

CHAPTER 4

FINANCING THE TRANSACTION

THE AUCTION PROCESS IN PRIVATE EQUITY TRANSACTIONS

4.1 As it is not common for PE investors to invest in existing shares of an investee company, the following discussion will focus on the sale of new equity by an investee company. Sale of new equity of an investee company by auction in a PE transaction allows the investee company to look for the most preferred purchaser or investor among a number of competing bidders. In some large transactions, the investee company may initiate an auction sale so that PE investors will have to compete with other potential investors and trade purchasers for the investment opportunity.

4.2 An auction sale offers many more advantages to an investee company than a traditional negotiated sale of new equity. It enables the investee company to reach out to a number of potential investors at the same time and make use of the competitive sentiment among them to obtain the most favourable terms. In order to win the bid, the bidders will often offer a higher purchase price for the investee company with less stringent investment terms. The investee company can maintain more control over the issuance and sale process than in a negotiated sale transaction.

Typical process of an auction sale

4.3 The process for an auction sale in the context of PE investments is similar to an auction sale of companies. It is typically divided into three stages:

4.4 *First stage:*

- (a) *Finding bidders:* With the assistance of its auction sales team which includes legal, financial and business advisers, the investee company will source interested bidders in the market. The sales team will prepare an information memorandum¹ which contains basic information about the investee company and its business.

¹ See Chapter 8.

- (b) *Evaluation and submission of indicative offers:* Based on the information memorandum, interested bidders will preliminarily evaluate the proposed transaction and submit their initial indicative offers.

4.5 *Second stage:*

- (a) *Selection based on indicative offers:* The investee company will review the bidders' indicative offers and decide which of them can participate in the auction sale. At this stage, the investee company will also provide a draft subscription agreement or a sale and purchase agreement to the selected bidders. The agreement will contain a framework of its expected structure and terms for the transaction.
- (b) *Initial due diligence:* The selected bidders will commence initial due diligence review to obtain more information for the proposed transaction.
- (c) *Submission of second round offers:* After evaluating additional information, the bidders can further consider the desirability of the proposed transaction and will submit their second round offers if interested.

4.6 *Third stage:*

- (a) *Selection of purchaser/investor:* Based on the second round offers, the investee company will select the most preferred bidder to be the purchaser/investor. They will commence formal negotiation of the final terms of the transaction and execute definitive transaction documents and close the transaction.

Important issues in each stage

4.7 *First stage:*

Confidentiality

4.8 As there will be a number of bidders having access to the investee company's information, the auction process will generate a higher risk of unauthorised use and dissemination of such information. Therefore, preservation of confidentiality will be a major concern for the investee company.

4.9 It is preferable for the investee company to prevent the bidders from knowing the identity of each other. Otherwise there may be a risk that some bidders will collaborate in secret and conspire to make offers on more or less the same terms that are not favourable to the investee company. This will frustrate the investee company's purpose to drive for the best transaction terms. In extreme cases, it may even lead to the abortion of the proposed transaction. As such, the investee company should require the bidders to keep their participation in the auction sale confidential.

4.10 If the investee company is a listed company in Hong Kong, it shall also impose on bidders the obligation to observe the insider dealing prohibitions under the Securities and Futures Ordinance (Cap 571) (SFO) and the bidders should not deal in any securities of the investee company when they have obtained inside information. The investee company should comply with the relevant Listing Rules and the Takeovers Code including all the disclosure and approval requirements in each step of the auction process.

4.11 These confidentiality matters are usually dealt with in a binding confidentiality agreement signed at the outset of an auction sale. Typical parties will be the investee company as the disclosing party and the bidder as the recipient. If any unsuccessful bidder breaches the confidentiality agreement, the investee company can enforce its rights against such person.

Information memorandum and process letter

4.12 An information memorandum is the principal selling document prepared by the investee company in an auction sale. It contains basic information about the investee company and its business which will be provided to potential bidders for evaluating their proposed investments. It assists potential bidders to decide whether to proceed with their initial indicative offers and on what terms. An information memorandum generally contains the following information of the investee company:

- (a) its incorporation history;
- (b) its business and operation;
- (c) its financial information and projections;
- (d) its major assets, major business relationships and material contracts;
- (e) information on its board members, management team and senior employees; and
- (f) an overview of market conditions and how the investee company competes in the market.

4.13 A process letter is usually distributed by the investee company together with the information memorandum. The process letter includes information such as a timetable of the auction sale, the required format of the indicative bids and other general instructions of the auction process. It is common for the investee company to state in the process letter that it has the right to amend or discontinue the auction. It will also reserve the investee company's right to select the most suitable bid at its sole discretion which means the highest-price offer may not necessarily mean a successful bid. This will give the investee company flexibility in controlling the auction process and choosing the most suitable purchaser/investor.

Initial indicative offers

4.14 A PE investor interested in making an indicative offer should prepare such an offer according to the format described in the process letter. Its contents should include a brief description of the major terms of the proposed investment such as the offer price, basis and form of consideration, and manner of payment. The PE

investor can add conditions which must be fulfilled before making its offer such as satisfactory due diligence results, obtaining its investment committee's approval and consents and regulatory clearance, if required. Since an initial indicative offer is preliminary, the terms therein are non-binding and subject to contract.

4.15 *Second stage:*

Due diligence and data rooms

4.16 Unlike a negotiated acquisition where the purchaser/investor often prepare a due diligence questionnaire for the investee company to answer, the investee company in an auction sale usually takes the initiatives to prepare the data room to facilitate the potential bidders' due diligence review. The advantages of preparing a data room are that the information which the investee company will disclose to the bidders will be standardised, thus ensuring a fair auction process in respect of information disclosure. It also spares the investee company from having to duplicate its efforts to answer various sets of similar but different due diligence questionnaires of the bidders. The investee company can better monitor the dissemination, use and security of information through the use of data rooms. To enhance efficiency and security, virtual data rooms are becoming popular nowadays. They allow multiple bidders to review the documents at the same time in a secured manner which also prevents the bidders from learning each other's identity in the due diligence process. At this stage, the investee company will send the bidders a draft subscription agreement or a sale and purchase agreement (**Subscription Agreement**) which illustrates its position.

4.17 *Third stage:*

Selection of the most preferred investor

4.18 Based on the results of a due diligence review and after reviewing the investee company's draft Subscription Agreement, the potential bidders will prepare and submit their second round offers. Similar to the initial indicative offers, the second round offers are not binding and subject to further negotiations and execution of definitive transaction documents.

4.19 Apart from the offer price when deciding which investor should be formally selected, the investee company should also consider whether the proposed transaction structure and the major proposed terms as stated in the second round offers are acceptable. If a preferred investor is a PE investor and the investee company will retain its existing shareholders, the investee company should take into account, the PE investor's management record of other portfolio companies, its management style and whether it can blend in with the existing management, and restrictions which are likely to be imposed by the PE investor on the company and its future operation.

