Practice Note 26 – Guidance Note on the application of the Codes on Takeovers and Mergers and Share Buy-backs relating to treasury shares

Purpose

1. Before 11 June 2024, listed issuers must cancel and destroy the documents of title of the repurchased shares under the Listing Rules. With effect from 11 June 2024, listed issuers may keep repurchased shares in treasury to the extent permitted under the applicable laws and regulations and their constitutional documents.

2. The purpose of this Practice Note is to provide guidance to offerors, offeree companies, their shareholders and market practitioners on the treatment of treasury shares under the Takeovers Code and the Share Buy-backs Code (collectively, the "**Codes**").

Background

3. Treasury shares are shares that an issuer holds in treasury after a buy-back. Holding treasury shares provides the issuer with more flexibility in managing its equity capital as this enables the issuer to raise funds, grant share awards or discharge its obligations under convertible securities without the need to issue new shares.

4. Treasury shares are not part of an issuer's outstanding share capital. Normally, their voting rights are suspended by law unless and until they are transferred out of treasury.

Treatment of treasury shares under the Codes

5. For the purpose of the Codes, treasury shares are either shares that are bought back and held by an issuer directly or the issuer's shares that are held by its subsidiary, agent or nominee on behalf of the issuer or its subsidiary, as permitted under the applicable laws, rules and regulations and constitutional documents. For the avoidance of doubt, treasury shares include shares bought back by an issuer and held on its behalf by HKSCC Nominees Limited in CCASS.

Overview

6. The treatment of treasury shares under the Codes is not affected by the introduction of the treasury shares regime under the Listing Rules. In general, treasury shares are disregarded for the purpose of determining whether a mandatory general offer is required or whether a voting, approval or acceptance threshold is met[1]. This remains the case unless and until

[1] For the avoidance of doubt, if a share buy-back results in a shareholder's proportionate interest in the voting rights of an issuer exceeding the relevant thresholds under the Codes, a mandatory general offer obligation will normally be triggered unless such shareholder is

treasury shares are resold or otherwise transferred out of treasury. For transparency, an issuer[2] should specify the number of issued shares that are held in treasury when disclosing[3] its issued share capital. A company proposing to buy back shares under the Share Buy-backs Code should specify in the relevant announcement and shareholders' document whether it intends to hold the repurchased shares in treasury and whether any voting rights attached to the treasury shares will be suspended.

7. Paragraphs 8 to 19 below elaborate how the key provisions of the Codes apply to treasury shares.

Requirements on voting, offer and acceptance

8. The note to the definition of "voting rights" expressly stipulates that the voting rights attached to treasury shares (if any) will not be treated as voting rights under the Codes.

9. Therefore, treasury shares are excluded from the voting rights or approval percentage calculation for the purpose of the mandatory general offer[4] provisions (including the 30% trigger and 2% creeper) and other relevant Codes requirements (e.g. those relating to acceptance conditions[5], whitewash waivers, special deals and frustrating actions and related disclosures[6]).

10. In addition, as treasury shares are held by, or on behalf of, an issuer or its subsidiary, they are not considered part of an issuer's outstanding equity or non-equity share capital. Where an offer is being made for the securities of an issuer, such offer does not need to extend to treasury shares.

11. Accordingly, treasury shares are not considered "disinterested shares" as referred to in the voting or acceptance percentage requirements under Rules 2.2, 2.10 or 2.11 of the Takeovers Code. Similarly, neither an issuer nor its nominees holding the issuer's treasury shares is regarded as a "disinterested shareholder" under Rule 2 of the Share Buy-backs Code.

12. Voting rights attached to treasury shares are normally suspended by law, and are so treated under the Codes. Where a transaction is subject to

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neither a director of the repurchasing company nor a party acting in concert with any of such directors. The position is the same regardless of whether the repurchased shares are cancelled or kept in treasury as treasury shares.

2 References to "issuer" in this Practice Note may be an offeror or an offeree company depending on the circumstances to which the guidance given in this note relates.

3 For example, the disclosure requirements under paragraph 19 of Schedule I, paragraph 3 of Schedule II and paragraph 22 of Schedule III to the Codes.

4 For the avoidance of doubt, in case of a share buy-back by an issuer or its nominees, the repurchasing company will not be regarded as having acquired voting rights for the purposes of Rule 26 of the Takeovers Code.

5 Under Rules 26.2 and 30.2 of the Takeovers Code.

6 For example, Rule 19.1 of the Takeovers Code requires offer results announcements to set out the percentages of voting rights represented by different classes of share capital. Treasury shares should be excluded from the calculation of the relevant voting right percentages.

shareholders' approval under the Codes, an issuer should confirm in the voting results announcement that no votes cast in favour of or against the transaction include any votes relating to treasury shares, regardless of whether the shares are held by the issuer or its nominees (e.g. CCASS) on the issuer's behalf. Whether the approval threshold required under the Codes is met must be determined by reference to the number of issued shares of the relevant issuer excluding treasury shares (if any).

Disclosures on dealings in "relevant securities"

13. In determining whether a person owns or controls 5% or above of any class of "relevant securities" of an issuer, and is therefore required to disclose its dealings under Rule 22 of the Takeovers Code as a class (6) "associate", it shall refer to the number of the issuer's outstanding issued shares (excluding treasury shares) in the calculation of its shareholding percentage.

14. To assist relevant parties in their compliance with dealing disclosure requirements under Rule 22, Rule 3.8 of the Takeovers Code provides that when an offer period commences, the offeree company must announce details of all its relevant securities together with the number of such securities in issue. Where an issuer has treasury shares, the Executive expects the announcement to specify[7] (i) the issuer's total number of issued shares excluding treasury shares; and (ii) the number of treasury shares held by the issuer. In addition, the issuer is required to announce as soon as possible any changes to its issued share capital during the offer period, including changes in the number of treasury shares.

Requirements on distribution and issue of shares

15. Resale of treasury shares or transfer of such shares out of treasury will result in an increase in an issuer's outstanding share capital and are treated in the same manner as the issue or distribution of shares for the purposes of the Codes.

16. The disclosure requirements for the issue of new shares under paragraph 21 of Schedule I, paragraph 4 of Schedule II and paragraph 22 of Schedule III to the Codes apply equally to the resale of treasury shares or the transfer of such shares out of treasury.

17. Similarly, any transfer of the repurchased shares out of treasury (including resale of treasury shares) is subject to the requirements concerning issue or distribution of shares under Rule 4 of the Takeovers Code and Rule 7 of the Share Buy-backs Code.

18. Therefore, once a bona fide offer has been communicated to the board of an offeree company or its board has reason to believe that a bona fide offer

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[7] For the avoidance of doubt, the announcement is also expected to disclose the issuer's total number of issued shares.

may be imminent, the board must not, without the approval of the offeree company's shareholders or the offeror's consent, issue any shares or resell any treasury shares or transfer any shares out of treasury (e.g. use the treasury shares as share awards) unless these actions are carried out pursuant to prior contractual obligations.

19. In addition, as soon as an issuer announces a non-exempt share buy-back, it shall not announce or engage in any issue or distribution of shares, resale of treasury shares or transfer of shares out of treasury until after the 31st day immediately following the completion or withdrawal of the buy-back.

20. In case of doubt about the treatment of treasury shares under the Codes or any part of this Practice Note, the Executive should be consulted at the earliest opportunity.

24 May 2024