

Practice Note 2 (PN 2) – Issues relating to profit forecasts under Rule 10

Rule 10 of the Takeovers Code governs the treatment of profit forecasts and other financial information in the context of an offer or a possible offer. Where a document to shareholders includes information that constitutes a profit forecast under Rule 10 of the Takeovers Code, then, the party issuing the forecast must obtain and publish an accountant's report and financial adviser's report on the forecast in accordance with Rule 10.4. Rule 10.4 further provides that when a forecast is made in an announcement, that announcement must contain a statement that the forecast has been reported on in accordance with the Takeovers Code and the reports have been lodged with the Executive. If a company's forecast is published first in an announcement, it must be repeated in full, together with the reports, in the next document sent to shareholders by that company ("Shareholder's Document").

The purpose of this Practice Note is to clarify (i) the meaning of "reporting on" under Rule 10 of the Takeovers Code, (ii) the circumstances where Rule 10.4 may be relaxed; and (iii) the application of Rule 10.9 to unaudited quarterly results published by companies with dual listings.

I. Meaning of "reporting on" under Rule 10 of the Takeovers Code

Rule 10.1 and Note 1(c) to Rules 10.1 and 10.2 and Rule 10.4 of the Takeovers Code are relevant.

Reporting on a profit forecast involves (i) the financial advisers reviewing and discussing the assumptions with their client in order to satisfy themselves that the forecast has been made with due care and consideration; and (ii) the auditors or accountants satisfying themselves that the forecast, so far as the accounting policies and calculations are concerned, has been properly compiled on the basis of the assumptions made. Financial advisers and the auditors/accountants are not normally required to provide written confirmations to the Executive in relation to the above matters. In both cases it is normally sufficient for the relevant written confirmations, which form part of the report referred to in Rule 10.4 of the Takeovers Code, to be published in the document addressed to shareholders containing the profit

forecast. If the profit forecast is made in an announcement, then the reports must be lodged with the Executive before the announcement is published and such reports must be published in the next document issued by the company to shareholders Shareholder's Document.

There may be occasions, particularly when an estimate relates to a period already ended, when no assumptions are required as provided under Note 2(c) to Rules 10.1 and 10.2 of the Takeovers Code. For the avoidance of doubt, an estimate of profit for a period which has already expired should be treated as a profit forecast under Rule 10.6 (b). In these circumstances, instead of reviewing the assumptions, the financial advisers and auditors ~~/ or~~ accountants should review and report on the bases of the profit estimates.

II. Circumstances where Relaxation of Rule 10.4 of the Takeovers Code may be relaxed

- (a) ~~Financial projections published under the laws and regulations of an overseas jurisdiction~~

~~During the course of a Code-related transaction, an offeree company (or an offeror in the case of a securities exchange offer) may be required under the laws and regulations of an overseas jurisdiction to include certain financial projections in documents that are sent to shareholders containing details of the transaction.~~

~~II. Such financial projections would normally be regarded as profit forecasts under Rule 10 of the Takeovers Code and would therefore need to be 'reported on' by both the offeree company's financial advisers and its accountants or auditors in accordance with Rule 10.4.~~

~~Notwithstanding this if~~ if the only reason for publishing the profit forecasts ~~forecast~~ is that it is required by the laws and regulations of certain overseas jurisdiction ~~to which an offeror or offeree company is subject~~ (and is not otherwise proposed to be published by the offeror or offeree company) and the parties have encountered genuine practical difficulties (time-wise or otherwise) in meeting the reporting requirements set out in Rule 10.4, the Executive will normally be prepared to permit publication of the forecasts ~~forecast~~ in an announcement without full compliance with Rule 10. In this instance, the announcement containing the profit

~~forecasts~~forecast must be accompanied by an appropriate warning that ~~they do it~~ does not meet the standard required by Rule 10 and that shareholders and potential investors should exercise caution in placing reliance on ~~such forecasts~~ the forecast in assessing the merits and demerits of the transaction. The Executive will also normally require the ~~forecasts~~ forecast to be reported on as soon as reasonably practicable and the relevant reports to be contained in the next ~~document to be sent to shareholders~~ Shareholder's Document. This may require the ~~issue~~ issuance of a supplemental document to shareholders if an offer document, response document or whitewash ~~document~~ circular has already been sent out. In determining what constitutes "practical difficulties", the Executive will take into account the specific facts and circumstances of each case. In cases of doubt the Executive should be consulted at the earliest opportunity.

The Executive will normally relax the requirements of Rule 10.4 in the following circumstances:

- (b) Financial projections published under the laws and regulations of an overseas jurisdiction

During the course of a Code-related transaction, an offeree company (or an offeror in the case of a securities exchange offer) may be required under the laws and regulations of an overseas jurisdiction to include certain financial projections in announcements containing details of the transaction. Such financial projections would normally be regarded as profit forecasts under Rule 10 of the Takeovers Code and are normally required to be 'reported on' by both the offeree company's financial advisers and its accountants or auditors in accordance with Rule 10.4. The Executive normally is prepared to relax the strict application of Rule 10.4 to the announcement but will require compliance with the requirements of Rule 10.4 in the next Shareholder's Document.

