



**SECURITIES AND
FUTURES COMMISSION**
證券及期貨事務監察委員會

Consultation Conclusions on
the Securities and Futures (Stock Market Listing) Rules
and
the Securities and Futures (Transfer of Functions –
Stock Exchange Company) Order

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Introduction

1. On 6 May 2002 the SFC issued a consultation paper (“Consultation Paper”) on the draft Securities and Futures (Stock Market Listing) Rules (“draft Rules”) and the draft Securities and Futures (Transfer of Functions – Stock Exchange Company) Order (“draft Order”) to be made under the Securities and Futures Ordinance (5 of 2002) (“Ordinance”). The draft Rules and draft Order will be subsidiary legislation under the Ordinance and deal with effective regulation of information disclosure by listed companies and listing applicants.
2. The proposals in the draft Rules and draft Order received broad support from the public; press reports following the release of the Consultation Paper also reflected this. They were generally viewed as a positive move to improve the quality of corporate information disclosure.
3. The consultation period ended on 7 June 2002 but late submissions were also accepted and considered. A total of 11 submissions were received, including one submission from a law firm made on behalf of 4 financial institutions, one submission from a professional body summarizing a survey conducted of its members, and submissions from other professional bodies, practitioners, and a market organization. A profile of the respondents is set out in the Annex.
4. The majority of the submissions were in favour of the proposed disclosure arrangements and regulation by the SFC. Most of the detailed comments relate to operational and technical issues. There were no comments on the draft Order. This document, to be read in conjunction with the Consultation Paper, analyses the consultation submissions and sets out the conclusions.

Consultation Conclusions

General

5. Under the draft Rules, companies that disseminate information to the public pursuant to applicable rules or laws will have to file a copy of the disclosure materials, including any prospectuses and listing documents, with the SFC. Any person who intentionally or recklessly provides false or misleading information when making the disclosure (i.e., any company that lies to the public) would be subject to the statutory powers of the SFC. The SFC will be able to employ its existing investigatory powers in gathering evidence and establishing the facts. In appropriate cases, the SFC may bring (or refer to the Department of Justice to bring) offenders to prosecution in the courts.
6. Most of the respondents supported and welcomed the proposals. They saw the draft Rules as a positive regulatory measure to enhance corporate governance as well as the transparency, credibility, and competitiveness of the Hong Kong securities market. One of the respondents also remarked that the proposals would facilitate and enhance the role of the Stock Exchange as the frontline regulator of listing matters, while allowing the market to continue to enjoy the benefits of the flexibility of the non-statutory Listing Rules.
7. Two of the respondents suggested that in addition to the proposal, the SFC should take on entirely the prospectus vetting and listing regulatory functions, which would be in line with development overseas. It was suggested that the then proposed abolition of the Listing Committee could remove a vital check and balance mechanism within the Exchange.

Criminal liability on the provision of false or misleading information

8. The draft Rules extend criminal liability under existing laws, re-enacted as section 384 of Ordinance, to persons who intentionally or recklessly provide false or misleading information in listing documents and on-going disclosure materials (i.e., persons who lie to the investing public).
9. The majority of respondents supported this proposal. However, two respondents believed existing civil and criminal provisions under the Ordinance and the Companies Ordinance deal adequately with false or misleading statements or communications concerning securities and futures contracts. They queried whether statutory filing of disclosure documents with the SFC would provide any greater investor protection.
10. One of these two respondents noted that false or misleading disclosure under section 384 of the Ordinance has lower threshold for liability than offences under sections 277 and 298 of the Ordinance (on disclosure of false or misleading information inducing transactions). It was further noted that the SFC would not need to give any warning of potential liability before receiving filings.

11. The SFC would like to point out that sections 277 and 298 do not deal directly with the obligation of truthful disclosure by listing applicants or listed companies.
12. Our securities market is founded on proper disclosure of reliable information. Intentional and reckless provision of false or misleading information to the public undermines this principle and those responsible should be held to account. There is a general expectation that this will be the case; it would be wrong to require a specific warning before each filing is made.
13. A respondent queried whether the Rules would apply to sponsors, arrangers, or lead managers. The SFC confirms that these persons are not considered “applicants” or “issuers” as defined in the Rules. However, professionals and intermediaries are also reminded of the important role they play and their associated duties, many of which are set out in the SFC Corporate Finance Adviser Code of Conduct and in the Stock Exchange Listing Rules. Failure to satisfy these responsibilities could lead to disciplinary action.

