

## Highlights

- Compliance burden and costs reduced
- Flexible approach to position limits effected
- Online information packs on IPOs for retail investors
- First Islamic fund authorised
- More observations on sponsors' due diligence in IPO applications

## Introduction

The SFC has taken some further practical steps to reduce the compliance burden and costs of market participants and increase flexibility to better meet market needs.

In December 2007, we adopted a new approach to granting waivers to structured product issuers. Subject to certain conditions, the new approach grants waivers to issuers to exempt all structured products issued over a 12-month period from the statutory reporting of changes in shareholdings. During the same month, Exchange Participants or their affiliates were given the flexibility to exceed the position limits for Hang Seng Index and H-share Index Futures and options contracts by up to 50% where this is required to serve their clients' needs.

Other initiatives to further improve market efficiency include our proposals to mandate the electronic submission of financial returns and disclosure of interests notices. Consultation on these proposals has been completed and we are analysing the responses.

Separately, the SFC and the Financial Reporting Council have entered into a Memorandum of Understanding (MOU) to recognise the importance of the compliance with financial reporting standards by listed entities and the relevant professional standards by their auditors and reporting accountants. It is hoped that the MOU will facilitate co-ordination of effort and exchange of information between the two parties, thereby enhancing the protection of investors and maintaining their confidence in Hong Kong.

## Compliance Costs for Structured Products Reduced

The SFC adopted a new measure to reduce the compliance burden and costs of issuers of structured products, including derivative warrants, from 21 December 2007.

In Hong Kong, structured product issuers generally do not list their shares on the Stock Exchange. However, they are regarded as listed corporations since they have securities listed on the Exchange. These structured product issuers and their corporate insiders, including their substantial shareholders and directors, are required to report changes in their shareholdings in the issuer under Part XV of the

Securities and Futures Ordinance.

Unlike disclosures relating to shareholdings in listed companies, this information is generally not useful to investors and structured products issuers therefore regularly apply to the SFC for exemption from this reporting requirement. As the number of structured products listed on the stock exchange has grown substantially, the SFC has noted many cases of the same issuer applying for multiple waivers, which are routinely granted.

Requiring structured products to apply for exemption from Part XV in respect of each listed product where the circumstances of the application are identical results in an administrative burden and costs to the industry and indirectly therefore to investors. The SFC considers that these applications to be more effectively dealt with by issuing a single waiver, exempting all structured products issued over a 12-month period from the reporting obligations, subject to receiving certain standard assurances from the issuer.

It should be noted that the waiver is given solely to the issuer of the structured product. The existing obligations of any listed entities whose shares are the underlying asset of that product are not affected.

Information on the new waiver approach has been sent to all issuers of structured products and their legal advisers.

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## Flexible Position Limits Better Meet Market Needs

Changes to the position limits regime, arising from amendments to the Securities and Futures (Contracts Limits and Reportable Positions) Rules (Rules) and the SFC's Guidance Note on Position Limits and Large Open Position Reporting Requirements (Guidance Note), came into effect on 21 December 2007.

The changes introduce flexibility to the existing regime by enabling the SFC to authorise Exchange Participants, or their affiliates, to exceed the statutory position limits for Hang Seng Index futures and options contracts and H-share Index futures and options contracts, by up to 50% where this is required to serve clients' needs.

Please follow this [link](#) to view the final changes to the Rules. The finalised [Guidance Note](#) is accessible via the SFC website.

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## Earlier Disclosure of Information by IPO Applicants

The pilot scheme for posting of web proof information packs ("WPIP") on the website of Hong Kong Exchanges and Clearing Limited ("HKEx") commenced on 1 January 2008.

The pilot scheme requires a new listing applicant, including a collective investment scheme ("CIS"), to submit to HKEx for posting on its website a WPIP no later than the time when information about the listing applicant is first provided to institutional investors. In the case of a company, the WPIP should be in the nature of a near-final draft prospectus and in the case of a CIS, a near-final draft offering circular. A WPIP should omit pricing and related financial and offer size information and must contain the prescribed warning statements.

The rationale for requiring a new listing applicant to submit for posting a WPIP prior to its issue of an initial public offering ("IPO") prospectus is to address the apparent inequality of the timing of information dissemination between institutional and retail investors in an IPO. It also helps ensure a more level playing field amongst all investors, brings the IPO regime in Hong Kong more in line with other leading international jurisdictions and assists in reducing media speculation or market rumours.

