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Private and confidential **By fax and by hand**

Ref.: P1-L013

Securities and Futures Commission
8th Floor, Chater House
8 Connaught Road Central
Hong Kong

17th November, 2003

Attention: Mr. Brian Ho/Ms. Gail Humphryes
Corporate Finance Division

Dear Sirs,

CLP Holdings Limited ("CLP")

We refer to your letter of 6th November, 2003 setting out your decision on our request and submission dated 28th October, 2003 (the "Submission") for a ruling relating to Rule 32 of the Takeovers Code. We are now writing to request a review of the Executive's ruling by the Takeovers and Mergers Panel (the "Panel") pursuant to paragraph 9 of the Introduction to the Takeovers Code.

Application of Rule 32

We note that the Executive is satisfied that the drafting of Rule 32 is deliberate in not providing a whitewash mechanism for general offer obligations triggered by on-market share repurchases; nevertheless, the wording of Rule 32.1 does not specifically exclude a whitewash application on such grounds and it is evident from the research included in the Submission that market practices have moved on significantly since the wording of Rule 32 was last revised. We therefore consider it is open to the Panel to take the view that a whitewash application triggered by on-market share repurchases is possible.

Possible Code amendment

We also note your response on a possible Code amendment. We had hoped, when we initially raised this matter, that it might be dealt with expeditiously as part of an imminent review of the Code. It is apparent from your reply that the drafting and implementation of revisions require a number of stages to be completed, and you conclude that it is too early to speculate and premature to give a ruling on what amendments might be made. In addition, you have given no indication whether you would be inclined to concur with a possible amendment specifically to allow waiver applications triggered by on-market share repurchases. CLP has concluded that it is unsatisfactory from its point of view for this

question to "hang fire" for a prolonged period in these circumstances and that an early resolution one way or the other should be sought.

Strengths of a voluntary system

One of the great strengths of a voluntary system, as emphasised for example by Peter Scott in his 2002 London Panel Chairman's statement, is flexibility in decision-making. A ruling that whitewash applications triggered by on-market share repurchases are possible would be, in our view, a positive example of a Rule being applied flexibly so that Hong Kong does not lag behind international practice.

Grounds of review

We therefore apply for a review, on the basis of the merits of CLP's Submission and the developments in international markets generally, to the effect that:

(i) Rule 32 should be interpreted to permit whitewash applications triggered by on-market repurchases; and, further

(ii) alternatively, the Panel considers that, in accordance with paragraph 2.1 of the Introduction concerning the spirit of the Code, a strict application of Rule 32, if it is construed to disallow whitewash applications following on-market share repurchases, would be inappropriate having regard to the merits of this particular case and the legitimate interests of CLP and all its shareholders.

We attach a cheque for the requisite fee of HK$50,000 in respect of our application for a Panel review of the ruling.

Yours faithfully,
for and on behalf of
Somerley Limited

M. N. Sabine
Chairman

c.c. Stephenson Harwood & Lo
Client

CLP Holdings Limited ("CLP")

Paper to Takeovers Panel members

Application for a review by the Takeovers Panel of a ruling by the Executive concerning applications for whitewash waivers from general offer obligations triggered by on-market share repurchases ("on-market waivers")

1. CLP's share repurchase programme

CLP has operated a share repurchase programme since May 1998 within parameters carefully defined by the Board. A total of approximately 129 million shares have been purchased under the programme at a cost of almost HK$4 billion.

The programme has proved a great success. It has enhanced the earnings per share for the benefit of all shareholders. It has received overwhelming support from shareholders and favourable comment from analysts. It is the wish of CLP's Board and shareholders that the programme continues.

