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Mergers & Acquisitions Law Guide 2013/14

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The 1st Annual Guide to Practicing M&A Law in Asia

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Foreword

On behalf of LexisNexis, it is with great pleasure that we are publishing the Mergers & Acquisitions Law Guide 2013/14. This is not only our inaugural edition on this topic; it is the first in an exciting new series of Law Guides we are commencing this year.

Mergers and acquisitions very often are marked as defining moments in a corporation's history. Furthermore, mergers and acquisitions are unquestionably on the rise in the Asia-Pacific region, with the volume, size and complexity of the deals increasing substantially in recent years. Knowing the M&A laws and regulations, and their implications, can have a crucial bearing on the success or failure of a merger or acquisition, particularly if they are being undertaken in an unfamiliar jurisdiction. By publishing this Guide, we aim to help legal practitioners and companies preparing for mergers or acquisitions to understand what needs to be done at different stages and to gain control of the process – all in a single source and covering major jurisdictions in the Asia-Pacific region.

The Mergers & Acquisitions Law Guide 2013/14 brings a comprehensive review and analysis on the current laws and regulations that govern mergers and acquisitions across the Asia-Pacific region. We have structured the book into two key sections. The Q&A section of the Guide provides a consistent set of questions and answers about general M&A practices across twelve jurisdictions in the region. The Specialist Articles section includes three articles delving deeper into the issues that Chinese enterprises face as they expand their activities across the globe, recent developments in Japan's insider trading regulations in the context of M&As, and Switzerland's growing prospects in Asia.

My thanks to all of the law firms who participated by contributing their excellent and informative chapters for this publication. We look forward to hearing your feedback on this Guide, and bringing you more Law Guides on topics we hope will be equally relevant to your needs in the very near future.

Yours sincerely,

Shawn Clark
CEO Asia, LexisNexis

TOWERS WATSON

Challenges and Solutions on the Road to the Globalisation of Chinese Multinationals

Towers Watson

Recently, the United States, Germany and Japan have seen a spate of inbound M&A transactions with most of the buyers being Chinese enterprises in the manufacturing industry, which is in desperate need of upgrading. This phenomenon tells us a few things: First of all, we can assume that global industrial transfer has reached its peak; second, many industries in the US and Europe are hard-pressed for capital following the 2008 financial crisis, leading to numerous opportunities for M&A deals; and lastly, the external appreciation and internal depreciation of the Renminbi has simultaneously put pressure on and empowered Chinese enterprises to expand their businesses overseas.

In this paper, we will discuss the expansion of Chinese companies in more detail, including the challenges they face on the route to globalisation and the learnings they can take away, with a particular focus on human capital.

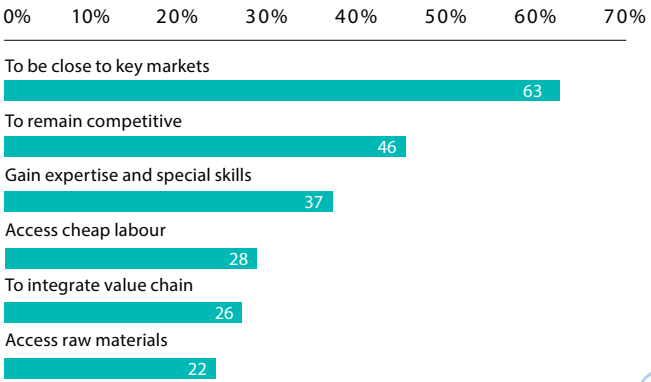
In our experience, we have found that the importance of the "people" aspect in acquisitions is often underestimated by Asian organisations — and Chinese companies are no different. We have identified the roadblocks that Chinese organisations may face and divided them into eight main headings:

1. Hiring and Retaining Key Talent
2. Underestimating the Importance of HR Due Diligence
3. Differences in Culture/Management Style
4. Differences in National Cultures
5. Power of Overseas Labour Unions
6. Mobility Difficulties
7. Difficulty in Attaining Core Technology

I. The Goals of Chinese Outbound M&A

The challenges faced by Chinese companies as they expand abroad will depend to a large extent on the reasons for expansion. The Towers Watson 2012 *Asian Trailblazers* study found that the most prevalent reason for Asian expansion (Figure 1 below) was to be close to key markets, cited by 63 per cent of respondents.