- (c) Profit warning warnings or positive profit alert ~~announcements~~ alerts

During an offer period an offeree company may ~~see the need to~~ issue a profit warning or positive profit alert announcement

pursuant to the Listing Rules and the inside information provisions under Part XIVA of the Securities and Futures Ordinance which took effect from 1 January 2013. The profit warning or positive profit alert ~~announcements~~announcement would normally be regarded as a profit forecast~~forecasts~~ under Rule 10 of the Takeovers Code and ~~would therefore need~~is normally required to be 'reported on' by both the offeree company's financial advisers and its accountants or auditors in accordance with Rule 10.4. This would also be relevant to an offeror in a securities exchange offer.

Often profit warning or positive profit alert announcements are issued almost immediately after the directors of the listed issuer come into possession of the relevant inside information. Given the time constraints faced by listed issuers when issuing these announcements, the Executive ~~adopts a similar approach as described in subparagraph (a) above. In all cases involving this issue the~~will normally permit the relaxation of Rule 10.4. The Executive should be consulted at the earliest opportunity in such cases.

Normally, the requirement to include the Rule 10 reports in the next Shareholder's Document under this paragraph will no longer apply if the quarterly, interim or annual results to which the profit warning or profit alert relates have been announced and the relevant results together with the notes to the financial statements are included in the Shareholder's Document. This is because the published financial results will fall within the ambit of Rule 10.9 of the Takeovers Code.

(c) Notifiable transaction announcements

Where a listed issuer enters into a Code-related transaction which is also classified as a notifiable transaction under the Listing Rules, Listing Rule 14.58 requires the disclosure of the net asset value of, and net profits or losses attributable to, the assets acquired or disposed of for the two financial years immediately preceding the transaction ("Required Financial Information") in the announcement that contains details of the transaction. Listing Rule 14.58 does not require the Required Financial Information to be audited.

In a Code-related transaction, the Required Financial Information, if unaudited and disclosed in an announcement, constitutes a profit forecast under Rule 10 and normally would be required to be reported on by both the offeree company's financial advisers and its accountants or auditors in accordance with Rule 10.4. In order to facilitate timely disclosure of the Required Financial Information, the Executive is prepared to relax the strict application of Rule 10.4 to such an announcement. However, compliance with the requirements of Rule 10.4 in the next Shareholder's Document is still required.

III. Unaudited quarterly results published by companies with dual listings

Companies with dual listings of their shares may publish unaudited quarterly results pursuant to a requirement under the relevant laws or regulations of the overseas jurisdiction during an offer period.

Rule 10.9 requires any unaudited profit figures published during an offer period to be reported on except with the consent of the Executive or in the following instances:

- (i) unaudited statements of annual or interim results which have already been published;
- (ii) unaudited statements of annual results which comply with the requirements for preliminary profits statements as set out in the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules");
- (iii) unaudited statements of interim results which comply with the requirements for half-yearly reports as set out in the Listing Rules in cases where the board of the offeree company has not publicly advised its shareholders not to accept an offer;
- (iv) unaudited statements of interim results by offeror which comply with the requirements for half-yearly reports as set out in the Listing Rules, whether or not the offer has been publicly recommended by the board of the offeree company but provided the offer could not result in the issue of

securities which would represent 10% or more of the enlarged voting share capital of the offeror

The Note to Rule 10.9 extends the exemptions from the reporting requirements to unaudited quarterly results of companies listed on the Growth Enterprise Market of the Stock Exchange (“GEM”).

The exemptions for companies listed on The Stock Exchange of Hong Kong Limited (“Stock Exchange”), either on the Main Board or GEM, from the reporting requirements contained in Rule 10.9 are appropriate as:

- (i) the relevant unaudited interim and quarterly figures and preliminary announcements of results are required to be published and prepared to the standards required by the respective applicable Listing Rules¹; and
- (ii) the unaudited figures must be included in a full-year audit in due course.

The Executive believes that if a company has a dual listing and is required by the relevant laws or regulations of the overseas jurisdiction to publish unaudited quarterly results the exemption from the reporting requirements in Rule 10.9 should also apply.

In relevant cases where a company with a dual listing wishes to take advantage of the exemptions from the reporting requirements in Rule 10.9 the Executive must be consulted at the earliest opportunity. Where appropriate the Executive may require the relevant party to apply for a formal ruling under section 8 of the Introduction to the Codes.

Rule 10.9 also provides that the Executive should be consulted in advance if a company is not listed on the Stock Exchange but wishes to take advantage of the exemptions under this Rule.

~~30 September 2013~~ 31 March 2015

¹ See Appendix 16 to the Main Board Listing Rules and Chapter 18 of the GEM Board Listing Rules.