HKEx Announces Consultation Conclusion for New Treasury Shares Rules

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If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last page or call your regular Skadden contact.

In its conclusions to a market consultation process held in late 2023, the Stock Exchange of Hong Kong Limited (HKEx) has announced it will permit listed companies to hold their own shares as treasury shares and introduced rules for companies' resale of treasury shares. The new rules will be effective on 11 June 2024.

Please refer to our publication "HKEx To Permit Treasury Shares" for further details of the consultation.

Treasury Shares To Be Permitted

Historically, the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the Listing Rules) have not allowed listed companies to retain treasury shares and have required any repurchased shares to be cancelled. HKEx has now announced it will abolish the requirement to cancel repurchased shares. As a result, listed companies may hold repurchased shares in treasury for future resale, if permitted under the laws of their places of incorporation. Many of the most popular jurisdictions of incorporation for HKEx-listed companies, such as the Cayman Islands and Bermuda, permit treasury shares.

If a company's existing articles of association prohibit the company from holding treasury shares, the company will be required to obtain shareholders' approval to amend its articles of association before it can take advantage of this new treasury share regime.

Share repurchases will continue to be conducted under existing rules pursuant to a share repurchase mandate obtained from shareholders, which permits a company to repurchase up to 10% of its shares on-market in any 12-month period. The company must disclose in the related explanatory statement to shareholders (sent at the time of convening the shareholder meeting to obtain the mandate) whether the company intends to cancel repurchased shares or retain them as treasury shares. The company may also state that it may cancel any repurchased shares and/or hold them as treasury shares subject to, for example, market conditions and its capital management needs at the relevant time of the repurchases[1]. The company's next-day filing to report returns after repurchasing shares must disclose (i) whether the company will cancel or hold the repurchased shares in treasury; and (ii) where applicable, the reasons for any deviation from the intention statement previously disclosed.

Resales or Transfers of Treasury Shares

The rules applicable to the issuance and sales of new shares will also govern resales of treasury shares.

- Resales of treasury shares will be subject to preemptive rights (*i.e.,* offered to all shareholders on a pro rata basis) or conducted under a shareholders' mandate, which may be either a general mandate or specific mandate.
  - Most listed companies in Hong Kong obtain a general mandate from shareholders to issue new shares representing up to 20% of the company's issued share capital in any 12-month period.
  - In addition, this general mandate is increased by the number of shares repurchased in a year (up to the 10% share repurchase mandate limit), so resales of treasury shares will count in fulfilling these mandate limits.

[1] FAQ 159-2024.

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  - Note that the general mandate is required to specifically authorize the resale of treasury shares.[2] Therefore, companies intending to retain and resell treasury shares will need to amend the wording of their customary general mandate resolutions to take advantage of the new rules.
- Resales of treasury shares under general mandate (whether on-market or off-market) will be subject to a maximum price discount of 20%, similar to placings of new shares under a general mandate.

New listing applicants will be permitted to retain their treasury shares upon listing. The listing prospectus must disclose details of the treasury shares. The existing six-month moratorium on issuances of new shares after listing will also apply to resales of treasury shares.

Companies can use treasury shares to satisfy award grants under share schemes, in which case such grants will be treated as share awards funded by new shares and subject to the overall share scheme limits. Scheme rules must be amended to allow the use of treasury shares to satisfy award grants. HKEx has indicated the exchange will not regard such amendments as a material alteration to the scheme rules, so shareholder approval will not be required to make these amendments.[3]

Restrictions on Treasury Shares and Resales

There will be no restrictions on the actual number of treasury shares that a company may hold.

Treasury shares may not be voted and will be disregarded in calculations of total outstanding shares for the purposes of the Listing Rules (*e.g.*, in calculating public float, market capitalization, mandate limits, size tests for notifiable transactions or connected transactions, as well as when determining the percentage of rights of a controlling shareholder, substantial shareholder and weighted voting rights (WVR) beneficiary (if any) to vote at a general meeting).