Figure 1. Key reasons for Asian multinationals to enter new markets



* Responses do not total 100% because some respondents chose multiple categories

Source: 2012 Towers Watson *Asian Trailblazers* survey report.

In our experience, Chinese companies have three main reasons for expansion:

1. **To acquire advanced branding and technology.** A common reason for expansion for Chinese organisations is to obtain key technologies and branding resources from targets with a strong industrial foundation and excellent brand image. One example is Shanghai based Fosun International's acquisition of the Greek jewellery and luxury goods retailer Folli Follie Group.

2. **To facilitate industrial upgrading.** While the Chinese government has been pushing for industrial upgrading, the domestic manufacturing industry cannot undergo these processes without external assistance.

3. **Secure access to natural resources.** This type of M&A often takes place between developing countries and state-owned resource enterprises, such as the China National Offshore Oil Corporation and the China National Petroleum Corporation. People aspects play a lesser role in resource deals and as such they are out of the scope of this discussion.

II. Challenges Chinese Companies Face in Outbound M&A Deals

Challenge 1: Hiring and Retaining Key Talent

Whatever the goal of a merger or acquisition – whether to tap into global markets or gain access to advanced technologies and management know-how – the success of the deal will depend largely on having experienced professionals with the organisation's vision in mind to guide it on its way. Acquiring companies overseas is not like setting up new factories in a foreign country, where everything can be built from scratch. In most cases, the target company will have an existing culture and processes that need to be integrated into the new entity. So having experienced management that can handle these delicate issues becomes of great importance, especially for companies in the knowledge industry.

Chinese organisations can face a number of difficulties on this front: China's current labour market does not provide sufficient numbers of management personnel or professionals experienced in international negotiations and integration. This often means that deal makers do not have the resources to perform thorough pre-

negotiation research and can underestimate the difficulty of a deal. The problem also persists after the deal has closed, as organisations may fall short of the labour needed to run the target company and integrate resources post-deal.

A survey conducted by the China Council of the Promotion of International Trade and Peking University showed that 75 per cent of respondents believe that lack of experienced international talent is the biggest obstacle for their global expansion. When TCL Communication Technology Holdings entered into a joint venture with Alcatel in 2004, company chairman Li Dongsheng launched a global recruitment drive to find an international assistant. However, ultimately, this position could not be filled suitably, paving the way for the failure of the joint venture.

In another example, when acquiring Korean Ssangyong Motors in 2005, SAIC did not have any Korean-speaking personnel. Although SAIC retained the original management team from Ssangyong, there existed a gap in cultural communication between the two sides, which added to the incessant troubles following the acquisition.

If enterprises decide to globalise in the next few years, it is suggested that they learn from other multinational corporations' best practices, for instance, taking English as a second official language, as Danone, Rakuten and Uniqlo have done. Rakuten's president Mikitani Hiroshi even declared that if critical position employees can't speak English after two years on board, they may not work in the organisation long. This might be a bit difficult for many Chinese companies, but many can take first steps in this direction by asking their employees (at least at the top management level) to work in two languages. In doing so, they may avoid problems associated with ineffective communication during an overseas labour dispute or other conflict.

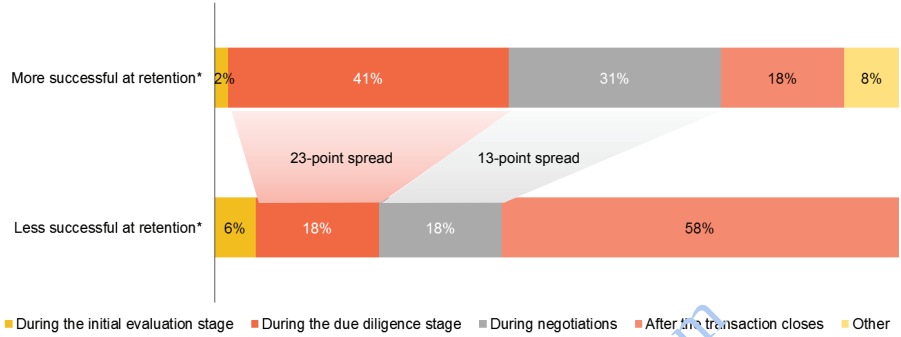
Other steps to consider to enhance in-house talent include:

- Developing a global recruitment process for expatriate executives. Some large multinational corporations such as Nissan and Sony develop their global business through recruiting non-Japanese executives.
- A plan to cultivate the organisation's talent pool through global rotation schemes and multi-language training. For example, because of its global rotation training scheme, two-thirds of Komatsu's executives have overseas working experience.

