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Mergers and Acquisitions Guidance Note

The governance professional will know that the stage of 'signing' signifies a celebratory moment in mergers and acquisitions (M&A) transactions, and for that matter any agreement. This guidance note revisits the scenario of a split signing and closing situation, which is fairly common in larger M&A transactions, and walks the governance professional through the key aspects in relation to the signing stage to facilitate a smooth signing process.

In a nutshell, the signing stage signifies an agreement of terms and conditions among the parties. Closing will occur upon the satisfaction of agreed conditions. In some cases, there may be a lengthy gap between the two stages, in particular when multiple regulatory approvals are required for the consummation of the transaction. These could include anti-trust clearance and a change of controllers in regulated industries.

Internal approval

A pre-requisite for all corporate entities entering into the signing of an M&A transaction is the seeking of internal approvals. Typically, these approvals include those from the board of directors and in some cases investment committees (if one has been established). For joint ventures and deals involving listed companies, shareholders approvals may well be required, as well as specific shareholders' consents or waivers in relation to any pre-emption rights.

In this connection, the corporate entities' constitutional documents and agreement among shareholders are the primary sources for identifying the necessary internal approvals. For listed companies, references should also be made to the compliance requirements of the Listing Rules.

Flexibility for amendments

As the governance professional would know, more often than not, internal approvals are obtained when the terms and conditions of the transaction are still being negotiated. The parties may also agree to amend the terms to deal with unforeseen circumstances after signing but before closing. In addition, regulatory authorities may impose conditions when providing their consents.

In view of these potential obstacles to a successful signing and/or closing of the transaction, flexibilities permitting changes to the agreed terms are usually built into the internal approvals. For board and shareholder approvals, a common way of doing this is by granting power to authorised persons to approve amendments or modifications to the terms and conditions of the transaction as they consider 'necessary or desirable'.

An alternative way to allow flexibility, but within a pre-determined scope, is to give the authorisation subject to satisfying certain conditions. By way of example, to pre-empt situations where a regulator grants its approval subject to conditions, the internal approvals may specify that they are given subject to meeting conditions imposed by regulators.

Where a party is a listed company

If a party to the transaction is a company listed on The Stock Exchange of Hong Kong (SEHK), or for that matter, any overseas exchange, the completion of an M&A transaction by that company may require prior shareholders' approval at a meeting and interested shareholders (and their associates) may have to abstain from voting. In this case, the transaction documents need to build in provisions to make the transaction conditional on the company obtaining this approval.

Signing logistics

Even where a transaction has appropriate authorisation, the governance professional knows that these would have to comply with legal formalities. The major requirements are summarised below as a refresher in this guidance note.

Execution by individuals

Signing of simple contracts or deeds by individuals is straightforward. Individuals may execute a contract or deed by signing it and, in the case of a deed, also attaching a seal (usually a small red circle wafer) next to the signature. Individuals may also by a power of attorney authorise an attorney to execute the document on their behalf. For example, a guarantor may need to sign a guarantee, to guarantee certain matters, or aspects, under the M&A transaction.

Execution by companies

Simple contracts. The execution of contracts on behalf of a company incorporated in Hong Kong is straightforward. The contract can be signed by any director or any person authorised by the board of directors (such as an attorney).

Deeds. In contrast, a Hong Kong company has to observe other formalities when executing a deed. Under the Companies Ordinance (Cap 622), a deed is considered to be duly executed by a Hong Kong company by fulfilling the following conditions:

(i) (a) executing the document under the common seal (see the paragraph below); or (b) (1) the sole director signing the document under hand (if the company has just one director); or (2) any two of the directors or any director and the company secretary signing the document under hand (if the company has two or more directors);

(ii) having the document expressed to be executed by the company as a deed; and

(iii) delivering the document as a deed.

Alternatively, a company may, by a power of attorney, authorise an attorney to execute a deed on its behalf.

It is worth noting that, since 2014, a Hong Kong company is no longer required to have a common seal. If a Hong Kong company adopts a common seal and wishes to execute a document by affixing the seal, it must follow the procedures contained in the articles of association in authorising the use of the seal. It is also good practice to check that the signatories are duly authorised to execute the deed by requesting a copy of the company's board resolutions.

Methods for signing a Hong Kong law contract

There are broadly three methods used when executing commercial contracts.

Wet ink signatures. This is the traditional method by which a hard copy document is signed by signatories who are present at the same physical meeting.

Virtual signing. The document is signed by signatories who are not physically present in the same location. This typically involves a hard copy document being signed in wet ink, converted into electronic form, and sent by email.

E-signing. The document is signed by signatories using electronic signatures. This can take many forms, including using a web-based e-signing platform (such as DocuSign), applying an electronic image of a handwritten signature into, or typing the name into, the relevant signature block on a soft copy version of the contract.

Not all of the methods described above will work for all types of contracts. For example, there are restrictions on using electronic signatures for certain types of documents in Hong Kong. This is sometimes the case where the documents are subject to specific formalities imposed by statute or jurisdictional requirements relating to the future use of the document or the party executing the document, including as to their form or required method of execution.

