scope.

The Takeovers Panel also agreed that the Restructuring Plan was not analogous to the appointment of a liquidator or receiver and that accordingly the dispensation under Note 2 of the dispensations from Rule 26 would not be available to New Holdco. In normal circumstances the Note only applies to the appointment of a liquidator or receiver as these terms are generally understood in Hong Kong.

Whether to exercise its discretion to waive the mandatory offer obligation

The Takeovers Panel considered whether to exercise its discretion under Section 2.1 of the Introduction to the Takeovers Code to waive the requirement for New Holdco to make a mandatory offer for the shares in Greenheart not owned by it or parties acting in concert with it immediately after implementation of the Restructuring Plan.

While the Takeovers Panel had considerable sympathy, it considered that the meaning of the wording of Note 8 to Rule 26.1 and its implications for parties were clear; they were operating in the manner for which they were designed and how they had been interpreted previously. In view of this it did not appear that there were proper grounds to modify the application of Note 8 based on the provisions of Section 2.1 of the Introduction to the Takeovers Code. The Note is intended to place parties on notice that the transfer of an indirect holding of a controlling interest always comes within the provisions of the Takeovers Code which is why the Takeovers Executive should always be consulted.

While Rule 26.1 itself allows for the waiver of the mandatory offer obligation, the Takeovers Panel considered that it would be setting a dangerous precedent were it to have waived a mandatory offer obligation for reasons other than those specifically set out in Rule 26 and its Notes. For these reasons, the Takeovers Panel decided that it was not appropriate for it to exercise its discretion to waive the mandatory offer obligation on the part of New Holdco in relation to Greenheart and, accordingly, were the Restructuring Plan to be implemented in accordance with its then terms, a mandatory offer obligation for Greenheart would be triggered.

Following the Takeovers Panel decision, Emerald Plantation Group Limited, a company newly incorporated by the Ad Hoc Committee, announced a mandatory general offer for the shares of Greenheart on 31 January 2013.

The full written decision of the Takeovers Panel can be found in the “Regulatory functions – Listings & takeovers – Takeovers & Mergers – Decisions & statements – Takeovers and Mergers Panel and Takeovers Appeal Committee decisions and statements” section of the SFC website.

Appointments and reappointments to the Takeovers Panel and related committees

We welcome the following new appointments and reappointments to the Takeovers Panel, the Takeovers Appeal Committee (Appeal Committee) and the Nominations Committee with effect from 1 April 2013:

Takeovers Panel and Appeal Committee

New appointments - Mr Freeman Chan (Deputy Chairman of the Takeovers Panel), Mr David Webb (Deputy Chairman of the Takeovers Panel) and Ms Melissa Brown

Reappointments - Mr Stephen Clark (Chairman of the Takeovers Panel), Mr Roger Denny, Mr Ernest Ip, Mr Edward Lam, Mr Bonn Liu, Mr Joseph Lo, Ms Teresa Ma, Mr Christopher Swift, Mr Andrew Tortoishell and Mrs Judy Vas

Nominations Committee

Reappointment – Mr Anderson Chow, SC

We wish to thank Mr Daniel Rodgers and Ms May Tan who have stepped down from the Takeovers Panel and the Appeal Committee for their valuable contributions over the years.

Members are appointed for a term of two years and unless otherwise stated, their current terms are until 31 March 2014. The membership lists for the Takeovers Panel, the Appeal Committee, the Disciplinary Chair Committee and the Nominations Committee are set out below.

Takeovers Panel

The Takeovers Panel hears disciplinary matters in the first instance, reviews rulings by the Executive at the request of any party dissatisfied with such a ruling and considers novel, important or difficult cases referred to it by the Executive. It also reviews, upon request by the SFC, the provisions of the Codes and the Rules of Procedure for hearings under the Codes and recommends appropriate amendments to the Codes and Rules to the SFC.

