China

Carl B. Cheng

Freshfields Bruckhaus Deringer LLP

Miles Ma

1 Relevant Authorities and Legislation

1.1 What regulates M&A?

Public M&A in the People's Republic of China (the PRC) is regulated by a number of government entities, including the State Council, the Ministry of Commerce (MOFCOM) (where foreign investment is involved), the China Securities Regulatory Commission (CSRC), the State Administration for Industry and Commerce (SAIC), the State Administration of Foreign Exchange (SAFE) and the State-owned Assets Supervision and Administration Commission (SASAC). Sector-specific industry regulators are also involved, such as the China Insurance Regulatory Commission and the China Banking Regulatory Commission (CBRC), which set out certain qualification and approval requirements for substantial shareholders of financial institutions.

The primary legislation underpinning M&A involving public companies is the Company Law and the Securities Law, both of which were revised as of 2006. The Securities Law contains detailed provisions regarding the issuing and trading of shares, corporate bonds and other securities recognised by the State Council; areas not covered by the Securities Law are picked up by its catch-all Article 2 which stipulates that 'other laws and administrative regulations shall apply to issues not covered by this Law'. Of these 'other laws', the Administrative Rules on Takeovers of Listed Companies (the Takeover Rules) and the Administrative Measures on Strategic Investment in Listed Companies by Foreign Investors (the Strategic Investment Rules) are most significant.

The Takeover Rules apply to all investors seeking to invest in public companies, as well as the acquisition of a domestic company which may have a subsidiary listed on a Chinese stock exchange.

The Strategic Investment Rules are designed to allow foreign investors to acquire, in certain circumstances, domestic RMB-denominated shares listed on the Shanghai or Shenzhen stock exchanges (known as 'A' shares).

The Regulations Concerning Mergers with and Acquisitions of Domestic Enterprises by Foreign Investors (Amended 2006) (the M&A Regulations) is the primary piece of legislation that governs the acquisition of PRC domestic enterprises by foreign investors. The M&A Regulations are applicable for the acquisitions of listed and non-listed companies in the PRC by foreign investors. Equity acquisitions where the target is a foreign invested enterprise, rather than a purely domestic PRC company, are governed by the Several Rules on Changes in Equity Interest of Investors in Foreign Invested Enterprises.

Also relevant to M&A transactions in the PRC are the Anti-Monopoly Law of the PRC (the AML), which became effective as of 1 August 2008, and its supporting regulations. The Rules on Notification Standards for Concentrations of Undertakings (the Merger Control Notification Thresholds) released by the State Council on 3 August 2008 specify the threshold standards triggering the requirement for notification to the enforcement authority. The Anti-Monopoly Enforcement Authorities designated by the State Council are responsible for the actual enforcement of the AML, while the Anti-Monopoly Commission established under the AML is in charge of organising, coordinating and supervising AML-related work. For further details on the AML, see question 10 below.

1.2 Are there different rules for different types of public company?

Public companies are not divided into different types as such, although in practice public companies can be analysed in terms of the different types of shares they issue. Traditionally, the majority of shares in PRC public companies were unlisted 'stated-owned' or 'legal person' shares owned by government or government-affiliated entities. Chinese stock markets view the existence of a controlling shareholder as normal, for example, in the context of an initial public offering where a state-owned enterprise floats 25% of its shares to the public while the state retains the remaining 75%. At one point an estimated two-thirds of equity in PRC public companies was unlisted. To accelerate the privatisation of China's state-owned assets, a process known as the 'share reform' was initiated in 2005, under which these shares are currently being converted into listed shares. There are several different types of shares in PRC listed companies, distinguished by their listing status and the extent to which foreign investment is possible:

(i) 'A' shares are denominated and traded in RMB. 'A' shares have traditionally not been open to foreign investors, but now foreign investors can acquire 'A' shares by qualifying as either a 'Qualified Foreign Institutional Investor' (QFII) or a 'strategic foreign investor'. The percentage of shares held by a single QFII in any one listed company may not exceed 10% of the listed company's total issued shares. QFII status is available to large financial institutions upon approvals by CSRC (for QFII qualification) and SAFE (for investment quota). Strategic foreign investors (see question 1.3) can purchase 'A' shares of companies which have undergone or were listed after the share reform process initiated in 2005. 'A' shares acquired by foreign strategic investors are subject to a three-year lock-up period from the date of the purchase;