Hiring new employees is one part of the equation. Another, particularly when acquiring a company for its management know-how or technological processes, is to retain the employees of the acquired company. This is also crucial to keep some continuity, so that the deal does not become too disruptive and the new entity can begin to operate normally as soon as possible.

Towers Watson research has found that in successful deals, key talent for retention is identified early in the deal cycle (Figure 2 below).

Figure 2. Successful companies identify key employees to retain early in the process

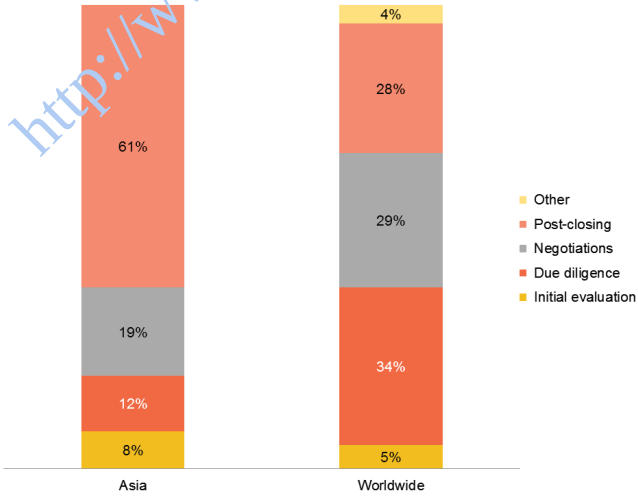


* "Successful at retention" is defined as those rating their retention agreements highly or mostly effective at retaining employees during an acquisition and retaining all or nearly all of their employees through the retention period in past acquisitions.

Source: 2012 Towers Watson *M&A Employee Retention Study*.

In light of this finding, it is troubling to note that Asian employers identify talent to retain later in the life cycle of a deal than do their global counterparts (Figure 3 below). Given the importance of key talent retention in the success of a deal, this could have the potential to put Asia Pacific employers at a significant disadvantage.

Figure 3. Stage at which global acquirers identify talent to retain



Source: 2012 Towers Watson *M&A Employee Retention Study*.

Australia

Corrs Chambers Westgarth

CORRS CHAMBERS WESTGARTH lawyers

1. What are the key laws and regulation that govern mergers and acquisitions in your jurisdiction?

Proposals to acquire control of widely held Australian entities (those listed on the Australian Securities Exchange (ASX) or with more than 50 members) are highly regulated in Australia. Smaller entities may be acquired by private contract.

The guiding principles of takeover regulation are that:

1. Control acquisitions should take place in an efficient, competitive and informed market;
2. Shareholders should:
   a. Know the identity of potential acquirers;
   b. Have reasonable time and enough information to consider proposals; and
   c. Have reasonable and equal opportunity to participate in benefits; and
3. Appropriate procedures for compulsory acquisition of securities (hereinafter known as 'compulsory acquisition') must be followed.

Generally, a potential acquirer (hereinafter known as 'bidder') may not increase the power it has, together with associates, to control voting or disposal in relation to shares (hereinafter known as 'voting power') in a target company (hereinafter known as 'target') to more than 20 per cent or from above 20 per cent up to 90 per cent. A bidder wishing to do so must generally proceed by way of takeover bid (hereinafter known as 'takeover') or scheme of arrangement (hereinafter known as 'scheme').

Limited other exceptions are available, including increases of three per cent of voting power every six months (hereinafter known as 'three per cent creep') or acquisitions approved by target shareholders (with appropriate disclosure and no voting by the bidder and associates).

Takeovers and schemes are statutory procedures regulated by the Corporations Act 2001 (Corporations Act), overseen by the Australian Securities and Investments Commission (ASIC) and the Takeovers Panel (hereinafter known as 'Panel') (see Question 2). ASIC and the Panel publish guidance on aspects of control transactions.

Takeovers

Takeovers involve bidders offering to acquire the shares of all shareholders of the target, either on-market or off-market.