UK Mercury rule and virtual signing

It will be useful for the governance professional to know that parties entering into commercial contracts have used virtual signings for many years. The 2008 English High Court judgment in *R (on the application of Mercury Tax Group Ltd & Anor) v HMRC & Ors* has resulted in specific

guidance for carrying out virtual signings in the UK and has led legal practitioners in Hong Kong to re-examine the practice of attaching previously signed signature pages to the execution draft of a contract. It is difficult to predict whether and how the ruling of the Mercury case will be applied in Hong Kong. To err on the side of caution, it is recommended to adopt a prudent approach that a Hong Kong law deed requires the full document to be executed in order to validly execute the deed.

Announcement

In an M&A transaction where one or more parties are Hong Kong listed companies, they should be sensitive as to whether the entering into of the transaction may constitute inside information and whether the transaction is of a substantial size where additional compliance requirements such as an announcement may need to be published.

The Securities and Futures Ordinance (Cap 571) requires a Hong Kong listed company to disclose any inside information to the market as soon as reasonably practicable. The Hong Kong Listing Rules also contain obligations on the company to disclose information to avoid a false market in its securities.

Inside information disclosure

M&A transactions are commonly viewed as important transactions of a listed company and news of the company entering into such transactions may affect the trading price or volume of the company's listed securities. If the senior management or directors of a listed company considers entering into the proposed M&A transaction to be inside information, it is crucial to maintain its confidentiality until it is ready for release by way of a full announcement (usually immediately after the deal has been signed). If the necessary degree of confidentiality cannot be maintained or confidentiality may have been breached, the inside information must be disclosed immediately by the publication of a holding announcement and, if necessary, requesting a temporary suspension of trading prior to the holding announcement being published.

Notifiable/connected transaction disclosure under the Hong Kong Listing Rules

In addition to being considered inside information, an M&A transaction may constitute a notifiable transaction and/or a connected transaction pursuant to Chapters 14 and 14A of the Listing Rules which, among other compliance requirements, may need to be disclosed by issuing a deal announcement on the HKEXnews website and the listed company's own website.

How disclosure is made

The Listing Rules require all announcements of listed companies to be published on the HKEXnews website and at the same time they must be released on the company's own website. A listed company may use additional channels to disseminate news such as issuing a press release through wire services or holding a press conference. These methods should only be used in addition to publishing a formal announcement on the HKEX website and on the issuer's own website.

Pre-vetting by regulators

In a shift of its regulatory focus from pre-vetting to post-vetting and in the context of M&A transactions, the SEHK now only requires announcements of very significant transactions to be pre-vetted, that is, if the transaction is of a significant size relative to the assets, profits, revenue and market capitalisation of the listed issuer and it constitutes a very substantial acquisition, a very substantial disposal, an extreme transaction or a reverse takeover (as defined in the Listing Rules). Draft announcements of these transactions should be sent to the SEHK for review and the listed issuer may only publish them after receiving clearance from the SEHK. The turnaround time for the SEHK to pre-vet announcements is typically the same day[1], depending on the time of the submission of the announcement and the completeness of the information disclosed. It is good practice to start communicating with the SEHK in advance to allow a buffer for the pre-vetting process.

If any proposed transaction or part of it is subject to the Takeovers Code in Hong Kong, then the announcements should also be submitted to the Takeovers Executive at the Securities and Futures Commission for pre-vetting. In these cases, the officers of the SFC will take the driving seat in reviewing and clearing the announcements.

5 Pursuant to the 'Report on the Securities and Futures Commission's review of the Exchange's performance in its regulation of listing matters' (published in June 2020 p. 41), the turnaround time for the SEHK to pre-vet announcements was the same day in 97% of instances in 2018.

Timing

Announcements relating to inside information and M&A transactions may only be published during the SEHK permitted submission windows. These are:

(i) normal business day: 06.00 to 08.30, 12.00 noon to 12:30 and 16.30 to 23:00, and

(ii) non-business day preceding a business day: 18.00 to 20.00.

There are special arrangements for the eves of Christmas, New Year and Lunar New Year and during bad weather.

Signing outside of trading hours

Bearing in mind the limited publication windows, the statutory requirement to publish inside information as soon as possible and the need to submit draft announcements to regulators for pre-vetting, a listed company should carefully time the entering into of substantial transactions (and the signing of related documents) to avoid and minimise a trading halt.

Voluntary announcement

If a listed issuer enters into an M&A transaction which does not strictly fall within the ambit of the disclosure regime pursuant to the Listing Rules (as discussed above), it may opt to release a voluntary announcement.

The proper entry into a transaction, along with related compliance requirements is important for an M&A and other transactions. This guidance note should serve as a handy refresher and resource of the major issues relating to signing of agreements, and help explain them to parties to a transaction.

The members of the Institute's Takeovers, Mergers and Acquisitions Interest Group are Michelle Hung FCG FCS (Chairman), Dr David Ng FCG FCS, Henry Fung, Kevin Cheung, Lisa Chung, Patrick Cheung and Philip Pong. Gratitude is expressed to Kevin Cheung, Partner, Linklaters as the author of this paper. Mohan Datwani FCG FCS(PE), Institute Deputy Chief Executive, serves as Secretary to the Institute's Interest Groups. If you have any comments and/or suggestions relating to the Institute's Interest Groups, he can be contacted at: mohan.datwani@hkics.org.hk.