(ii) 'B' shares are foreign-invested listed shares, traded and denominated in US Dollars (on the Shanghai exchange) and Hong Kong Dollars (on the Shenzhen exchange). There are no restrictions on foreign investors acquiring 'B' shares. Only a limited portion of a PRC company's share capital is listed in the form of 'B' shares;

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(iii) 'C' shares (named as a matter of alphabetical convenience) are state-owned shares and legal person shares that are not listed and are not tradable on the PRC domestic stock exchanges. Foreign investors can acquire 'C' shares by agreement subject to a process of public bidding. The purchase of 'C' shares is required to comply with applicable securities regulations including those on takeovers and disclosure of information. A formal state-owned assets valuation may also be required under SASAC rules designed to ensure that state-owned assets are not sold below market value. A lock-up period of 12-months applies to the acquisition of 'C' shares running from the date of acquisition. Under the share reform process, 'C' shares are being converted into 'A' shares. The vast majority of listed companies have either completed or started the process of share reform, and 'C' shares will gradually become less significant;

(iv) 'G' shares (from the Chinese *gai ge*, meaning 'reform') are 'C' shares which have been converted into 'A' shares pursuant to the share reform. 'G' shares are treated exactly the same as 'A' shares with the exception that 'G' shares are subject to restrictions on sale for up to three years after conversion. For 'G' shareholders other than strategic foreign investors, there is an initial lock-up period of one year after the shares are converted into 'A' shares. Thereafter, 'G' shareholders holding 5% or more of the total equity of the company may not sell more than 5% of the total equity in the company in the first year following the lock-up, and may not sell more than 5% of the total equity in the company in the second year following the lock-up. Strategic foreign investors are subject to a three-year lock-up period from the date of purchase of 'G' shares. Foreign investors can invest in 'G' shares by qualifying as a QFII or strategic foreign investor;

(v) 'H' shares are shares of PRC companies listed on the Hong Kong Stock Exchange and subscribed for and traded in Hong Kong dollars, and may only be purchased by persons or entities from outside mainland China. 'H' shares are governed by applicable Hong Kong regulations and are open to foreign investment;

(vi) 'Red Chip' shares initially refer to shares of companies incorporated outside of the PRC which have a substantial portion of their business interest in mainland China and are listed on the Hong Kong Stock Exchange, and denominated and traded in Hong Kong Dollars. Subsequently, this term has also been used to describe shares of non-PRC companies which have a substantial portion of their business interest in mainland China and are listed on overseas exchanges (such as the Singapore Stock Exchange) and denominated and traded in foreign currencies (such as the Singapore dollars); and

(vii) shares of PRC companies listed on overseas exchanges are commonly referred to as 'N' shares (New York), 'T' shares (Tokyo), 'L' shares (London), 'S' shares (Singapore), etc.

1.3 Are there special rules for foreign buyers?

Key to the foreign investment regime in the PRC is the Catalogue for the Guidance of Foreign Investment in Industries (the Catalogue) jointly promulgated and revised by the National Development and Reform Commission (NDRC) and MOFCOM from time to time. The Catalogue classifies industries as encouraged, restricted, or prohibited for foreign investment. Industries not listed are simply 'permitted'. In certain sectors, the Catalogue places specific caps on the proportion of shares that can be held by foreign investors. Foreign buyers may not purchase shares at all in companies engaged in industries in the 'prohibited' category, while investments in the 'restricted' category are subject to more stringent approval processes.

Subject to the sectoral restrictions set out in the Catalogue, the Strategic Investment Rules permit 'strategic foreign investors' to purchase 'G' shares, 'A' shares of companies which have undergone the share reform, and 'A' shares of companies which were listed after the share reform. Strategic foreign investors, as with all foreign investors, can also purchase shares that are open to foreign investment, such as 'B' shares, 'H' shares, and shares listed on overseas exchanges. To qualify as a strategic foreign investor, a foreign investor must demonstrate that it (i) has overseas assets of US$100 million or more or manages overseas assets of $500 million or more; (ii) has stable finances, good credit, and sound management; and (iii) has a 'strategic reason' for making the investment, meaning some justification other than mere speculation. The Strategic Investment Rules are designed to encourage medium to long-term strategic investments and therefore require a minimum initial investment of 10% of the total issued shares of the company, and a lock-up period of three years. Approvals and registrations are also required from MOFCOM, CSRC and SAFE, among others.

Restrictions apply to the size of interests that QFIIs may acquire in the 'A' shares of listed companies, as follows:

(i) the percentage of shares held by a single QFII in any one listed company may not exceed 10% of the listed company's total issued shares; and

(ii) the aggregate percentage of shares held by all QFIIs in any one listed company may not exceed 20% of the listed company's total issued shares.