In on-market bids, which are rare, bidders offer to acquire shares on the securities market on which they are traded at a certain price for a period of at least one month (see Question 10).

In off-market bids, bidders send written offers to the target and its shareholders. Offers are accepted by target shareholders returning acceptance forms before the offer expiry date. Bidders must obtain interests in at least 90 per cent of the shares in the target (and 75 per cent of those bid for) to be entitled to proceed to compulsory acquisition of the remaining shares (see Question 12).

Bidders may offer cash and/or other consideration, usually bidder securities. The offer of bidder securities may be regulated by local laws in the jurisdictions where foreign target shareholders reside. The consideration must at least equal the highest price paid by the bidder for any target shares acquired in the previous four months.

Schemes

Schemes are arrangements between targets and their shareholders for transfer or cancellation of their shares in exchange for consideration from the bidder. The target prepares a booklet for target shareholders containing information about the proposed scheme (hereinafter known as 'Scheme Booklet'). The arrangement must be approved at a meeting of target shareholders (hereinafter known as 'Scheme Meeting'). Court approval is also required (see Question 2). Schemes are binding on all target shareholders if all necessary approvals are obtained.

Target board support is essential for a scheme to proceed.

For targets listed on ASX, the ASX Listing Rules require the target to:

1. Disclose proposed takeover activity (other than indicative, non-binding proposals);
2. Not issue securities for three months after becoming aware of a proposed takeover; and
3. Ensure its officers do not receive termination benefits on a change in control of the target.

2. What are the government regulators and agencies that play key roles in mergers and acquisitions?

ASIC is the main government body responsible for regulating and enforcing takeover and scheme laws. ASIC has power to modify some takeover laws, with the relief applying either generally in takeovers or in individual cases. Individual relief applications are determined on a case-by-case basis and may be declined or granted conditionally. Relief is often sought from:

1. Disclosure obligations for Scheme Booklets; and
2. Requirements to notify acceptances during takeovers.

The Panel is a peer review body with members appointed from the legal and business communities. The Panel is the primary forum for resolving disputes about takeovers during the bid period.

The Panel has wide powers in relation to takeovers, primarily to declare circumstances that infringe the guiding takeovers principles explained in Question 1 to be unacceptable. It also has power to review ASIC modification decisions.

Schemes and Scheme Booklets must be approved by the Federal Court or the Supreme Court of an Australian State or Territory (court). The court orders Scheme Meetings to be held and its approval of the scheme is required following approval by target shareholders.

Scheme documentation is reviewed by ASIC, which assists the court's review by advising the court if it has any concerns.

If the target is listed on ASX, key takeover and scheme documents must be released to the ASX market.

For transactions resulting in full or partial foreign ownership of Australian companies, prior notification to the Foreign Investment Review Board (FIRB) may be required (see Question 15).

The Australian Competition and Consumer

China

King & Wood Mallesons

KING&WOOD MALLESONS 金杜律师事务所

1. What has been the general level of M&A activity over the last 12 months in your jurisdiction? What were the most notable mergers and acquisitions during that period?

In recent year, China has become the prime investment destination for foreign investors, as the Chinese middle class rises and foreign investors become more familiar with the M&A markets in China. Though the overall level of M&A transactions in 2012 saw a 14.3 per cent decrease in the number of deals and a 24.1 per cent decrease in the value of deals compared to 2011,[1] a strong recovery is expected in 2013. In 2012, there are a total of 42 inbound M&A by the foreign investors and 112 outboard M&A by Chinese domestic companies. The transaction value of these M&A deals totaled US$33.48 billion and accounted for 66 per cent of the total transaction value of all M&A deals involving Chinese domestic companies (ie including foreign M&A, domestic M&A and outbound M&A).[2]

Some of the notable Chinese outbound M&A transactions in 2012 include:

- Sinopec International Petroleum Exploration and Production Corporation acquiring 30 per cent equity in a Portugal energy company, GALP Energia
- Dalian Wanda Group acquiring 100 per cent equity in AMC Theatres Inc.
- Sinopec International Petroleum Exploration and Production Corporation acquiring the shale gas projects of Devon Energy Co.
- Bright Food (Group) Co., Ltd. acquiring 60 per cent equity in Weetabix Food Company
- Weichai Power Co., Ltd. acquiring 25 per cent equity in Kion Holding GmbH and 70 per cent equity in Linde Hydraulic

2. What are the most common methods for acquiring or merging with a public company in your jurisdiction?

The most common methods for acquiring or merging with a public company in China by domestic investors are:

- Tender offers.
- Acquisitions by agreement.
- Private placements of new shares.