2. CLP's dilemma

The dilemma faced by CLP is as follows:

- The Kadoorie family holds about 839 million CLP shares (34.84%). If CLP repurchases a further 11 million shares, the Kadoorie family interest will breach the trigger point (in their case) of 35%.
- 11 million shares is less than one week's repurchase of shares during several periods when CLP was actively pursuing its repurchase programme. The share repurchase programme is therefore, in effect, frozen.
- This is an unreasonable restraint on CLP because:
  - the share repurchase programme has been adopted as a long-standing policy
  - it has clear commercial benefits for CLP and its shareholders
  - it gains overwhelming shareholder endorsement each year at the AGM.
- In the absence of an on-market waiver, CLP's choice is to suspend the repurchase programme against the wishes of its shareholders or consider other methods which could be whitewashed, namely an off-market share repurchase or a general offer. Neither of these routes has the merits of the on-market

share repurchase programme. In particular, the on-market share repurchase programme is a wholly transparent process which treats all shareholders equally - all shareholders have the same opportunity to sell shares to the Company at the then prevailing market price. This is not so:

- in the case of an off-market share repurchase, where only selected shareholders have the opportunity to sell; or
- in the case of a general offer where price fluctuations between the date of offer and its implementation can hamper its effectiveness.

Moreover, the Company values its reputation for responsible corporate governance. As a utility, this is one of CLP's most valued assets. CLP is concerned that, should its request be rejected and it is compelled to proceed by way of off-market share repurchase or a general offer, there will be a perception, albeit unwarranted, that this is, in essence, a device to work round the Takeovers Code and to favour the interests of a major shareholder.

3. Initial presentation to Executive

This dilemma was first put to the Executive in a summary "PowerPoint" presentation dated 12th May, 2003 (the "Presentation"), to which Panel members' attention is particularly drawn. A copy is attached as Appendix I. The Presentation includes the benefits of the share repurchase programme and the constraints and safeguards CLP is willing to accept. It also discusses problems with other solutions and corporate governance aspects and summarises international practice.

4. Reasons for requesting a ruling from the Executive and making the Submission

At the meeting held with the Executive on 12th May, 2003, we gained the impression that there was some sympathy with CLP's dilemma and that there was a reasonable chance that revisions to the Code due in some 6-9 months time might address the point. If such changes to the Code were likely in a reasonable time period, CLP was prepared to carry out research and put forward a proposal.

Intervening conversations with the Executive suggested the process would be delayed. However, it still seemed worthwhile to make the submission dated 28th October, 2003 (the "Submission") based on further research which confirmed that on-market waivers were becoming standard internationally and that the rules could accommodate the consequences (e.g. as regards the creeper) relatively easily. As there seemed no settled timetable for revisions, and as market conditions are volatile so that resumption of share repurchases may become an urgent matter, CLP also instructed Somerley to ask for a ruling that Rule 32 in its present form does not preclude on-market waivers or, if it was held that it did, an exception could be made under paragraph 2.1 of the Introduction to the Code. The covering letter and the Submission, with an edited version of the Appendices, are attached as Appendix II.

This is the reason for the somewhat different approach taken in the Presentation and the Submission. The Presentation deals principally with the merits of CLP's case; the Submission deals with broader issues of principle assuming that changes to clarify the scope of the relevant rules were thought desirable.

5. Contents of Submission

The Submission is more lengthy than the Presentation, principally because it includes various Appendices as follows:

Appendix 1	*a one-page report discussing aspects of Chinese takeover regulations as regards share repurchases.*
Appendix 2	*an extract from the pre-1998 London Code on share repurchases. We consider the pre-1998 more informative to look at as the London Code still had a "creeper" provision at that time.*
Appendix 3	*the relevant extract from the Singapore Code.*
Appendix 4	*four sample whitewash circulars from the UK.*
Appendix 5	*two sample whitewash circulars from Singapore.*
Appendix 6	*differences between the Singapore, UK pre-1998, UK post-1998 and Australian models.*

The Appendices mostly contain supporting material but need not be read in detail to follow the argument. To reduce the length of this paper, we have only included Appendices 3 and 6 and extracts from Appendix 4. We would be pleased to circulate the full set of Appendices if members would prefer.

The text of the Submission highlights the following points:

- ***International practice***

  As noted above, international markets allowing on-market waiver applications include the US, the UK, Australia and Singapore. For the reasons explained, we have concentrated on the UK and Singapore. Appendix 3 contains relevant extracts from the Singapore Code.

  We believe the following points from the UK experience and practice are particularly relevant:

  - Out of a total of 50 whitewashes granted in 2002 for all reasons, 15 (30%) were on-market waivers. They have become routine, among the most common grounds for any kind of whitewash waiver. A full circular and IFA opinion does not normally seem to be required (see Appendix 4 to the Submission).