HKEx explicitly discourages companies from repeatedly repurchasing and reselling their own shares on the market with the intention of manipulating the share price or making a trading profit. To guard against market manipulation, the following limitations will apply:

- The existing moratorium on issuing new shares within 30 days after any share repurchase will also apply to resales of treasury shares, so companies may not resell any treasury shares within 30 days after a share repurchase.
  - However, the rules provide a carve-out for (i) capitalization issues, (ii) share grants under a share scheme that complies with Chapter 17 and (iii) any issuance of new shares or transfer of treasury shares upon vesting or exercise of share awards or options under the share scheme.
- Conversely, companies also may not undertake an on-market share repurchase within 30 days after any resale of treasury shares.
- The existing restriction on undertaking share repurchases while there is undisclosed inside information or during the 30-day period preceding any results announcement will also apply to resales of treasury shares.
- Companies may not knowingly sell treasury shares on-market to a core connected person.
  - On-market sales of treasury shares to a connected person without knowledge will be fully exempt from the connected transaction rules.
  - Sales of treasury shares off-market to connected persons will be subject to the usual connected transaction rules.

Arrangements To Hold or Transfer Treasury Shares

A listed issuer intending to resell treasury shares on HKEx may hold or deposit such shares with the Central Clearing and Settlement System (CCASS), registered under the name of HKSCC Nominees Limited as a common nominee. To facilitate the identification of treasury shares when they are held with CCASS, the issuer is expected to hold or deposit its treasury shares in a segregated account in CCASS. The issuer should also instruct the relevant broker to maintain a proper record of these treasury shares.

If the laws of an issuer's place of incorporation require repurchased shares to be held in the issuer's own name in order to be classified as treasury shares, the issuer should, upon completion of the share repurchase, withdraw the repurchased shares from CCASS and register the repurchased shares in the issuer's register of members in the company's own name as treasury shares. The issuer may redeposit its treasury shares into CCASS only if it has an imminent plan to resell them on HKEx, and the issuer should complete the resale as soon as possible.

Shareholders' rights attached to treasury shares (such as voting, dividend and distribution) should be suspended either through the statutory requirements of an issuer's place of incorporation or by the company imposing appropriate measures (*e.g.*, (i) the company should ensure its broker does not give instructions to Hong Kong

[2] FAQ 161-2024.

[3] FAQ 162-2024.

Securities Clearing Company Limited to vote at general meetings for the treasury shares deposited with CCASS; and (ii) in the case of dividends or distributions, the company should withdraw the treasury shares from CCASS and either re-register them in its own name as treasury shares or cancel them, in each case before the record date for the dividends or distributions).

The issuer should disclose the following:

- **In any explanatory statement for share repurchase mandate:** the interim measures the company adopted if it may hold treasury shares in CCASS for resale on HKEx.
- **In any poll results announcement:** the number of treasury shares (including any treasury shares held or deposited with CCASS) that have been excluded from the total number of issued shares entitling holders to attend and vote on the resolution(s) proposed at the general meeting.
- **In any announcement relating to the declaration of dividends or distributions:** (i) the number of treasury shares (including any treasury shares held or deposited with CCASS); (ii) that such treasury shares will not receive the dividends or distributions; and (iii) where the issuer is incorporated in a jurisdiction requiring treasury shares to be held in its own name, a statement that the issuer will withdraw all repurchased shares (if any) from CCASS and either re-register them in its own name as treasury shares or cancel such repurchased shares, in each case before the record date for the dividends or distributions.

Implications Under the Takeovers Code and SFO

The introduction of the treasury share regime under the Listing Rules is not expected to result in significant changes to the existing practices for takeovers and share buybacks. The Securities and Futures Commission (SFC) will issue a practice note clarifying the treatment and implications of treasury shares in the context of a Takeovers Code-related transaction when the regime comes into effect.

Treasury shares will remain part of a listed issuer's issued shares for the purposes of the disclosure-of-interests regime under Part XV of the Securities and Futures Ordinance (SFO), so shareholding interest percentages will need to be calculated accordingly. The SFC will update its "Outline of Part XV of the SFO – Disclosure of Interests" to provide further guidance on the treatment of treasury shares, including the calculation of percentage interests if treasury shares are involved.

Waivers

HKEx has in recent years granted waivers to a number of overseas companies listing in Hong Kong on a case-by-case basis, permitting them to hold treasury shares. Transitional arrangements require these issuers to comply with the new Listing Rules requirements in relation to treasury shares by an issuer's second annual general meeting after the effective date of the new rule amendments.

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