The Shanghai and Shenzhen Stock Exchanges may require QFIIs to sell down their shares if any of the above limits are exceeded. The Exchanges will make public announcements when the investment by QFIIs in a listed company exceeds 16%.

Foreign buyers should also be alert to ad-hoc policies that may be issued by the State Council, the NDRC and MOFCOM from time to time that restrict foreign ownership in certain sectors.

In respect of private M&A, the M&A Regulations set out the rules with which a foreign investor must comply with, including the approvals that must be obtained, should it wish to invest in a domestic company, thereby converting it into a foreign invested enterprise.

1.4 Are there any special sector-related rules?

The Catalogue places specific caps on the proportion of shares that can be held by foreign investors in certain sectors. See question 1.3.

1.5 What are the principal sources of liability?

Under the Securities Law, in making a public acquisition or disposal, 'informed persons with insider information on securities trading' and 'persons who have unlawfully obtained insider information' are prohibited from using such information to trade in securities; disclosing such information; or making recommendations to third parties to buy or sell securities. The Securities Law also prohibits various types of activities that have the effect of manipulating the securities market.

A person who is involved in market manipulation or insider dealing, including recommending others to do so, can be ordered to dispose of the relevant securities, is liable to have any gains confiscated and be fined up to five times the gain. A person that commits an act of market manipulation or insider dealing that causes other investors to suffer a loss can be liable in damages to those investors.

In the context of private M&A, failure to obtain approval from MOFCOM and other relevant authorities in accordance with the M&A Regulations may result in the transaction being revoked retrospectively.

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Non-compliance with the AML and supporting rules may result in the transaction being unwound and subject the parties involved to significant fines.

2 Mechanics of Acquisition

2.1 What alternative means of acquisition are there?

There are a number of methods of acquisition of public companies available to foreigners pursuant to the Takeover Rules and the Strategic Investment Rules, including:

(i) private placement, where strategic foreign investors subscribe for newly issued shares;

(ii) acquisition by agreement, where the acquirer purchases shares from the target's parent company or other shareholders. This would include acquisitions of 'C' shares, where applicable;

(iii) acquisition by offer, under which the bidder makes either a general or partial offer to the target's shareholders. Partial offers must be for at least 5% of the issued shares.

Regardless of which method an acquirer adopts, if an acquirer's shareholding in the public target reaches 30% (including any aggregate shareholdings with concert parties), it is obliged to make a general or partial offer to all the shareholders of the target and generally may not acquire further shares by any means other than acquisition by offer. However, a no less than 30% shareholder of a listed company may apply to the CSRC for an offer exemption within three days after it acquires shares in the target at less than 2% every 12 months after it reaches 30%.

2.2 What advisers do the parties need?

For all three acquisition methods outlined in question 2.1, the parties generally retain financial and legal advisers and accountants.

For private placements, a sponsor must also be engaged by the company to prepare and submit to CSRC the application documents for the issuance of new shares under the private placement.

As for acquisitions by offer, the bidder must retain a CSRC-approved financial adviser registered in the PRC. The bidder must also appoint a PRC-registered securities company to apply to a securities registration and clearing organisation to make necessary arrangements for custody of shares during a pre-acceptance period. The board of directors of the target is required to retain an independent financial adviser to provide an independent professional opinion on the acquisition which will be annexed to the 'Report of the Board of Directors of the Target Company' to be submitted to the CSRC and the relevant stock exchange.

2.3 How long does it take?

For acquisitions by private placement where the acquirer is a foreigner, preliminary approval from MOFCOM can take several months to obtain, or longer if the acquisition triggers anti-trust filings or national security concerns. The CSRC will not start to review the private placements until MOFCOM or the relevant specific industry regulator (such as CBRC) issues its approval. As the price must be at least 90% of the average trading price for the 20 days preceding the 'price reference date', CSRC approval may be delayed if the trading price as at the time the CSRC is conducting its review differs significantly from the trading price when the agreement was signed. SASAC approval may be required if the target is controlled by a state-owned enterprise.

For acquisitions by agreement, acquiring shares directly from the listed company's parent company or other shareholders is administratively less burdensome, and in general only approval from MOFCOM or the relevant specific industry regulator (such as CBRC) is required. However, SASAC valuations may be required in dispositions of state-owned assets, and if de facto control of the company changes hands or where foreign strategic investment is involved the process will be delayed further by the need to obtain approval from the CSRC.