Definition and scope of listing applications

Definition of listing application

14. In the draft Rules, “application” is defined to include all documents in support of or in connection with an application, including any replacement of, or amendment or supplement to, such application.
15. Two respondents believed that the definition of listing “application” was too wide, because it would include any communication from an issuer in response to a request from the Exchange for additional information, clarification or elaboration in connection with an application.
16. The SFC disagrees. The listing applicant is applying for access to the market to raise funds from public investors. The information it provides to the public or to the regulators in order to gain access is crucially important. Those who intentionally or recklessly provide false or misleading information during this process should be held liable.
17. One respondent suggested that there should be a cut-off time for the provision of such communication. The SFC agrees with this suggestion and has amended the draft Rules accordingly.

Requirements for a listing application

18. As in the existing Securities (Stock Exchange Listing) Rules, clause 3 of the proposed new Rules sets out a list of requirements for a listing application.
19. Two respondents believed that these items should be a matter for the Listing Rules of the Exchange and, where appropriate, the Third Schedule of the Companies Ordinance. In addition, certain requirements in clause 3 may not always be relevant to particular types of listed products.

20. The SFC agreed with the suggestions and has amended the draft Rules accordingly.

Exemptions from the requirements of a listing application

21. As in the existing Securities (Stock Exchange Listing) Rules, clause 4 of the proposed new Rules sets out a list of exemptions from the requirements of a listing application.
22. Two respondents believed that the existing list of exemptions should be expanded. One respondent also suggested that the SFC should have the flexibility to specify additional exemptions in order to be responsive to market development.
23. The SFC agrees. The draft rules have been amended to exempt shares issued pursuant to an employee stock option scheme that has been approved by shareholders in a general meeting. The list of exemptions will be reviewed from time to time and further amended in light of market development.

Dual filing and vetting by the Exchange and the SFC

Dual filing

24. Clause 5 of the draft Rules requires companies seeking access to the public market to file a copy of its listing application made to the Exchange with the SFC. In order to avoid duplication, the clause provides that a company may simply authorize the Exchange to making the filing on its behalf.
25. This cost saving measure was welcomed by the respondents. One respondent believed that flexibility should be afforded to the Exchange as to the extent and timing of the information to be provided to the SFC. The respondent also believed that the SFC should channel its request for further information and the applicant should channel its response through the Exchange.
26. The SFC has deliberately framed the draft Rules to ensure that the listing process is not burdened with additional red tape. Under the “deemed filing” provisions, listing applicants and listed issuers satisfy their obligations once they file with the Exchange, provided that they have authorized the Exchange to forward a copy to the SFC. The administrative arrangements between the Exchange and SFC are matters for the two organizations. (With the enactment of the new Ordinance, the SFC and the Exchange would need to revise the Memorandum of Understanding between the two bodies. The new MOU will be published as soon as it is ready.) Indeed, since the Exchange is already moving towards electronic submission/reception and dissemination of disclosure documents, forwarding to the SFC can be automatic. By using FinNet, the communication would also be secure.

Dual vetting

27. In line with the model practiced in all major overseas markets, under the draft Rules, the SFC will be able to comment on the draft listing disclosure materials (principally the prospectus) and object to a company accessing the public market on the basis of insufficient or inadequate disclosure within a 10-business-day period.
28. Some respondents felt that this might result in duplication of effort between the SFC and the Exchange, create uncertainty as to the regulatory roles of the two bodies, and potentially increase compliance costs. One respondent specifically argued that the “dual” approach is unnecessary as the SFC should take over entirely all vetting and listing regulatory functions.
29. The SFC would like to make clear that, with the “deemed filing” provisions in the draft Rules, the Exchange will remain the point of contact with listing applicants and will conduct the frontline review. Arrangements will be made between the SFC and the Exchange to ensure consistency of comments given to the listing applicant.
30. The proposal should not add to compliance costs. Providing truthful information to the public is an existing obligation and all relevant compliance mechanisms should be in place. The SFC will raise queries and take enforcement action only if there are grounds to suspect that there is a disclosure problem.
31. Some respondents commented that the 10 business days period is too long and might lead to delay in the listing process. In particular, one of the respondents suggested that the period should be shortened for derivative warrants and structured products.
32. The SFC would like to clarify that the 10-day period would run concurrently with the Exchange’s vetting timetable, which usually takes a minimum of 25 clear business days. It would not prolong the listing approval process. The SFC also agrees with the suggestion that certain structured products are marketed with standard disclosures. To address the different considerations arising out of varied products, the SFC will take into account the special nature of different products and confirms its “no objection” to the listing in as short a timeframe as possible.
33. One respondent suggested that there should be a cut-off time for further documents to be subject to the 10-day vetting period. The SFC agrees with this suggestion and has amended the draft Rules accordingly.