Exclusivity

4.20 It is common for the selected investor to ask for an exclusivity period considering it would have already spent much time and costs on the auction

process and due diligence. An exclusivity period ensures the investee company will not continue to solicit other bidders. Sometimes the investee company will, on its own initiative, grant the selected investor an exclusivity period to demonstrate sincerity and enhance the confidence of the selected investor in the on-going course of dealings. It will provide a period of time for the selected bidder to conduct a final round of due diligence and for the parties to negotiate the final transaction terms and prepare and execute the definitive transaction documents.

PRIVATE EQUITY FINANCING – EQUITY

4.21 The structure of a PE investment, as well as its terms and conditions will vary in nature and complexity depending on the type and size of the investment. Key goals for a PE investor will usually include:

- (a) gaining full access to management decisions/discussions, business records and other information so as to monitor the investment;
- (b) allowing management to run the business but gaining the ability to take control of the management of the business or block certain types of action if necessary; and
- (c) exiting the investment for a profit (a return on investment measured either by an internal rate of return or an investment multiple) usually after three to five years.

4.22 In short, a PE investor wants to monitor, prevent actions that might harm its investment and find a profitable exit.

4.23 These key goals can be broadly achieved by a combination of careful structuring of the investment and clarity in the equity documentation as to the rights and obligations of all parties. At the outset, it is important that all parties seek tax advice on the structure of the proposed investment as even slightest variation can have a marked impact on the tax efficiency and harmony of interests.

Structure

Developmental capital

4.24 A developmental capital investment will generally consist of a PE investor subscribing for preferred ordinary shares and/or redeemable preferred options or notes in an existing company. The shares issued to the PE investor will usually be preferred ordinary shares, generally known as A shares, B shares or preferred shares, depending on whether other rounds of investment have preceded or are anticipated. Existing shareholders prior to the first investment will hold standard (or vanilla) ordinary shares.

4.25 In most cases, the investee company will need to amend its articles of association or adopt new articles to enable it to issue the types and number of securities required to be issued under the investment arrangements and to incorporate the preferential rights of the PE investor. In rare cases, a PE investment will require a restructuring of the investee company (or group) or the incorporation of a new company or companies as part of the investment process.

Buyouts

4.26 Buyouts are generally more complex than developmental capital investments. The most basic structure is for a new company to be incorporated to buy the target's business or the target company. More commonly, a buyout structure involves the incorporation of two or more new companies. Each of the companies will have a different function within the new group. Even more complex structures involve the incorporation of three or more companies. This usually establishes a structural subordination of debt in favour of senior lenders whereby they will lend to companies that are closer to the core assets of the business.

4.27 Whatever the complexity of the buyout vehicles' structure, the PE investor will subscribe for preferred shares and preferred options or notes in the parent company of the new group of companies. Management will subscribe to a different class of ordinary shares with different rights.

4.28 The share classes together form the equity component of the investment. The PE investor will hold what is commonly referred to as the institutional strip and the managers will hold the sweet equity. This reflects the fact that management shares are meant to act as an incentive to management and are often subscribed for at a lower price than the PE investor's shares.

*Investment capital***Ordinary shares**

4.29 Ordinary shares are the standard and most basic form of capital instrument. The rights attached to ordinary shares are generally set out in the governing documents (ie, the memorandum of association and the articles of association). In the context of a buyout, it is unusual for management to receive dividends on their equity (structured as ordinary shares) prior to exit. Some other incentive scheme is often provided to management as an incentive for reaching the performance goals prior to the buyout.

Preferred shares

4.30 Preferred shares have priority over ordinary shares and may have preference over other classes of shares. Preferred shares will usually form the bulk of capital received by a PE investor (unless notes are used, as discussed below).

4.31 Preferred shares will normally have rights that are significantly more favourable than shares held by other shareholders (in the case of a buyout, by management). The rights attached to preferred shares are generally set out in the governing documents (ie, the memorandum of association and the articles of association) and in the shareholders agreement if one is adopted. The most important rights will be:

- (a) *Dividends*: PE investors seeking an ongoing yield from their equity investment may require a dividend expressed as a percentage of

profits or on a fixed rate based on a percentage of the issue price of the preferred shares. These dividends may be payable from the outset or after a specified period has passed. Any unpaid dividends (eg, if there are insufficient distributable profits to pay dividends) may be rolled-up or converted to debt at a much higher interest rate. In the context of a buyout, it is unusual for ordinary shareholders/management to receive dividends prior to exit.

- (b) *Voting rights*: Preferred shares generally are enfranchised to enable the PE investors to take ultimate control of the investee company by allowing the preferred shareholders to vote as ordinary shares at some predetermined ratio that give them a substantial (if not majority) stake. If the PE investors control a majority of the voting power in the investee company (as calculated on an as converted basis), they will have ultimate control over board matters and possibly on winding-up (if there is greater than 75% control). However if they are only minority shareholders, the PE investors will want to limit the power of the majority in the definitive transaction documents.
- (c) *Return of capital*: Preferred shares will rank ahead of ordinary shares on a return of capital at windup and possibly on exit if the PE investor faces a loss on its investment.

Notes

4.32 A note is not equity. Rather, it is a debt instrument and like other forms of debt, requires interest to be paid and the principal to be repaid by a specified date. These will usually form the bulk of the note investment by the PE investor (unless preferred shares are used, as described above).

4.33 The terms of the note will be set out in a note instrument rather than in the articles of association. Notes generally carry a higher rate of interest relative to senior debt. In terms of risks and reward, notes sit between equity and senior debt. Notes may be secured but will generally be subordinate to other forms of debt (senior or mezzanine).

4.34 Although notes give the appearance of more debt on an investee company's balance sheet, their benefits include:

- (a) interest payable on the notes is generally deductible thereby reducing taxable profits;
- (b) notes heighten the investee company's gearing ratio by theoretically increasing profits per share; and
- (c) interest and principal payments are generally not as restrictive under the law as dividend payments and redemption.

4.35 In a buyout, management may invest in notes, especially in secondary or subsequent buyouts where there are certain tax advantages for managers who roll-over some or all of their original investment.

Agreed to and accepted by:

The Company:

For and on behalf of

[insert name of the Company]

[insert name of authorised signatory]

Position:

The Majority Shareholder

For and on behalf of

[insert name of the corporate Majority Shareholder]

[insert name of authorised signatory]

Position:

[OR]

[insert name of the individual Majority Shareholder]

CHAPTER 10

EQUITY COMMITMENT LETTER

INTRODUCTION AND BACKGROUND

10.1 This is a precedent equity commitment letter under which the private equity (PE) investor is asked to confirm that sufficient funds will be put in place for the purchasing vehicle (ie, the Purchaser) to complete the acquisition of the shares of the selling shareholders, prior to the execution of the relevant sale and purchase agreement (SPA). The letter should be modified to suit the actual circumstances. The sellers may consider adding more undertakings into the letter as appropriate.