In respect of acquisitions by offer, the bidder must first submit a report of the offer to the CSRC and the relevant stock exchange. The bidder is then permitted to announce its offer within 15 days after submission of the report provided it has received a notification from the CSRC that it has no objections to the report. The offer period will last a minimum of 30 days and a maximum of 60, unless a competing offer is made (in which case, the offer period will be extended not less than 15 days). The offer cannot be revoked during this period. The purchase of shares by strategic foreign investors also requires approval from MOFCOM or the relevant specific industry regulator (such as CBRC) (see question 1.3).

Where the acquisition triggers merger control filings, clearance of merger control must be obtained before the completion of the acquisition of shares. The merger filing procedure may take several months to process which involves 30 days for preliminary review, another 90 days for further review if MOFCOM requests and this 90-days further review period may be extended by no more than 60 days under certain circumstances. In practice, the merger filing procedures are currently led by MOFCOM.

2.4 What are the main hurdles?

Obtaining the government approvals set out in question 2.3 is key to the success of any deal.

2.5 How much flexibility is there over deal terms and price?

The price for acquisitions by private placement must be at least 90% of the average trading price for the 20 days preceding the 'price reference date'.

In the case of acquisition by offer, there are two floor prices that the bidder has to meet for its offer. First, the offer price cannot be lower than the highest price paid by the bidder for the same type of shares in the six months preceding the announcement. Second, if the offer price is lower than the daily weighted average price of the same type of shares in the 30 trading days preceding the announcement, the bidder's financial adviser must provide their opinion on, among other things, the fairness of the bidder's offer price.

For all three acquisition methods outlined in question 2.1, the CSRC may play an active role in ensuring that deal and price terms meet with its approval, particularly where the price agreed on differs from the trading price at the time of review by the CSRC or, where applicable, the amount set out in the SASAC state-owned assets valuation.

2.6 What differences are there between offering cash and other consideration?

In respect of acquisitions by offer, the Takeover Rules allow payment in cash, securities, a combination of the two, or such other lawful means. Differences between these payment methods are as follows:

(i) For cash acquisitions, the bidder is required to deposit a sum of not less than 20% of the total consideration in a bank account designated by the relevant securities registration and clearing

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organisation within three days after the announcement is made.

(ii) If the bidder offers listed and non-listed shares as consideration it must provide the audited financial and accounting reports, together with a securities valuation report, of the issuer of the shares for the three years preceding the announcement. In addition, the bidder must also coordinate with an independent financial adviser retained by the target to undertake any necessary due diligence work.

(iii) If the bidder offers listed shares, in addition to the above requirement, it must place such shares (with the exception of new shares to be issued) to be used as consideration in the custody of a securities registration and clearing organisation.

(iv) If the bidder offers only non-listed shares, it must also offer cash as an alternative form of consideration.

(v) If the bidder offers bonds as consideration, such bonds must have been traded on a stock exchange for at least one month.

2.7 Do the same terms have to be offered to all shareholders?

Private placements are usually targeted at a limited number of specified investors (the number of target subscribers shall not exceed 10). A general/partial offer to all shareholders is not necessary if the 30% threshold is not triggered as a result of the private placement. The price of each share issued to different investors under one private placement must be the same.

Acquisitions by agreement are normally carried out on an individual basis and directed towards a minority of shareholders. A general/partial offer to all shareholders is not necessary if the 30% threshold is not triggered as a result of the acquisition by agreement. As each shareholder's bargaining position is different, the acquirer may pay a different price to each shareholder.

For acquisitions by offer, all the acquisition terms proposed in the acquisition offer shall be applicable to all shareholders of the target. However, where there exists qualifications as to the acquirer, restrictions in the types of shares or unique circumstances as stipulated by the law, administrative regulations or provisions of the statutes, the bidder may apply for an exemption from the CSRC.

2.8 Are there any limits on agreeing terms with employees?

Under the M&A Regulations, foreign investors acquiring shares in domestic companies must submit a plan for the re-settlement of employees of the target as part of the approval application, and MOFCOM approval is sometimes conditioned on either the guarantee of continued employment or reasonable settlement with employees whose employment will be discontinued.

In the case of an asset acquisition of a state-owned enterprise, the Interim Provisions on Utilisation of Foreign Investment to Restructure State-owned Enterprises provide that the target's 'employees representative congress' (a union-like body common to all state-owned enterprises and many large private companies in China) must be consulted about the transaction and a re-settlement plan should be prepared and approved by the representative congress, local labour administrative authorities and the central government.