The pilot scheme applies to listing applications that are to be heard by the Listing Committee on or after 1 January 2008, and to CIS listing applicants that receive the SFC's approval-in-principle letter on or after that date.

We and HKEx will commence reviewing the operation of the pilot scheme in April 2008 and assuming that no major defect is identified during the pilot period, HKEx will codify the WPIP-posting requirement by amending the Listing Rules.

For further information on the WPIP-posting requirement, please follow this [link](#) to our press release issued on 5 November 2007 to view the policy statement and a set of FAQs.

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## Hong Kong's First Islamic Fund

In support of the Government's initiative to develop Islamic finance, we authorised the first Islamic fund for sale to retail investors in Hong Kong in November 2007.

Islamic funds aim to comply with the investment principles under the Islamic religious law of Shariah which generally preclude investments in businesses such as conventional financial services, alcohol, pork-related products, gambling, leisure and entertainment, etc. The Shariah Principles also preclude interest bearing investments and investments in companies with unacceptable levels of debt.

Like other retail funds, Islamic funds that are offered to the public in Hong Kong need to comply with the requirements of the Code on Unit Trusts and Mutual Funds. In view of the unique features and investment principles of Islamic funds, we have required clear disclosure and easy-to-understand descriptions of the special features of Islamic funds in offering documents and marketing materials, in particular the selection of Islamic permitted stocks and the donation of interest and dividend income to charitable organisations. Prominent disclosure of related risk factors is also included in the product documentation. The management company of the Islamic fund is also required to inform us immediately if the fund fails to obtain an annual Shariah compliance certificate due to non-compliance with Shariah laws.

We have also issued investor education materials specific to Islamic funds to promote the understanding of the product by retail investors. Intermediaries are welcome to use these materials, which are available at [www.InvestEd.hk](http://www.InvestEd.hk), to enhance their customers' understanding of these funds.

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## Disclosure of Relationships Between Listing Applicants and Related Parties

The latest quarterly update on the Dual Filing arrangements highlights the deficiencies in disclosures of relationships between listing applicants and their major customers and suppliers.

In a listing application in the period under review (July to September 2007), a group of shareholders appointed a nominee to hold shares in the listing applicant and this nominee in turn appointed a further nominee to hold the shares on its behalf. Most of the members of this group of shareholders were employees of a major customer of the listing applicant. However, it was only in response to the regulators' enquiries that full disclosure of these relationships was made in the prospectus and that transactions between the listing applicant and the major customer were subjected to scrutiny as related parties transactions.

In another case, the listing applicant was involved in a major dispute with its largest customer. The listing applicant failed to disclose sufficient information for investors to understand the circumstances leading to the dispute and the implications for the listing applicant's operations and financial position.

Sponsors are reminded to ensure that listing applicants properly disclose all material features of their relationships with major customers and suppliers, including the implications for the applicant's business of any material litigation or disputes.

For more details of the update on Dual Filing, please follow this [link](#) to our press release dated 5 December 2007.

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## Publications & Circulars

The following publications and circulars have been published since the release of the last newsletter. Publications are available on the SFC website under 'Speeches, Publications & Consultations' – 'Publications'. Circulars can be found under 'Legislation & Regulatory Handbook' – 'Regulatory Handbook' – 'Codes, Guidelines and Circulars'.

### Publications

1. Enforcement Reporter – January 2008 (28.1.2008)
2. SFC Takeovers Bulletin – December 2007 (20.12.2007)
3. Quarterly Report – July to September 2007 (13.12.2007)
4. Consultation Paper on Proposal to Mandate Electronic Submission of Disclosure of Interests Notices (30.11.2007)
5. Financial Review of the Securities Industry – July to September 2007 (30.11.2007)
6. Consultation Paper on Electronic Submission of Financial Returns (9.11.2007)

### Circulars

1. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing - (1) United Nations (Anti-Terrorism Measures) Ordinance (2) US President's Executive Order 13224 (28.1.2008)
2. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing - (1) United Nations Sanctions (Liberia) Regulation 2005 (2) US President's Executive Order 13224 (8.1.2008)
3. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing - (1) United Nations (Anti-Terrorism Measures) Ordinance (2) US President's Executive Order 13224 (16.11.2007)

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Feedback and comments are welcome and can be sent to [sfcbulletin@sfc.hk](mailto:sfcbulletin@sfc.hk)