PRECEDENT EQUITY COMMITMENT LETTER

[Letterhead of the Investor]

Strictly private and confidential

[insert names of selling shareholders]

[insert address]

Date: [insert date]

Dear Sirs,

Proposed Sale and Purchase of the [Entire] Issued Share Capital of [insert name of investee company] (the Company)

- 1 We refer to the proposed sale and purchase of the [entire] issued share capital of the Company (the **Proposed Transaction**) by [name of purchaser] (the **Purchaser**), subject to the terms and conditions of a sale and purchase agreement to be made between you as sellers (the **Sellers**) and the Purchaser (the **SPA**). The latest draft of such SPA is attached to this letter. Unless otherwise defined, capitalised terms used herein shall have the same meanings as those defined in the SPA.¹
- 2 In consideration of the Sellers entering into the SPA, we hereby undertake to the Sellers that we will, and will procure that, sufficient funds will be provided to the Purchaser on or before the Completion Date for the purpose of completion of the Proposed Transaction in accordance with the terms of the SPA, *subject to* the conditions that:
 - (a) all conditions precedent contained in the SPA having been fulfilled or waived in the manner prescribed therein; [and]
 - (b) the SPA being in full force and effect[;]
 - (c) [all requisite approvals and consents of our Investment Committee having been obtained for the Proposed Transaction and all third party consents and necessary governmental approvals having been obtained; and]
 - (d) [the Purchaser having drawn down the credit facilities made available to it by the Banks pursuant to the Credit Agreement].²

¹ Paragraph 1 provides the background of the proposed transaction and incorporates the definitions of the final form of the SPA into the letter.

² Paragraph 2 is the key undertaking by the PE investors as to their obligation to put in place sufficient funds for completing the proposed transaction. Such undertaking will be provided against the Sellers agreeing to enter into the SPA with the PE investors. The PE investors' undertaking to procure funds should be given on the conditions that the SPA's terms and conditions will be satisfied and the acquisition will proceed. If the acquisition would require the consent/approval of the PE investors' own investment committees, such prior consent/approval should be made as a condition to the undertaking. Further, as it is common that a PE investment will be financed by banks' credit facilities, the funding obligation will be conditional upon the availability of such credit facilities.

- 3 We undertake to procure the Purchaser to:
 - (a) [subject only to satisfaction of the conditions referred to in paragraphs 2(a), 2(b) and 2(c) above, take all steps to draw down the credit facilities under the Credit Agreement on or before the Completion Date, and to enforce its rights under the Credit Agreement where necessary;]
 - (b) make due payment of the Consideration in accordance with the terms of the SPA; and
 - (c) perform such other relevant obligations under and in accordance with the terms of the SPA for the consummation of the Proposed Transaction.³
- 4 We will not, and will procure our investors and their affiliates not to, amend or agree to amend the terms of, or waive any of the Purchaser's rights or any conditions under, or take any steps that would result in an Event of Default (as defined in the Credit Agreement), which will prejudice the Purchaser's ability to make due payment of the Consideration pursuant to the SPA.⁴
- 5 We warrant to the Sellers that:
 - (a) we have full and unfettered right, power and authority to enter into and perform the obligations set out in this letter;
 - (b) the execution, delivery and performance of our obligations under this letter does not and will not violate our constitutional documents, and will not violate the provisions of any applicable laws or contractual documents binding on us; and
 - (c) the Purchaser has received confirmation from the Banks that the conditions precedent under the Credit Agreement are satisfied, or that the documents constituting satisfaction of such conditions precedent are in agreed form, as the case may be.⁵

³ Paragraph 3 is an additional undertaking by the PE investors to procure the Purchaser to fulfill certain obligations. Where debt financing is used and the Purchaser is a borrower under the credit facilities agreement, the sellers will usually ask the PE investors, as the Purchaser's controlling owner, to ensure that the Purchaser will draw down the credit facilities to pay the purchase price on or before completion of the proposed transaction. It is common to request the PE investors to ensure that the Purchaser will generally comply with the SPA, including making due payment of the consideration.

⁴ Paragraph 4 expands the scope of the PE investors' undertakings, such that they have to ensure that their investors (such as limited partners) and their affiliates will not do anything which may create an event of default under the credit facilities agreement, which will prevent the Purchaser from drawing down the credit facilities to satisfy the payment obligations.

⁵ Paragraph 5 includes the general warranties to be given by the PE investors as to their power and authority to sign the equity commitment letter and to perform their obligations under the letter. Warranty (c) is a confirmation from the PE investors that the necessary conditions of the credit facilities agreement have been fulfilled, which will give further comfort to the sellers that sufficient funds will be available to the Purchaser on completion.

- 6 We acknowledge that the Sellers are relying on the undertakings and warranties given by us in this letter in entering into the SPA.
- 7 This letter and our obligations hereunder shall expire and be of no further force or effect upon completion of the Proposed Transaction or the termination of the SPA, whenever is earlier.⁶
- 8 The letter shall be governed by and construed in accordance with the laws of the Hong Kong Special Administrative Region of the People's Republic of China.
- 9 We and the Sellers irrevocably agree that the Hong Kong courts are to have non-exclusive jurisdiction to settle any disputes and to entertain any suit, action or proceedings arising out of or in connection with this letter (**Proceedings**) and waive any objections to Proceedings and such courts on the grounds of inappropriate forum.

Yours sincerely,
 For and on behalf of
 [insert name of the Investor]

 Name:
 Title:

We, the Sellers, hereby acknowledge that we accept the terms of this letter on [insert date].

For and on behalf of	For and on behalf of	For and on behalf of
[insert name of Seller A]	[insert name of Seller B]	[insert name of Seller C]

_____ Name:	_____ Name:	_____ Name:
_____ Title:	_____ Title:	_____ Title:

6 Paragraph 7 provides when the obligations of the PE investors under the equity commitment letter will expire. It is crucial to have a specific extent of liabilities which the PE investors will have to bear under the letter.

CHAPTER 11

EXCLUSIVITY LETTER

INTRODUCTION AND BACKGROUND

11.1 An exclusivity agreement/letter primarily benefits the Investor by preventing the Company from negotiating with other potential investors for a certain period of time, ie, the Exclusivity Period. Because the Company will be bound under an exclusivity agreement not to look for other investors, it gives the Investor time and an opportunity to conduct due diligence, conduct negotiations, make financial arrangements, and prepare definitive transaction documents during the Exclusivity Period, without having to worry about other prospective competitors. It also reduces the chance of the Company leveraging the interest of other potential competitors against the Investor and pressure the Investor to accept a higher subscription price or transaction terms which may be less favourable to the Investor. The risks of wasting the Investor's time and money on a proposed transaction which may be ambushed and fall apart can be minimised to a certain extent.

11.2 An exclusivity agreement may take the form of a separate agreement or form part of the heads of terms as binding provisions.