2.9 What documentation is needed?

The principal documents in a private placement are:

(i) a board proposal (which includes a feasibility study for the use of funds raised, a report on the previous funds used and other necessary matters of clarification);

(ii) shareholders' resolutions;

(iii) private placement memorandum and agreement;

(iv) application documents to MOFCOM (where strategic foreign investors are involved); and

(v) issuance application documents to be submitted to the CSRC.

The principal documents in an acquisition by agreement are:

(i) the sale and purchase agreement;

(ii) application documents to MOFCOM (where strategic foreign investors are involved);

(iii) report to the CSRC and the relevant stock exchange and announcement in respect of the acquisition; and

(iv) upon completion of the acquisition, report to the CSRC and the relevant stock exchange and announcement in respect of the state of the acquisition.

The principal documents involved in an acquisition by offer are:

(i) report of the offer to be sent to the CSRC and the relevant stock exchange (unless a waiver from the CSRC has been granted). The offeror must, in particular, provide particulars of the amount required for the funding of the takeover and where the source of funding is guaranteed;

(ii) announcement of the offer (after the CSRC has indicated that it does not object);

(iii) preliminary prospectus to be published at least three times within 30 days after the announcement in the news media designated by the CSRC;

(iv) formal circular issued by the bidder, containing, among others, financial information on the target and, where shares are offered as consideration, audited financial and accounting reports, together with a securities valuation report, of the issuer of the shares for the three years preceding the announcement;

(v) 'Report of the Board of Directors of the Target Company' issued by the target board within 20 days after the announcement advising shareholders of its views on the offer and the advice of the independent financial adviser;

(vi) within 15 days after the expiry of the acquisition period, the acquirer shall report and deliver the status related to the acquisition in a written report to the CSRC, and shall simultaneously send a copy to the local branches of the CSRC and the relevant stock exchange and notify the target; and

(vii) application documents to MOFCOM (where strategic foreign investors are involved).

2.10 Are there any special accounting procedures?

In respect of an acquisition by offer, where the bidder offers listed and non-listed shares as consideration, it has to provide the audited financial and accounting reports, together with a securities valuation report, of the issuer of the shares being offered as consideration for the three years preceding the announcement and is required to cooperate with the independent financial adviser in any further due diligence.

In respect of an acquisition by private placement, where the subscriber pays the subscription price in the form of assets or shares, a profit forecast report on such assets or shares is required to be included in the application documents. Such report should be verified by an accounting firm which is qualified to conduct securities-related business. If the price for the assets or shares is based on the results of asset appraisal, the asset appraiser should, in principle, adopt two or more appraisal methods to make the appraisal.

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2.11 What are the key costs?

In addition to the funds required by the acquirer to acquire the target shares, costs may be incurred in relation to borrowings, including interest payments and commitment fees. Other fees will include professional fees in respect of financial advisers, legal counsel, accountants and other professional advisers, fees in respect of printing and distribution, and taxes. PRC stamp duty is payable on the sale and purchase of A, B, C and G shares at the rate of 0.1%. PRC stamp duty is not payable on the transfer of shares listed on an overseas exchange, provided that the transfer is not executed or received in the PRC. However, such transfers may be subject to stamp duty in the other jurisdictions.

2.12 What consents are needed?

Private placements require approval from the target's board of directors and shareholders' general meeting, MOFCOM (and/or specific industry regulator) and CSRC.

Acquisitions by agreement require approval by the target's board and shareholders as well as MOFCOM (and/or specific industry regulator), although CSRC approval will not be required in all cases. For example, CSRC approval is required if de facto control of the company changes hands or where foreign strategic investment is involved. Where shares involve those that are held by state-authorised organisations, approval must also be sought from the state's relevant department in charge.

Acquisitions by offer require the consent of the CSRC, and in the case of strategic foreign investors, the consent of MOFCOM (and/or specific industry regulator).

See also questions 2.3 (governmental approvals).

2.13 What levels of approval or acceptance are needed?

In a partial offer, the bidder must offer to acquire at least 5% of the issued shares of the target and where the pre-acceptance level is higher than that offered, the bidder must acquire the pre-accepted shares on a pro rata basis.