  - The great majority (over 80%) of whitewashes granted in 2002 in respect of share repurchases were on-market waivers. Not only are on-

market waivers permitted, they are much more frequent than waivers for other types of share repurchase (see Appendix to the Presentation).

- The companies concerned are similar to many Hong Kong listed companies - small or medium-sized and controlled by a family or other small group of shareholders.

- *Possible changes to the Code*

  Possible changes are set out, particularly pages 3-4, which could be made to clarify the present Code. It is shown both (i) that the existing Code can deal adequately with on-market share repurchases; and (ii) that clarifications could be introduced relatively easily if it was thought desirable.

- *Acquisitions by controlling shareholders under the permitted creeper*

  The impact of on-market share repurchases on the creeper is explored. Appendix 6 to the Submission works through five detailed scenarios on this point. Reasonable solutions are available for apparent problems regarding the creeper if on-market waivers are allowed.

- *Corporate governance*

  The Executive mentioned that objections to on-market waivers had been previously raised on corporate governance grounds. A number of safeguards and solutions are proposed.

  We would offer the following general comments as regards corporate governance:

  (a) we do not believe on-market purchases raise different or more difficult corporate governance concerns than off-market and general offer waivers, and certain other 'whitewashable" transactions which shareholders are allowed to consider on their merits;

  (b) we do not consider Hong Kong corporate governance standards to be worse than Singapore, which allows on-market waivers; and

  (c) some aspects of UK corporate governances are different to Hong Kong. However, the UK companies to which on-market waivers are relevant are very similar in shareholding structure to many Hong Kong listed companies.

  In summary, we see no valid distinction on corporate governance grounds between on-market waivers and off-market and general offer waivers, and nor apparently do other international markets where Takeovers Codes operate.

6. Comments on the Executive's paper

- References are made in paragraphs 4 and 11 to discussions held in 1998. We believe that such discussions are not germane to the present hearing. We are unaware of the context of such discussions and the factors to which participants' attention may have been drawn. In any event, conditions and practice have changed substantially since 1998.

- Reference is made in paragraph 11 to possible defensive action taken to ward off an unwelcome bid, but this seems already to be covered under Rule 4(e) "No frustrating action". A second point relates to obtaining and consolidating control by on-market share purchases. However, off-market share repurchases and general offer share repurchases can more conveniently be (and may already have been) used for this purpose. In our view, the potential for abuse (if there is one) may be greatest in the case of an off-market share repurchase, which could easily be a form of "greenmail".

  As regards the difficulties an independent financial adviser ("IFA") might face, solutions are proposed in the Submission. In the UK, the IFA's attitude seems quite straightforward -- if on-market share repurchases are in shareholders' interest, then it is a matter of course to approve a waiver to enable such repurchases to be carried out (see Appendix 4 of the Submission).

  As a general comment, the risk of abuse by on-market repurchases is probably less than other "whitewashable" transactions because on-market repurchases can occur purely at the initiative of the listed issuer against the will of the major shareholder. In contrast, most of the other "whitewashable" transactions (except off-market repurchases) involve collaboration with the major shareholder (i.e. to inject an asset, to subscribe for new shares, to take up scrip in a scrip dividend, to undertake not to accept a repurchase by way of GO) and cannot proceed against the wishes of the major shareholder.

- The Executive cites the Regent case in paragraph 13 but we do not see its relevance. It is accepted that share repurchases (by whatever means) are acquisitions of voting rights. Presumably such an acquisition would be a "disqualifying transaction" in the UK, yet in the UK on-market waivers are routine.

- As regards the Executive's comments in paragraph 14, there are many examples of asset injections and cash subscriptions which seem aimed at a change of control of a listed company, and repurchases by way of GO which seem aimed at a consolidation of control of the existing major shareholders. On the other hand, we do not believe it is plausible to argue that on-market repurchases are normally made for the primary purpose of acquiring or consolidating control.