11.3 This precedent takes the form of a letter from the Investor addressed to the Company in relation to a proposed investment in the Company by way of subscription of preference shares to be issued by the Company. Modifications will be needed to reflect the results of negotiation and to suit the actual circumstances.

PRECEDENT EXCLUSIVITY LETTER

[Letterhead of the investor]

Strictly private and confidential

To: Board of Directors

[insert name of investee company]

[insert address of investee company]

[insert date]

Dear Sirs,

Exclusivity Letter

- 1 We refer to our recent discussions in relation to our proposed investment in [insert name of investee company] (the **Company**) by way of subscription of preference shares to be issued by the Company (the **Proposed Subscription**).¹
- 2 In consideration of [our costs and expenses incurred in carrying out due diligence investigations in connection with the Proposed Subscription] [OR] [our payment of HK\$[100.00] to you (receipt of which you hereby acknowledge)], you hereby undertake that during the period from the date of this letter until [insert time] on [insert date] (or such other time and date as may be mutually agreed to by you and us in writing) (the **Exclusivity Period**):
 - 2.1 you shall terminate all discussions and negotiations with third parties relating to the Proposed Subscription immediately;
 - 2.2 you shall not directly or indirectly solicit, invite, initiate or encourage any other approach, proposal or offer, nor enter into any discussions, negotiations, arrangements or agreements (whether legally binding or not), from or with any other person for the purpose of securing an offer for the subscription, sale, transfer or in any way dispose of any shares and/or key assets of the Company (except that in the case of sale of any asset only, in the ordinary course of business); and
 - 2.3 you shall not give or make available any confidential information relating to the Company and/or the Proposed Subscription to any third parties (including any third parties with whom you and/or your shareholder(s) have been in discussion or negotiation with prior to the date of this letter), unless disclosure is required by the applicable laws and regulations or court orders.²

¹ Paragraph 1 contains a general description of the Proposed Subscription.

² For the exclusivity letter to be binding and enforceable as an agreement, the obligations under the exclusivity letter have to be supported by consideration. It can either be the payment of a nominal amount or the costs incurred by the Investor

- 3 You shall use your best endeavours to procure that the following persons comply with the provisions in paragraph 2 above:
 - 3.1 your [insert figure]% shareholders, directors, employees, officers, agents, professional advisers and other representatives; and
 - 3.2 any of your affiliates and subsidiaries and their respective directors, employees, officers, agents, professional advisers and other representatives.³
- 4 If during the Exclusivity Period, any third party approaches the Company in connection with any proposed offer or expression of interest for the acquisition of the entire or any part of the issued share capital of the Company, the subscription of any shares of the Company, and/or the acquisition of any key assets and/or the business of the Company, you shall:
 - 4.1 immediately inform us in writing of the incident [without being obliged to disclose the name of the relevant third party]; and
 - 4.2 notify the relevant third party of the existence of this letter and the provisions of this paragraph, while keeping our identity as the potential investor and any information in relation to our discussions and negotiations in relation to the Proposed Subscription private and confidential.⁴
- 5 This letter shall immediately terminate and we may withdraw from discussions or negotiations with you if any of the following occurs, whichever is earliest:
 - (a) we give you a [3] days' notice in writing stating that we will not proceed with the Proposed Subscription;

in connection with the proposed investment. The Investor has to ensure that it has already incurred certain costs at the time the exclusivity letter is entered into.

Paragraph 2 also sets out the duration of the Exclusivity Period to be granted to the Investor and the exclusivity obligations of the Company, including its obligations not to solicit offers, whether directly or indirectly, and not to disclose any confidential information relating to the Company or the Proposed Subscription to any third parties.

- 3 Paragraph 3 imposes an obligation on the Company to ensure that all related parties of the Company will comply with similar obligations as those set out in paragraph 2. If the Company has many shareholders, some of whom it cannot control, it is common to restrict only shareholders with a certain minimum shareholding.
- 4 Paragraph 4 imposes an obligation on the Company to immediately notify the Investor in writing if any third party approaches the Company in connection with any proposed offer or expression of interest for investment or acquisition of the Company, its assets and/or its business. In case of approaches by third parties, the Company is required to notify such third parties that it is bound by the obligations under the exclusivity letter, and shall not reveal the Investor's identity and any information relating to the Proposed Subscription.

- (b) [you give us a [3] days' notice in writing stating that you will not proceed with the Proposed Subscription]; or
- (c) the Exclusivity Period expires.

Any rights accrued to us under this letter shall remain in full force and effect notwithstanding termination.⁵

- 6 If you fail to observe any of your obligations under this letter, you shall fully indemnify and keep us indemnified from and against all or any loss, claim, penalties, reasonable costs, expenses and fees (including professional fees) or other liability which we incurred as a direct result of your breach of any such obligations, within [period] upon the presentation of the relevant amounts so incurred by us.

[OR]

If you fail to observe your obligations under this letter, within [7] days after your receipt of our written request, you shall pay us a total sum of HK\$[insert amount] as liquidated damages for all or any loss, claim, penalties, reasonable costs, expenses and fees (including professional fees) incurred by us. You acknowledge that the said amount is a genuine pre-estimate of the losses and damages which we may suffer for the breach of your obligations under this letter.⁶

- 7 You accept and acknowledge that damages alone would not be an adequate remedy for any breach of the provisions of this letter by you. Without prejudice to any other rights or remedies that we may have, we shall be entitled to the remedies of injunction, specific performance or other equitable relief from the courts of any applicable jurisdiction in the event of a breach or threatened breach by you. Nothing contained in this letter shall be construed as prohibiting us from pursuing any other remedies available to us for any such breach or threatened breach.⁷
- 8 This letter is intended to be legally binding and shall be governed by and construed in all respects in accordance with the laws of the Hong Kong Special Administrative Region of the People's Republic of China

5 Paragraph 5 specifies how and when will the exclusivity letter terminates, and preserves the right of the Investor to claim against the Company for any antecedent breach of the exclusivity letter. It is common not to give the Company any unilateral right to terminate the exclusivity letter as this will defeat the purpose of the Exclusivity Period.

6 Paragraph 6 provides the right of indemnification to the Investor for any breach of the Company's obligations under the exclusivity letter. The indemnity can be either generally worded to cover the costs incurred by the Investor, or can specify an agreed amount of liquidated damages which should represent a genuine pre-estimate of the losses and damages.

7 Paragraph 7 provides that the Investor is free to pursue other forms of remedies notwithstanding the indemnity provision in paragraph 6.

(Hong Kong). Each party to this letter hereby irrevocably submits to the [exclusive]/[non-exclusive] jurisdiction of the courts of Hong Kong.⁸

- 9 If any one or more of the provisions contained in this letter are held to be unenforceable, invalid or illegal in any respect, such provision(s) shall, to the extent required by the applicable laws, be severed from this letter and rendered ineffective, with the enforceability, validity and legality of the remaining provisions unaffected.⁹

Please acknowledge your agreement to the terms of this letter by signing and returning the enclosed duplicate of this letter to us.