2.14 When does cash consideration need to be available?

In respect of an acquisition by offer, where the acquirer pays for the cost of acquisition with cash, it shall, at the time when making the circular for the acquisition offer, deposit not less than 20% of the acquisition cost in a bank appointed by the securities depository and clearing organisation as a guarantee of the execution of the offer. If the acquirer offers only non-listed shares, it must also offer cash as an alternative form of consideration.

If the acquirer makes a general offer for termination of the listing status of a listed company, or because it fails to obtain a waiver from CSRC after making an application, it shall pay the acquisition price by cash; should it pay the acquisition price by transferable securities in accordance with the law, it shall also offer option of acquisition by mean of cash for shareholders of the target to select.

3 Friendly or Hostile

3.1 Is there a choice?

There are no technical legal constraints on hostile bids, although given the large number of unlisted shares and issues concerning government approvals, hostile takeovers are currently not feasible in many cases.

3.2 How relevant is the target board?

The target board is required to carry out investigations as to the qualifications and creditworthiness of the bidder, and its intent to acquire. It must analyse the terms of the offer, hire an independent financial advisor for a professional opinion and provide advice to shareholders as to whether they should accept the offer. The support or rejection of an offer by the board, together with the Report of the Board of Directors of the target, will be influential both in terms of shareholder assent and government approval.

3.3 Does the choice affect process?

From a legal perspective, hostile bids and friendly takeover offers must be treated equally. However, as a practical matter, the scope of confidential pre-bid discussions and due diligence enquiries by a friendly bidder may be contrasted to the information disclosed to a hostile bidder whose advances have been rejected and who is forced to rely on public information to assess the value of the target.

4 Information

4.1 What information is available to a buyer?

The extent of due diligence may be restricted by the willingness of the target to provide information, so a proactive approach should be taken. Where disclosure is restricted, the bidder may be limited to publicly available information.

4.2 Is negotiation confidential?

The Securities Law provides that all persons who have confidential information, particularly price-sensitive information, must not disclose that information. Secrecy is required to be maintained in respect of negotiations and confidential information before the offer is announced.

If confidential information is leaked to the media or the target's share price exhibits abnormal trading patterns prior to an announcement, the target must immediately launch an inquiry of the parties involved. The target must then make an announcement upon receiving written responses from those parties.

4.3 What will become public?

In respect of an acquisition by offer, 15 days after the bidder has submitted its offer report to the CSRC and the relevant stock exchanges, the CSRC will issue a letter of no objection if the report meets with its requirements. Thereafter, the offer will become public, including the offer's terms such as the term and price of the takeover, the quantity, and guaranteed funding available for the takeover.

See also question 5.2 (disclosure triggers).

4.4 What if the information is wrong or changes?

In respect of an acquisition by offer, once the acquisition offer is issued and announced, the bidder shall be constrained by the offer within the offer period and shall not withdraw or alter at will. If there are any material changes in any basic information of the offer,

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the bidder must detail such changes within two days by submitting a written report to the CSRC, the relevant stock exchange and the target, and make a supplementary announcement.

If any announcement or acquisition offer document is found to contain false or misleading information or major omissions, the CSRC will order the issues to be rectified and adopt appropriate disciplinary procedures, which could include the suspension or termination of the acquisition. Further, prior to the rectification, the acquirer is prohibited from exercising its direct or indirect voting rights over the target's shares.

5 Stakebuilding

5.1 Can shares be bought outside the offer process?

During the acquisition offer period, the bidder shall not carry out trading of the shares of the target in any form outside of the provisions of the offer and those exceeding the terms of the offer (see question 2.5).

5.2 What are the disclosure triggers?

(i) Investors holding 5% of a listed company must disclose such interest by filing a 'Brief Report' with the CRSC and the stock exchange, notifying the target, and making a public announcement. These disclosures also apply to every 5% incremental increase thereafter. 5% would also make the investor a 'connected person' of the target, and any transactions between the investor and the target are 'connected transactions', subject to the various disclosure and approval requirements under the stock exchange listing rules. In addition, a director nominated by the connected shareholder to the board of the target will be deemed a 'connected director' subject to certain voting restrictions.

(ii) At 20%, a 'Comprehensive Report' is required, to include information such as:

- confirmation as to the existence of any actual or potential competition between the acquirer (or its concert parties, their respective controlling shareholders or person who has de facto control over them) and the listed company; the existence of any connected transaction; and any arrangement to prevent such competition and to maintain the independence of the listed company; and
- major transactions between the investor and its concert parties and the listed companies over the preceding 24 months.