Objection to listing applications

34. Clause 5(6) of the draft Rules empowers the SFC to object to a listing if the applicant does not comply with the applicable rules and requirements or if it appears that the listing would not be in the interest of the investing public or in the public interest.

35. Some respondents queried what steps the SFC will have to take to be in an informed position to consider whether to object to a listing. Two respondents also felt that this might contradict the statement in the Consultation Paper that the SFC will not be looking at the merits of a transaction.
36. The SFC would like to make clear that it will not attempt to assess the commercial merits of each listing applicant. The draft Rules provide that SFC may ask a listing applicant for further information. This is standard practice in developed markets and is part and parcel of disclosure-based regulation.
37. The “interest of the investing public and public interest” criterion mirrors clause 7(1)(c) of the draft Rules, which is based on a similar provision in the existing Securities (Stock Exchange Listing) Rules empowering the SFC to suspend dealings in the interest of the investing public or in the public interest.
38. One respondent raised the need to clarify follow-up actions or consequences arising from objection by the SFC and to spell out the subsequent procedures.
39. The SFC would like to repeat its explanation in the Consultation Paper that, in the event it makes an objection, the applicant would have a full right of appeal to the independent Securities and Futures Appeal Tribunal for a fresh review. (This would require amendments to the list of specified decisions in Schedule 8 to the Ordinance.) The procedures are set out in Part XI of the Ordinance and related rules.

Suspension of dealing

40. The draft Rules provide for suspension of dealing in a security by the SFC under certain circumstances. Clauses 8 and 9 then provide for the making of representations by the issuer or the Exchange.
41. One respondent suggested that the sponsor, arranger, or lead manager to a transaction should have the ability to make representations to the SFC with respect to a listing application.
42. The SFC would like to clarify that clauses 8 and 9 deal with the suspension of dealings, not listing applications. Financial advisors would, of course, be able to make representations on behalf of the issuers.
43. Professionals and intermediaries may also make representations on behalf of a listing applicant, provided, of course, that the applicant authorizes so and takes responsibility for the truthfulness of the information.
44. Clause 17 of the draft Rules requires the Exchange to inform the SFC of its intention to suspend or permit recommencement of dealings in any securities before or as soon as practicable after the event.

45. One respondent felt that the Exchange should have the flexibility to inform the SFC of a suspension as soon as reasonably practicable, while another believed that the Exchange should be able to permit a resumption of trading following a suspension it has itself instigated without the prior approval of the SFC.
46. The SFC would like to clarify that, in the case of a suspension, the draft Rules already provide that, if it is not reasonably practicable for the Exchange to inform the SFC of its intention to suspend, it need only to inform the SFC as soon as possible after the event. In the case of resumption, the draft Rules only require the Exchange to give prior notice to SFC and no approval need be sought.

Approved share registrar

47. As in the existing Securities (Stock Exchange Listing) (Approved Share Registrar) Rules, clause 13 of the draft Rules requires a listing applicant to appoint an approved share registrar in Hong Kong to maintain its register of members.
48. Two respondents felt that the requirement to maintain a share register in Hong Kong should only apply to issuers whose shares, and not other types of securities, are listed on the Exchange.
49. To extent that the issue is, as the respondents believe, a matter of technical clarification of an established interpretation of existing laws, SFC would agree with the suggestion. However, as the issue also relates to stamp duty, SFC would need to seek confirmation from the Inland Revenue Department. It will make the appropriate amendment to the draft Rules accordingly.

Securities and Futures Commission
July 2002

Profile of respondents	Annex
<u>Nature of business</u>	<u>Number</u>
Legal advisers (<i>Note</i>)	2
Accounting firms	2
Financial institutions	1
Professional bodies	5
Other organizations	1
	11

Note: One legal adviser made its submission on behalf of 4 financial institutions