Yours faithfully,

[insert name of investor]

[On the enclosed duplicate of the letter]

We hereby acknowledge receipt of your letter dated [insert date]. We accept and agree to the terms set out therein.

[insert name of investee company]

[insert date]

- 8 The parties, especially if they are from different jurisdictions, should elect the applicable law to govern the exclusivity letter, and the courts where disputes should be resolved. A submission to the *non-exclusive* jurisdiction of certain courts means that the parties can litigate elsewhere apart from the selected jurisdiction; whereas electing to submit to an *exclusive* jurisdiction means that they must resolve their disputes in the specified forum. The parties should consider carefully before making the election as it will implicate the efficacy and costs of litigation and enforcement.
- 9 Paragraph 9 ensures that even if one or more paragraphs in the exclusivity letter are found to be unenforceable, the enforceability of the rest of the letter shall not be affected.

CHAPTER 12

SUBSCRIPTION AND SHAREHOLDERS' AGREEMENT

INTRODUCTION AND BACKGROUND

12.1 This Agreement is prepared on the basis that the drafter is acting on behalf of the investor.

12.2 In drafting this Agreement, it has been assumed that:

- (a) there is a single private equity investor;
- (b) there are a number of individual founders who retain their shares in the Company and do not participate in this investment round;
- (c) there are conditions to the investment and, as such, it contains provisions for split exchange and completion, and rights in favour of the investor to terminate the Agreement between exchange and completion;
- (d) there is no significant external debt finance; and
- (e) the Agreement is subject to the laws of Hong Kong.

12.3 For a long form investment agreement in a newly-incorporated private limited company by a private equity fund investor and members of the target's senior management team pursuant to a management buy-out, please see Investment agreement – multiple investors and Investment agreement – single investor.

PRECEDENT SUBSCRIPTION AND SHAREHOLDERS' AGREEMENT

THIS AGREEMENT is made on [insert day and month] 20[insert year] AMONG:

- 1 [insert name of company whose shares are held] incorporated in Hong Kong, Special Administrative Region of the People's Republic of China (Hong Kong), and limited in liability under number [insert company number] whose registered office is at [insert address], brief particulars of which are set out in Part 1 of Schedule 1 (the **Company**);
 - 2 the several persons whose names and addresses are set out in Schedule 2 (together the **Founders**); and
 - 3 [insert name of fund] incorporated in Hong Kong and limited in liability whose registered office is at [insert address] (the **Investor**);
- for the purposes of this Agreement, each of the Company, the Founders and the Investor being a **Party** and together the Company, the Founders and the Investor are the **Parties**.¹

RECITAL:

The Investor has agreed to invest in the Company subject to and in accordance with the terms and conditions of this Agreement.²

THE PARTIES AGREE:

1 Definitions and interpretation³

- 1.1 In this Agreement, unless the context otherwise requires the following expressions shall have the following meanings:

Accountants' Report means the accountants' report prepared by [insert name] as of [insert date], a true copy of which comprises Annexure 1;

- 1 The registered company name, office and number of the Company and the Investor should be inserted accordingly. If a company is trading under a name other than the registered company name, the words 'trading as [insert trading name]' may be inserted just after the relevant Party's address.

Each of the Founders should be detailed in Schedule 1, including their full names, addresses, email addresses and fax numbers.

- 2 Recitals are intended to explain the background of, and purpose to, the Agreement. They do not constitute substantive provisions, and are not binding unless they are specifically stated to be incorporated in the main body of the Agreement. They often state what is obvious from the title or from the first few clauses of an agreement, in which case the Parties may agree to omit them.
- 3 The definitions and interpretation provisions in this clause apply throughout the whole of this Agreement. The drafter should consider whether it is simpler to put certain definitions at the beginning of or in the relevant clause, Schedule or paragraph if used only in that clause, Schedule or paragraph.

Accounts⁴ means the audited accounts of [the Company] [each Group Company and the audited consolidated accounts of the Group] [for the accounting reference period ended on the Accounts Date] [for each of the [insert number] consecutive accounting reference periods, the last of which ended on the Accounts Date], comprising [in each case] a balance sheet, a profit and loss account [or a consolidated balance sheet and profit and loss account], notes and auditors' and directors' reports [and a cash flow statement];

Accounts Date⁵ means [insert date];

Annual Budget means the annual operating budget adopted under clause 6.3.1;

Articles means the proposed new articles of association of the Company in the approved terms to be adopted at Completion (as amended from time to time);

Board means the board of directors of the Company from time to time;

Business⁶ means the business of [insert description of the business] and all other activities including those ancillary or incidental to or in connection with such business as carried on by [the Company/the Group];

4 *Accounts*: The Investor will usually rely on the accounts of the Company/Group to determine the purchase price which it is prepared to pay for the Company/Group. If the Company has subsidiaries, individual audited accounts will be prepared for the Company and each Group Company and consolidated accounts will be prepared for the Group. This definition should be amended to identify the correct set of accounts.

The Investor will normally wish to obtain warranties in respect of the accounts of each of the Company, the Subsidiaries and the consolidated accounts of the Company and any Subsidiaries. If the definition is incorrect, the Investor may lose the protection provided by the accounts warranties. The Investor will wish to obtain warranties in respect of the audited accounts for the two to three year period prior to the Accounts Date and the definition should be amended accordingly.

5 *Accounts Date*: This should be amended to reflect the accounting reference date(s) of the Company and the Subsidiaries (ie, the date to which the Accounts are made up).

6 *Business*: This definition describes the business carried on by the Company (and Group) being acquired. The definition will be referred to throughout the Agreement (eg, in the restrictive covenants and warranties being given by the Founders). The drafter should ensure that it covers all aspects of the business at the relevant time.

Business Day	means a day, other than a Saturday, Sunday or public holiday, on which clearing banks are open for non-automated commercial business in Hong Kong;
Business Plan	means the business plan, a true copy of which comprises Annexure 2;
CO	means the Companies Ordinance (Cap 622) (CO);
[Certificate(s) of Title] ⁷	means the certificate(s) of title in the agreed form marked 'A' relating to each of the given at Completion by the Founders' solicitors and addressed to the Investor [and [insert the names of any other persons who are to receive the benefit of these certificates]];
Completion	means completion of the matters described in this Agreement by the performance of the Parties of their respective obligations in accordance with clause 3;
Completion Date ⁸	means [insert date] 20[insert year] or such other date as the Parties agree in writing;
Conditions ⁹	means the Conditions set out in clause 2.2; and Condition means any one of them;

7 *Certificate(s) of Title*: It is usual for the Investor's solicitors to investigate title and the Investor may require Certificates of Title where there are significant property interests. The Certificates of Title will confirm that the Company or any Subsidiary has good and marketable title to the Properties. If the Founders give Certificates of Title, consideration will need to be given as to how they interact with the Warranties. The Founders will usually wish to disclose the Certificates of Title generally for the purposes of qualifying the warranties relating to the Properties and the environmental warranties.