(iii) At 30% (or if it already owns 30% and acquires further shares), the acquirer must make either a full or partial (at least 5%) offer for the shares. Upon expiration of the offer period, the bidder is required to purchase all the shares in respect of which the offer has been pre-accepted in accordance with the terms of the offer. If the number of shares which are subject to pre-acceptances exceeds the pre-determined number of shares to be acquired, the bidder must acquire the shares which are subject to pre-acceptances on a pro rata basis.

5.3 What are the limitations?

'Informed persons', including directors, senior officers, shareholders with more than a 5% shareholding in the company and other persons who are able to obtain insider information by virtue of their position, are prohibited from using that information to trade in the shares.

6 Deal Protection

6.1 Are break fees available?

There is no specific prohibition on break fees or inducement fees.

6.2 Can the target agree not to shop the company or its assets?

It is possible to restrain target directors from actively soliciting an alternative offer in competition with a recommended bid by way of agreement. While such agreement may restrict the target directors from engaging in positive solicitation, the board cannot disregard or prevent the disclosure of an unsolicited competing offer.

Note also that to ensure state assets are sold openly and at market prices, 'C' shares must be sold through a process of public bidding followed by agreement between the parties and may require SASAC valuation. The compulsory public auction requirement may be waived in certain cases.

6.3 Can the target agree to issue shares or sell assets?

Under Article 33 of the Takeover Rules, after the bidder announces its offer, the target may not dispose of assets, undertake external investment, change the company's principal business or change any security arrangements for loans if such actions would materially affect the company's assets, liabilities, rights and interests or results of operations, unless the shareholders' general meeting approves. These restrictions do not apply to carrying on normal business activities or enforcing the resolutions of the shareholders' general meeting, although they would rule out the possibility of issuing shares or disposing of crown jewels to the preferred bidder in order to frustrate a hostile bid, unless such action is approved by the shareholders' general meeting.

6.4 What commitments are available to tie up a deal?

It is possible to obtain irrevocable undertakings from majority shareholders to accept the offer within a certain period and prohibit any action which could prejudice the outcome of the offer.

Note that in a public auction of 'C' shares, the target can grant the preferred bidder a right of pre-emption, i.e. the right to increase its bid to match the highest bid.

7 Bidder Protection

7.1 What deal conditions are permitted?

Chinese law does not set out what deal conditions are permitted or prohibited. In theory, therefore, the parties enjoy freedom of contract. See question 2.5 (flexibility over deal terms and price).

7.2 What control does the bidder have over the target during the process?

In an acquisition by offer, the bid must remain irrevocable for between 30 to 60 days (see question 2.3), meaning that the bidder is vulnerable to adverse changes which may occur in relation to the target during that time. However, it is possible to make the offer subject to certain conditions precedent, which could include the absence of material adverse changes.

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7.3 When does control pass to the bidder?

The bidder will take day-to-day control of the target once the directors, officers, and management personnel nominated by the new controlling shareholder are elected at a shareholders' meeting called in accordance with applicable laws and the articles of association of the target.

7.4 How can the bidder get 100% control?

There is no compulsory acquisition mechanism under PRC law allowing the bidder to squeeze out the dissenting shareholders or effect a scheme of arrangement. However, minority shareholders enjoy a sell-out right under Article 97 of the Securities Law, which provides that if, upon expiration of the takeover offer, the public float requirement is not met (10% for companies with a registered capital of more than RMB400 million and 25% for companies with a registered capital of not more than RMB400 million), the stock exchange shall terminate the listing and trading of shares of the target; the remaining shareholders of the target shall have the right to sell their shares on the same conditions as those provided by the takeover offer, and the purchaser must purchase the shares.

8 Target Defences

8.1 Does the board of the target have to tell its shareholders if it gets an offer?

Under Article 67 of the Securities Law, if a 'major event' occurs which may impact the trading price of the company's shares and which is not known to the investors, the listed company shall report such event to the CSRC and the stock exchange, and announce the same.

8.2 What can the target do to resist change of control?

Once the bid is announced, the target's ability to engage in frustrating action is constrained (see question 6.3). The Takeover Rules further require that any defences adopted by the board of directors must be in the interests of the company and the shareholders, and the board may not abuse its powers by improperly obstructing the takeover.

However, the board is required to investigate the bidder and report to the CRSC within 20 days after the bid is announced. This report is likely to be influential, and obtaining CSRC approval may be more difficult if the takeover is hostile.

8.3 Is it a fair fight?

Due to the lack of examples of hostile takeovers and the lack of transparency in the approval process, it is difficult to comment. There is, however, a general perception that one defence against a hostile bidder would be direct and confidential appeal to sympathetic government officials, who may in turn have some influence over the outcome of the approval process.