However, foreign investors looking to acquire or merge with a Chinese domestic public company are subject to additional requirements and governmental approval.

The most common methods by which foreign investors acquire or merge with Chinese public companies include:

- Qualified Foreign Institutional Investor (QFII) Investment. Such foreign investors must be approved by China Securities Regulatory Commission (CSRC) as a QFII to enter the Chinese secondary market. QFIIs can convert foreign currency into renminbi through strictly supervised special accounts and invest in the domestic securities market. The QFIIs' capital gains and dividends, after

verification, can be converted into foreign currency and remitted out of China. It should be noted that the operation of QFIIs are restricted and subject to quotas.

QFIIs are typically overseas fund management institutions, insurance companies, securities companies and other asset management institutions. Foreign investors can purchase Chinese listed companies' shares through a QFII; however, a QFII's shareholding in any single listed company cannot exceed 10 per cent of that company's total shares and the total foreign investors in a single listed company must not exceed 20 per cent of the company's total shares. Therefore, QFIIs do face great difficulties in reaching a position of control within a listed company.

- Acquiring tradable B and/or H shares. Although the A-share market provides a limited access to foreign investors, a listed company is allowed to issue B and H shares to foreign or Hong Kong investors. In principle, a foreign investor could achieve control of a listed company provided it has acquired sufficient B and/or H shares. However, only a small portion of listed companies has issued B and/or H shares and the share proportion of B and H shares is typically relatively small. Therefore, currently it is not always possible for a foreign investor to control listed companies by this means. In addition, it should be noted that foreign investors are prohibited from purchasing more than 30 per cent of B shares of a listed company through the secondary market.
- Strategic Investments. Strategic investments allow certain foreign investors that meet strict requirements to directly purchase A-shares of listed companies. The policy behind the Strategic Investments is to encourage medium-to-long term investment of a strategic nature. The Ministry of Commerce (MOFCOM) will need to approve the transaction prior to the foreign investor making the strategic investment. Pursuant to Article 5.1 of the 'Measures for Strategic Investment by Foreign Investors in Listed Companies jointly issued by MOFCOM, CSRC, State Taxation Administration, SAIC and SAFE in 2005' (hereinafter known as the 'Strategic Investment Measures'), foreign investors can make strategic investments through:

  1. Acquisitions by agreements;
  2. Private placements of new shares; or
  3. Any other method sanctioned by the PRC law.

3. What are the key laws and regulations that govern mergers and acquisitions in your jurisdiction?

The key laws and regulations that govern mergers and acquisitions in China are:

1. Company Law (revised in 2005). Issued by the National People's Congress, this law governs two types of corporations: limited liability companies and joint stock companies.
2. Securities Law (revised in 2005). Issued by the National People's Congress, this is the principal law regulating public M&A in China and sets out the basic legal framework for securities.
3. Provisions on the Mergers and Acquisitions of a Domestic Enterprise by Foreign Investors (revised in 2009). Issued by MOFCOM, these provisions outline the different means, approval procedures and process by which to initiate mergers and acquisitions of domestic Chinese enterprises by foreign investors. These provisions are the most comprehensive and specifically govern the takeovers

Hong Kong

Winston & Strawn

1. What has been the general level of M&A activity over the last 12 months in your jurisdiction? What were the most notable mergers and acquisitions during that period?

According to the research of *MergerMarket*, for the year 2012, there were over 760 M&A transactions in Hong Kong and China. The aggregate transaction value of 2012 increased by 4.7 per cent to US$144.9 billion as compared to 2011. Outbound cross-border M&A transactions remained strong in 2012 with the transaction value amounting to US$64.6 billion. Inbound activity, however, experienced a 20 per cent decline compared with 2011, slipping to US$25.3 billion.

Tops deals in 2012, in terms of their transactional value, include the acquisition of 15.57 per cent stake in Ping An Insurance Company by Charoen Pokphand Group Co Ltd and the acquisition of CDMA network assets in China Telecommunications Corporation by China Telecom Corporation Ltd.