8 *Completion Date*: If exchange and Completion occur on the same date, the definition should be amended to 'the date of this Agreement'.

9 *Conditions*: The Agreement includes a number of Conditions set out in clause 2.2 which must be satisfied before Completion. The drafter should consider whether there should be deemed repetition of the Warranties at Completion.

Confidential Information ¹⁰	all data or information (whether technical, commercial, financial or of any other type) in any form acquired under, pursuant to or in connection with, this Agreement and any information used in or relating to the Business (including information relating to [the Company's][any Group Company's] products (bought, manufactured, produced, distributed or sold), services (bought or supplied), operations, processes, formulae, methods, plans, strategy, product information, know-how, design rights, trade secrets, market opportunities, customer lists, commercial relationships, marketing, sales materials and general business affairs), and which are for the time being confidential to the Company;
[Consequential Loss] ¹¹	means consequential, special, indirect, incidental or punitive damages or loss or any loss of profits or other form of economic loss however arising;
Deed of Adherence	means the deed of adherence to this Agreement in the form of Schedule 7;

10 *Confidential Information*: This definition should include all information relevant to the Company and its business.

11 *Consequential Loss*: 'Consequential loss' means any loss that is not a direct loss and refers to damage which falls within the second limb in *Hadley v Baxendale* (see below). To be recoverable, indirect or consequential loss must not be beyond the reasonable contemplation of the parties to the contract at the time when the contract was made and it is sufficient that the kind of damage which may be caused by a breach was within the reasonable contemplation of the parties. Direct losses fall within the first limb and this may include loss of profit, depending on the circumstances. Due to this uncertainty, the Founders will want to exclude liability for loss of profit. The Investor, on the other hand, will want to be able to recover loss of profit if it flows naturally from the breach. A clause which excludes 'any direct or consequential loss (including loss of profit)' will not be sufficient to exclude all profits, only those which are consequential, whereas a clause which excludes 'any loss of profit or any indirect or consequential loss' would exclude all profit. The inclusion of a definition of 'Consequential Loss' will flow through the Agreement via its inclusion in the definition of 'Losses' (see below).

British Sugar plc v NEI Power Projects Limited [1997] 87 BLR 42 (CA (Eng)).
Hadley v Baxendale [1843-60] All ER Rep 461.

The rule in *Hadley v Baxendale* says that where two parties have made a contract, which one of them has broken, the damages which the other party ought to receive

Disclosure Letter¹²

means the letter dated the same date as this Agreement from the Warrantors to the Investor disclosing matters against the Warranties, together with its schedules and the documents attached to it;

Encumbrance¹³

means any mortgage, claim, charge, pledge, lien, hypothecation, guarantee, right of set-off, trust, assignment, right of first refusal, right of pre-emption, option, restriction or other encumbrance or any legal or equitable third party right or interest including any security interest of any kind or any type of preferential arrangement (or any like agreement or arrangement creating any of the same or having similar effect);

Environmental Laws

means all applicable laws, regulations, codes of practice and other similar controls and advice made or issued by national or local governments or any other regulatory or administrative body, and all regulations and directives under the laws of Hong Kong, that are now in existence and where relevant enforceable relating to protection of the environment, including without limitation prevention of pollution of any land, water or air due to: (a) the release, escape or other emission of

in respect of such breach of contract should be such as may fairly and reasonably be considered either (1) arising naturally (ie, according to the usual course of things from such breach of contract itself) or (2) such as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract, as the probable result of the breach of it.

12 *Disclosure Letter*: Normally the Warrantors will provide a disclosure letter to qualify the Warranties. The Agreement assumes that the Warrantors will address the letter to the Investor. The Disclosure Letter should not normally be addressed from the Founders' Solicitors to the Investor's Solicitors on its client's behalf, as the Warranties are given by the Warrantors (who include the Founders) to the Investor in the Agreement. The Warranties themselves may require that certain documents are 'disclosed' and it is usual for such documentary evidence to be appended to (and form part of) the Disclosure Letter.

13 *Encumbrance*: This definition covers encumbrances that create a security interest.

any substance, including radioactive substances; (b) the production, transportation, storage, treatment, recycling or disposal of waste; or (c) the making of noise;

Environmental Report means the environmental report, a true copy of which comprises Annexure 4;

Exit means a Sale or Quotation;

[Founders' Questionnaires] means the questionnaires signed by the Founders and delivered to the Investor dated [*insert date*], a true copy of which comprises Annexure [*insert number*];

Guarantee means any guarantee, suretyship, indemnity, bonding liability, letter of comfort or other assurance or security or obligation (including a joint and several obligation) given or undertaken to secure or support the obligations (actual and/or contingent) of any third party and whether given directly or indirectly and/or by way of counter indemnity to a third party;

Freehold Properties means the freehold properties of the [Company/Group] further details of which are set out in Part 1 of Schedule 6;

Fund means any bank, company, unit trust, investment trust, investment company, limited, general or other partnership, industrial provident or friendly society, any collective investment scheme, any investment professional, any high net worth company, unincorporated association or partnership or any high value trust (all as defined by in SFO), any pension fund or insurance company or any person who is an authorised person under the SFO;

[Group] means the Company and each of its subsidiaries and Group Company means any of them;]

- 6. This Deed may be signed in any number of separate counterparts. Each, when executed and delivered by a party, will be an original; all counterparts together will constitute one instrument.
- 7. This Deed is governed by and shall be interpreted in accordance with the laws of Hong Kong. The parties irrevocably submit to the [exclusive] [non-exclusive] jurisdiction of the courts of Hong Kong to settle any disputes and claims which may arise out of or in connection with this Deed.

In witness thereof this deed has been executed as a deed and is delivered by the Acquiror on the date stated at the beginning of this deed.

SEALED with the COMMON SEAL of) [Common seal of the
 [Name of the Acquiror]) Acquiror]
 and SIGNED by its director,)
 [Name of director])

in the presence of :-) [Signature of director]

Witness:
 [Signature of witness]
 [Name, Address [and occupation] of witness]

- ANNEXURE 1**
Accountants' Report
- ANNEXURE 2**
Business Plan
- ANNEXURE 3**
Property Report
- ANNEXURE 4**
Environmental Report
- ANNEXURE 5**
Legal Due Diligence Report
- ANNEXURE 6**
Founders' Questionnaire

CHAPTER 13

INVESTMENT AGREEMENT – SINGLE INVESTOR

INTRODUCTION AND BACKGROUND

13.1 The following is a precedent of an investment agreement for a management buy-out. It sets out the terms and conditions of the transaction between the private equity investor and management relating to their joint establishment of a new company (a triple Newco structure is assumed in this precedent) for the purpose of acquisition and post-buyout operation. Modifications to this precedent will be needed to reflect the actual result of negotiation between the private equity investor and the management.