9 Other Useful Facts

9.1 What are the major influences on the success of an acquisition?

While the approval process is conducted largely behind closed doors, reports suggest that recent bids by foreign investors have met with two main obstacles.

First, is the concern in official circles that foreign firms are gaining control over important state assets. In one high profile deal, an agreement was signed to purchase a controlling stake. After several rounds of negotiation and failing to win CSRC approval for nearly two years, the bid was gradually reduced to a minority stake.

The second, related factor, is the slow pace of approval in a buoyant market. Several deals have failed because the offer price, while fair when the agreement was signed, in hindsight appears low after stock prices surged during the year or more of waiting for CSRC approval. However, the PRC stock markets have plunged significantly in 2008. The sharp drop in share prices may lead to lower offer prices, thus affecting the shareholders' willingness to accept any acquisition offers.

9.2 What happens if it fails?

If a bid is withdrawn during the CSRC review period, the bidder may not bid for shares in the same company for 12 months.

10 Updates

10.1 Please provide a summary of any new cases, trends and developments in M&A Law in China.

China's anti-trust law, the AML, became effective 1 August 2008. The AML comprehensively covers the traditional antitrust topics, including abuse of monopoly power, and mergers and acquisitions. Under the AML, if proposed concentrations meet certain threshold standards, the enforcement authority must be notified and the transaction is subject to anti-trust review and approval. The current Anti-monopoly Enforcement Authority consists of three separate bodies - the Anti-monopoly Investigation Bureau of MOFCOM, the Fair Competition Bureau of SAIC and the NDRC - who oversee mergers, pricing and unfair competition respectively.

The Merger Control Notification Thresholds provide that a pre-merger notification is required if:

(i) the total worldwide turnover of all undertakings to the concentration in the previous fiscal year exceeds RMB10 billion, and at least the PRC turnover of each of two undertakings in the previous fiscal year exceeds RMB400 million; or

(ii) the total PRC turnover of all undertakings to the concentration in the previous fiscal year exceeds RMB2 billion, and at least the PRC turnover of each of two undertakings in the previous fiscal year exceeds RMB400 million.

The rules also give enforcement agencies the authority to review any transaction that does not meet these thresholds but that 'has, or could have, the effect of limiting or eliminating competition'.

In the case of banking, insurance, securities and futures, specific reporting requirements will be drafted by the relevant departments under the State Council.

If notification is required under the AML, a company must submit a notification letter, a description of the effects on the competition status in the relevant market, the actual merger or acquisition agreement and a financial accounting report for the previous year of the companies involved in the concentration. The enforcement authority can require companies to submit 'other documents and information' in order for the concentration to be approved.

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Carl B. Cheng

Freshfields Bruckhaus Deringer LLP
34th Floor, Jin Mao Tower
No. 88 Century Boulevard
Shanghai, 200121
People's Republic of China

Tel: +86 21 5049 1118
Fax: +86 21 3878 0099
Email: carl.cheng@freshfields.com
URL: www.freshfields.com

Carl Cheng is a partner of the firm and has been with the firm's corporate practice and China business group in Shanghai since 1993. He advises on mergers, asset and share acquisitions, restructurings, liquidations and direct investment transactions.
Carl Cheng studied at Yale University and the law school at the University of California, Berkeley. He also attended the National Taiwan Normal University, Beijing University and Keio University before joining the firm in 1993. He had previously practised in the US. He is fluent in spoken and written Mandarin and Japanese.

Miles Ma

Freshfields Bruckhaus Deringer LLP
34th Floor, Jin Mao Tower
No. 88 Century Boulevard
Shanghai, 200121
People's Republic of China

Tel: +86 21 5049 1118
Fax: +86 21 3878 0099
Email: miles.ma@freshfields.com
URL: www.freshfields.com

Miles Ma is an associate based in the Shanghai office of the firm. Miles advises on mergers and acquisitions, securities, financial services and China investment, and has experience in a variety of China-related corporate matters.
Miles Ma is qualified in the PRC. He joined Freshfields Bruckhaus Deringer in 2006. Prior to joining the firm, he worked in a leading Chinese domestic firm, focusing on mergers and acquisitions, securities and financial services.
Miles graduated from the East China University of Politics Science and Law with a Bachelor of Laws (Honours). Miles is a native Mandarin speaker, also fluent in written and spoken English.

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