7. **Role of Panel and flexibility and speed of decision-taking**

Since this matter was first raised in May, we have gained the impression that the merits of CLP's particular case have not been fully considered and procedural matters and past debates have taken undue prominence. In this respect CLP considers that the Executive's ruling of 6 November 2003 and its paper to the Panel of 28th November, 2003 have not responded fully to CLP's submission. In particular, the Executive

(a) has not addressed the specific merits of CLP's Presentation and Submission and considered the interests of its shareholders;

(b) has not addressed the wider merits of on-market waivers, as explained by CLP by reference to international practice; and

(c) argues that CLP's submission raises issues which can only be addressed in the context of broader changes to the Code, but provides no guidance as to when and in what form such changes might be implemented nor whether the Executive in principle supports such changes.

In their letter dated 6th November, 2003 replying to our request for a ruling, the Executive said it was satisfied that the drafting of Rule 32 is deliberate in not providing for an on-market waiver and cites discussions in 1998. We do not contest this but believe that it remains open to the Panel to rule that on-market waiver applications can be considered on their merits. To quote from the UK Takeover Panel 2002-2003 report (page 6): "The essential characteristics of the Panel system are flexibility, certainty and speed .... These characteristics are important to avoid over-rigid rules ....". Again, Peter Scott in his 2002 Chairman's statement (page 8): "The Panel's role is as important now as it has ever been. The Panel's .... ability to provide speed, certainty and flexibility in its decision-making remains the envy of other countries."

The clear implication is that one of the Panel's chief functions is to interpret rules flexibly not rigidly, speedily rather than administratively, recognising that rule changes are cumbersome and time consuming, so a more responsive and fast-acting approach is needed.

The wording of Rule 32 provides that if a situation arises whereby a shareholder may become obliged to make a mandatory offer, the Executive should be consulted at the earliest opportunity. The procedure laid down is to consult the Executive and the implication is that it is up to the Executive/Panel to rule on a particular solution, without restriction on what that solution can be, as warranted in response to changing market conditions and practice.

A prime function of the Panel is to interpret rules flexibly and not legalistically, particularly if corporate and market practice has moved on since the rules were drafted. It would be a poor reflection on the Hong Kong securities markets and disadvantageous to Hong Kong listed companies if Hong Kong lags behind the international markets with comparable regulatory systems. It was a long time before Hong Kong companies could repurchase their own shares at all and was one of the factors behind the wholesale migration of Hong Kong companies to Bermuda and

Cayman. A change to permit share repurchases in Hong Kong required a change in the law – in this case, the Panel can take the lead.

8. Paragraph 2.1 of the Introduction to the Code

The Executive concludes its paper by saying that they consider it is not open to the Panel to exercise its power under Section 2.1 of the Introduction to the Codes, partly on the narrow ground that "there is no question of Rule 32 applying at all ....". However, Rule 32 clearly does apply -- it is the Rule which deems that share repurchases will be treated as an acquisition of voting rights which in turn triggers a mandatory offer obligation. This is precisely the result from which CLP seeks an exception.

We believe there are good grounds for exercising discretion in this case if the view is taken that on-market waivers should not currently be generally permitted under Rule 32. As stated above, CLP is a company which has conducted a long-standing share repurchase programme for the benefit of all shareholders. The programme has not been mis-used to consolidate control but has simply come up against a technical barrier. Shareholders were informed of the effective restriction on repurchases in the notice of CLP's last AGM and no doubt expect the Board to take what action they can to remedy the situation.

While other "whitewashable" transactions may have to be considered, the most straightforward course would be to relax, under paragraph 2.1 of the Introduction to the Code, the strict application of Rule 32 if it is interpreted as not permitting on-market waivers. We submit that the strict application would indeed be "unnecessarily restrictive" in the context of CLP, its policies and its corporate governance standards.

CONCLUSION

In conclusion , CLP asks the Panel to give sympathetic and positive consideration to its application in circumstances where:

(a) the course of action which CLP wishes to pursue is wholly unobjectionable and in the best interests of the Company and its shareholders;

(b) the proposed course of action would be considered as wholly unobjectionable and permitted as a matter of routine in other leading markets against which Hong Kong typically benchmarks itself; and

(c) failure to allow CLP to proceed would effectively prevent the Company from continuing a longstanding programme of share repurchases which has enjoyed overwhelming support from all its shareholders.

4th December, 2003