PRECEDENT INVESTMENT AGREEMENT

THIS AGREEMENT is made on [insert day and month] 20[insert year]

AMONG:¹

- (1) [insert name of company whose shares are held] incorporated in Hong Kong, Special Administrative Region of the People's Republic of China (**Hong Kong**), under number [insert company number] whose registered office is at [insert address] (the **Company**);
- (2) [insert name of company whose shares are held] incorporated in Hong Kong under number [insert company number] whose registered office is at [insert address] (**Newco 2**);
- (3) [insert name of company whose shares are held] incorporated in Hong Kong under number [insert company number] whose registered office is at [insert address] (**Newco 3**);
- (4) The several persons whose names and addresses are set out in Schedule 1 (together the **Managers**); and
- (5) [insert name of fund] incorporated in Hong Kong under number [insert company number] whose registered office is at [insert address] (the **Investor**)

[(each of the Company, the Managers and the Investor being a **Party** and together the Company, the Managers and the Investor are the **Parties**)].

RECITAL:²

The Investor has agreed to invest in the Company subject to and in accordance with the terms and conditions of this Agreement.

1 The registered company name, office and number of the Company, Newco 2, Newco 3 and the Investor should be inserted accordingly. If a company is trading under a name other than the registered company name, the words 'trading as [insert trading name]' may be inserted just after the relevant Party's address.

If a company is registered in a place other than Hong Kong, the words 'Hong Kong' should be replaced with the relevant country of registration (eg, 'China'). If a Party is a foreign entity consider inserting a provision setting out the procedure for service in Hong Kong.

Each of the managers should be detailed in Schedule 1, including their full names, addresses, fax numbers and email addresses.

2 Recitals are intended to explain the background of, and purpose to, the Agreement. They do not constitute substantive provisions, and are not binding unless they are specifically stated to be incorporated in the main body of the Agreement. They often state what is obvious from the title or from the first few clauses of an agreement, in which case the Parties may agree to omit them.

This Agreement has been prepared on the basis that the drafter is acting on behalf of the Investor and it has been assumed that:

- (a) there is a single investor;
- (b) there are a number of individual managers who will also be shareholders in the Company;

THE PARTIES AGREE:

1 Definitions and Interpretation³

- 1.1 In this Agreement, unless the context otherwise requires the following expressions shall have the following meanings:

A Ordinary Shares means the A ordinary shares of HK\$ [insert amount] each in the capital of the Company;

Accountants' Report means the accountants' report prepared by [insert name], a true copy of which comprises Annexure 1;

Annual Budget means the annual operating budget adopted under clause 6.3.1;

Articles means the proposed new articles of association of the Company in the approved terms to be adopted at Completion (as amended from time to time);

B Ordinary Shares means the B ordinary shares of HK\$ [insert amount] each in the capital of the Company;⁴

Board means the board of directors of the Company from time to time;

Business Day means a day, other than a Saturday, Sunday or public holiday, on which clearing banks are open for non-automated commercial business in Hong Kong;

(c) there are conditions to the investment and, as such, it has been drafted with split exchange and completion with rights in favour of the Investor to terminate the Agreement between exchange and completion;

(d) there is a triple newco structure appropriate for most leveraged buy-outs in order to achieve structural subordination of debt for banking purposes and to separate investor debt from equity for tax purposes;

(e) there are restrictions on the managers operating the business between the date of the Agreement and completion; and

(f) the Agreement is subject to the laws of Hong Kong.

Provisions for syndication of the investment by the Investor (see Investment agreement – syndication provision) can be used with this Agreement, which depending on the nature of the transaction:

3 The definitions and interpretation provisions in this clause apply throughout the whole of this Agreement. The drafter should consider whether it is simpler to put certain definitions at the beginning of the relevant clause, Schedule or paragraph if used only in that context.

4 *B Ordinary Shares*: These shares are subscribed for by Management. If there is to be a ratchet, the price at which they are subscribed should be at a premium calculated to take into account the value of the ratchet, otherwise an income tax and national insurance charge may be incurred.

Business Plan	means the business plan, a true copy of which comprises Annexure 2;
CO	means the New Companies Ordinance (Cap 622);
Completion	means completion of the matters described in this Agreement by the performance of the Parties of their respective obligations in accordance with clause 3;
Completion Date	means [<i>insert date</i>] 20[<i>insert year</i>] or such other date as the Parties agree in writing; ⁵
Conditions	means the Conditions set out in clause 2.1; and Condition means any one of them; ⁶
Confidential Information	means all data or information (whether technical, commercial, financial or of any other type) in any form acquired under, pursuant to or in connection with, this Agreement and any information used in or relating to the Business (including information relating to [the Company's][any Group Company's] products (bought, manufactured, produced, distributed or sold), services (bought or supplied), operations, processes, formulae, methods, plans, strategy, product information, know-how, design rights, trade secrets, market opportunities, customer lists, commercial relationships, marketing, sales materials and general business affairs), and which are for the time being confidential to the Company; ⁷
[Consequential Loss	means consequential, special, indirect, incidental or punitive damages or loss or any loss of profits or other form of economic loss however arising;] ⁸

5 *Completion Date*: If exchange and Completion occur on the same date, the definition should be amended to 'the date of this Agreement'. The date shown will be the same date as that on which completion is to occur under the Share Purchase Agreement.

6 *Conditions*: The Agreement includes a number of Conditions set out in clause 2.1 which must be satisfied before Completion. The drafter should consider whether there should be deemed repetition of the Warranties at Completion.

7 *Confidential Information*: This definition should include all information relevant to the Company and its business.

8 *Consequential Loss*: See Chapter 12, footnote 11, p 131.

Deed of Adherence	means the deed of adherence to this Agreement in the form of Schedule 5;
Disclosure Letter	means the letter dated the same date as this Agreement from the Warrantors to the Investor disclosing matters against the Warranties, together with its schedules and the documents attached to it; ⁹
Environmental Report	means the environmental report, a true copy of which comprises Annexure 4;
Exit	means a Sale or Quotation;
Financing Documents	means the facilities agreement to be entered into on the same date as this Agreement between [Newco 3] and [<i>insert name of bank</i>] together with the [<i>list other financing documents, such as security and intercreditor documentation</i>] in the agreed form, as amended, supplemented, novated or replaced from time to time;
Fund	means any bank, company, unit trust, investment trust, investment company, limited, general or other partnership, industrial provident or friendly society, any collective investment scheme, any investment professional, any high net worth company, unincorporated association or partnership or any high value trust (all as defined under the SFO), any pension fund or insurance company or any person who is an authorised person under the SFO;

9 *Disclosure Letter*: Normally the Warrantors will provide a disclosure letter to qualify the Warranties. The Agreement assumes that the Warrantors will address the letter to the Investor. The Disclosure Letter should not normally be addressed from the Managers' Solicitors to the Investor's Solicitors on its clients' behalf, as the Warranties are given by the Warrantors (who include the Managers) to the Investor in the Agreement. The Warranties themselves may require that certain documents are 'disclosed' and it is usual for such documentary evidence to be appended to (and form part of) the Disclosure Letter.