Chairman

Mr Clark Stephen Edward*

Deputy Chairmen

Mr Chan Yuk Sing, Freeman[#]

Ms Ko, Teresa Yuk Yin, JP

Mr Liu Chee Ming

Mr Maguire John Martin

Mr Webb David Michael[#]

Members

Ms Brown Melissa[#]

Ms Charlton Julia Frances

Mr Cheung Yuk Tong

Mr Denny Roger Michael*

Ms Desai Kalpana

Mr Ip Koon Wing, Ernest*

Mr Kwok Tun Ho, Chester

Mr Lam Sung Lai, Edward*

Mrs Lee Pui Ling, Angelina, SBS, JP

Mr Liu Che Ning

Mr Liu Swee Long, Michael

Mr Liu Yun Bonn*

Mr Lo Kin Ching, Joseph*

Mr Lung Hak Kau

Ms Ma, Ka Ming Teresa*

Mr Nesbitt Gavin Paul

Mr Norman David Michael

Mr Norris Nicholas Andrew

Mr Sabine Martin Nevil

Mr Schuille Mark Andrew

Mr Swift, Christopher Lee*

Mr Tortoishell Andrew*

Mrs Vas Chau Lai Kun Judy*

Mr Winter Richard David

Ms Yu Ka Po, Benita

* reappointed on 1 April 2013 for a term of two years until 31 March 2015

[#] appointed on 1 April 2013 for a term of two years until 31 March 2015

Appeal Committee

The Appeal Committee reviews disciplinary rulings of the Takeovers Panel for the sole purpose of determining whether any sanction imposed by the Takeovers Panel is unfair or excessive. It comprises a Chairman who is a member of the Disciplinary Chair Committee and other members of the Takeovers Panel who are selected on a case-by-case basis.

Disciplinary Chair Committee

Members are nominated by the Nominations Committee on the basis that they are duly experienced senior counsel. Their role is to act as Chairman of the Takeovers Panel in disciplinary proceedings under the Codes or of the Appeal Committee on a case-by-case basis.

Members

Mr Chan King Sang, Edward, SC

Mr Ho Ambrose, SC

Ms Li Gladys Veronica, SC

Mr Ng Kar Fai, Peter, SC

Mr Wong Yuk Lun, Horace, SC

Nominations Committee

The Nominations Committee nominates members of the Takeovers Panel, the Appeal Committee and the Disciplinary Chair Committee.

Ex officio Members

Mr Alder Ashley Ian (Chairman)

Mr Clark Stephen Edward

Mr Ho Yin Tung, Brian

Members

Mr Chow Ka Ming, Anderson, SC*

Mr Tong Carlson, JP[#]

Alternate members to Clark Stephen Edward

Mr Chan Yuk Sing, Freeman

Ms Ko, Teresa Yuk Yin, JP

Mr Liu Chee Ming

Mr Maguire John Martin

Mr Webb David Michael

* reappointed on 1 April 2013 for a term of two years until 31 March 2015

appointed on 1 November 2012 for a term of two years until 31 October 2014

A full list of members of the Takeovers Panel, the Appeal Committee, the Disciplinary Chair Committee and the Nominations Committee can be found in the "Regulatory functions – Listings & takeovers – Takeovers & Mergers – Takeovers Panel & related committees" section of the SFC website.

Quarterly update on the activities of the Takeovers Team

In the three months ended 31 December 2012, the Executive dealt with nine takeovers-related cases (including privatisations, voluntary and mandatory general offers and off-market and general-offer repurchases) and seven whitewashes. The Executive also received 42 ruling applications.

The Takeovers Bulletin is available under 'Published resources' – 'Industry-related publications' of the SFC website at <http://www.sfc.hk>.

Feedback and comments are welcome and can be sent to takeoversbulletin@sfc.hk.

If you want to receive the Takeovers Bulletin by email, simply register for the subscription service at <http://www.sfc.hk> and select Takeovers and mergers.

Securities and Futures Commission
35/F, Cheung Kong Center, 2 Queen's Road Central, Hong Kong

Phone : (852) 2231 1222

Fax : (852) 2521 7836

SFC website : www.sfc.hk

Media : (852) 2231 1860

E-mail : enquiry@sfc.hk