In 2012, there were four privatisation transactions involving listed companies in Hong Kong, including Little Sheep Group Ltd, Zhengzhou China Resources Gas Co Ltd, Samling Global Ltd and Alibaba.com Ltd. According to the HKEx Fact Book 2012, 17 Hong Kong listed companies, including Far East Global Group Ltd, Frasers Property (China) Ltd and Hang Ten Group Holdings Ltd underwent takeovers and mergers in that year.

2. What are the most common methods for acquiring or merging with a public company in your jurisdiction?

Acquisitions of public companies in Hong Kong are commonly structured as a takeover offer or a scheme of arrangement.

Voluntary or Mandatory Takeover Offer

One of the common methods used for obtaining control of a public company in Hong Kong, if considered fit for commercial reasons, is to make a voluntary offer to acquire the shares held by the shareholders of the target public company (hereinafter known as the 'target company') pursuant to the Code on Takeovers and Mergers (the Takeovers Code) of the Securities and Futures Commission of Hong Kong (SFC). If the offer is accepted, the offeror will obtain the majority control of the target company. Subject to certain restrictions, the consideration for the offer can be in cash or in securities, or a combination of both.

Under the Takeovers Code, there are certain events – the occurrence of which will require a person or persons to make a mandatory offer to the shareholders of the target company to acquire all the shares of the target company's shareholders. This requirement to make a mandatory offer will arise if :

1. A person (and the persons acting in concert) acquires 30 per cent or more of the voting rights in the target company, whether through a single or a series of transactions; or

2. A person (and the persons acting in concert) holding not less than 30 per cent, but not

more than 50 per cent of the voting rights in the target company, and that person (and the persons acting in concert) acquires voting rights in the target company, which has the effect of increasing such person(s)'s percentage holding in the target company by more than two per cent from the lowest percentage holding of that person(s) in the 12-month period ending on and inclusive of the date of the relevant acquisition.

The consideration of a mandatory offer must be in cash or be accompanied by a cash alternative at not less than the highest price paid for by the offeror, or any person acting in concert with it, for shares carrying voting rights during the offer period and within the six-month prior to the commencement of the offer period.

Scheme of Arrangement

Apart from voluntary and mandatory takeovers, the Hong Kong Companies Ordinance (the 'CO') provides for a court-sanctioned scheme of arrangement, which can be undertaken by listed companies that wish to undergo corporate reorganisation or privatisation. A scheme of arrangement usually involves the controlling shareholder(s) of the listed target company acquiring the shares of the minority shareholders, which is usually called a 'transfer scheme', followed by an application to the Hong Kong Stock Exchange (the SEHK) to de-list the company. Apart from such acquisition, a scheme of arrangement may be effected through the cancellation of the existing shares of the minority shareholders and issuance of new shares to the controlling shareholder of the target company. This is sometimes referred to as a 'cancellation scheme'. If the scheme of arrangement is effected by way of a transfer scheme, stamp duty will be payable for the sale and purchase of shares. The implications of Hong Kong stamp duty are further elaborated in Question 8 below.

If a scheme of arrangement is proposed, the Hong Kong court, upon the application of the listed company, may order to convene a general meeting of all shareholders to consider, and if thought fit, approve the proposal. Under the CO and the Takeovers Code, which also applies to schemes of arrangement, a scheme of arrangement can only take effect if:

1. A majority in number representing 75 per cent in value of the disinterested shareholders present and voting either in person or by proxy at the meeting have approved the scheme;
2. The number of votes cast against the scheme at the meeting is not more than 10 per cent of the votes attaching to all disinterested shares; and
3. The court approves the scheme.

3. What are the key laws and regulation that govern mergers and acquisitions in your jurisdiction?

The Hong Kong Companies Ordinance

The CO is the main legislation governing M&A transactions in Hong Kong. Under the CO, all Hong Kong incorporated companies and overseas companies registered under Part XI of the CO must comply with the requirements applicable to such transactions.

The Securities and Futures Ordinance (SFO)

Bidders in takeover transactions will have to consider the implications of the requirements under the disclosure of interests regime under Part XV of the SFO. The statute imposes filing obligations on persons who acquire five per cent or more of interests in shares, whether voting or non-voting, of a Hong Kong listed company. Filings are required to be made for subsequent changes to such interests. Stricter obligations are imposed on directors of listed companies, who are required to report all their interests in shares held in the listed companies.