[Group] means the Company and each of its subsidiaries and **Group Company** means any of them;]

Investor Associate means: (a) each member of the Investor's Investor Group (other than the Investor itself); (b) any person who manages or advises any or all of the assets for the time being of the Investor or the family trusts of any of its executives for the purposes of any co-investment scheme; (c) any partner, general partner, nominee, trustee, custodian, operator, manager or adviser of the Investor or any member of the Investor Group; (d) any Fund, the assets of which are from time to time managed or advised (whether solely or jointly with others) by the Investor, manager or its successor or any member of the Investor Group; and (e) any Fund in respect of which the Investor or any member of the Investor Group is a general partner;¹⁰

Investor Consent means the giving of a written consent or direction by the [Investor or] holders of not less than [75]% in nominal value of the [A Ordinary Shares] [Investor Shares] in issue from time to time[, provided that for so long as there is an Investor Director, any such consent or direction required or permitted to be given under this Agreement shall be validly given if given by the Investor Director [or, if at any time there is more than one Investor Director, [each/a majority of the] Investor Director[s]], in the manner set out in clause 9];¹¹

Investor Director is defined in clause 5.5.1;

¹⁰ *Investor Associate*: The Investor will want this definition to be as wide as possible. It is relevant for the permitted transfer provisions in the Articles as well as clause 15.2 (Assignment).

¹¹ *Investor Consent*: If it reasonably contemplated that there is to be more than one Investor, then not only should syndication provisions be inserted, but also this percentage figure will need careful consideration.

Investor Group means, in relation to the Investor, the Investor and its [subsidiary undertakings] [wholly-owned subsidiaries] or, as the case may be, the Investor, any [parent undertaking, whether direct or indirect, of the Investor] [holding company of which the Investor is, directly or indirectly, a wholly-owned subsidiary] and any other [subsidiary undertaking] [wholly-owned subsidiary] of any such [parent undertaking] [holding company] from time to time and references to **member** or **members** of the **Investor Group** shall be construed accordingly;

Investor Shares means the shares to be subscribed by the Investor pursuant to clause 3.2.1;

Legal Due Diligence Report means the legal due diligence report, a true copy of which comprises Annexure 5;

[Loan Note Instrument] means the loan note instrument in the approved terms created by Newco 2 and executed at Completion;]

[Loan Notes] means the HK\$[insert amount] [insert rate]% [unsecured] loan notes 20[insert year] of Newco 2 to be constituted by the Loan Note Instrument and references to the **Loan Note** shall be construed accordingly;]

[Losses] means the questionnaires signed by the Managers and delivered to the Investor dated [insert date], a true copy of which comprises Annexure 6;]¹²

[Managers' Questionnaires] means all liabilities, costs, expenses (including legal expenses), claims, actions, proceedings, damages, fines, penalties, loss of profit [and Consequential Loss];]

Newcos means the Company, Newco 2 and Newco 3;

[Preference Shares] means the cumulative redeemable preference shares of HK\$ [insert amount], each in the capital of the Company;]

¹² *Losses*: Optional wording is provided to include Consequential Losses. Care must be taken if the definition incorporates Consequential Losses as this can be far-reaching.

Property Report	means the property report, a true copy of which comprises Annexure 3;
Quotation	means trading on the Stock Exchange of Hong Kong's market for listed securities or any other Recognised Stock Exchange;
Recognised Stock Exchange	means a recognised exchange, recognised overseas exchange, designated exchange or designated overseas exchange, in each case for the purposes of the SFO; ¹³
Sale	means the sale of the whole of the issued equity share capital of the Company to a single buyer or to one or more buyers as part of a single transaction;
Service Agreements	means the service agreements in the approved terms;
SFO	means the Securities and Futures Ordinance (Cap 571);
Share	means a share in the capital of the Company;
Shareholder	means any holder of any Share from time to time;
Share Purchase Agreement	means the agreement to be entered into on the same date as this Agreement and made between [<i>insert name</i>] and [Newco 3] relating to the acquisition of the entire issued share capital of the Target;
Target	means [<i>insert name</i>] Limited;
Target Group	means the Target and each of its subsidiary undertakings from time to time and references to Target Group Company shall be construed accordingly;
Warranties	means the warranties [and representations] set out in Schedule 3; ¹⁴
Warrantors	means the Managers [and the Company]; ¹⁵

13 *Recognised Stock Exchange*: The list of exchanges covered by this definition should be confirmed by the Investor.

14 *Warranties*: See Chapter 12, footnote 20, p 138.

15 *Warrantors*: The advantage for the Investor of joining the Company in the warranties is that, if the warranties are breached in circumstances which cause the Company to go into liquidation, the Investor will rank as an unsecured creditor to the extent of

Warranty Claim means a claim (for damages, compensation or any other relief) by the Investor under any Warranty in respect of any event, matter or circumstance which is inconsistent with, contrary to, or involves, relates to or is otherwise a breach of, any of the Warranties.

1.2 Unless the context otherwise requires:¹⁶

1.2.1 each gender includes the other;

1.2.2 the singular includes the plural and vice versa;

1.2.3 references to this Agreement include its Schedules and Appendices;

1.2.4 references to clauses, sub-clauses, Schedules and/or Appendices are to clauses and/or sub-clauses of and Schedules and/or Appendices to this Agreement and references in a Schedule or part of a Schedule are to a paragraph of that Schedule or that part of that Schedule;¹⁷

1.2.5 the word 'today' refers to the date of this Agreement;

1.2.6 references to persons include individuals, unincorporated bodies and partnerships (whether or not having a separate legal personality), governments, government entities, companies and corporations and any of their successors, permitted transferees or permitted assignees;

1.2.7 [the words '*insert words*' and '*insert words*' shall have the same meanings given to them by the [*insert the relevant legislation*]/words and phrases defined in [*insert any relevant legislation or documentation*] have the same meaning in this Agreement;]¹⁸

the warranty claim (as opposed to ranking as a shareholder) and will have a greater opportunity of retrieving its investment.

16 This clause sets out the interpretation provisions which apply to the Agreement. This adds to the existing legislation that applies to the construction and interpretation of expressions and words in deeds, contracts and other instruments.

17 This allows the drafter to refer to clauses, sub-clauses, Schedules and Appendices without using terms such as 'below', 'above' and 'hereof'.

18 The drafter should give consideration as to whether there is any specific legislation or other documentation which contains definitions that are applicable to this Agreement (ie, the CO or Inland Revenue Ordinance (Cap 112)). If so, this sub-clause can be