



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

**Consultation conclusions in relation to expanding
the scope of short position reporting and the
corresponding amendments to the Securities and
Futures (Short Position Reporting) Rules**

24 February 2016



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Foreword

1. On 27 November 2015, the Securities and Futures Commission (SFC) released a public consultation proposing to expand the scope of the short position reporting regime to cover all Designated Securities and make a few other enhancements (Consultation Paper). The SFC sought comments on these policy proposals and modifications to the Securities and Futures (Short Position Reporting) Rules (SPR Rules) to reflect the proposed enhancements.
2. The consultation ended on 31 December 2015. A total of 51 written submissions were received. The submissions mainly came from two groups: financial institutions and professional associations representing the views of their members, and individuals. The list of respondents (other than those that requested to remain anonymous) is set out at Appendix A. The comments received (unless requested to be withheld from publication) can be viewed at the SFC's website.
3. This paper sets out SFC's responses to the comments received, SFC's conclusions and the proposed way forward after taking into account public feedback. This conclusions paper should be read in conjunction with the Consultation Paper.

Executive Summary

4. A majority of the financial institutions and professional associations agreed with the proposal to expand the scope of short position reporting to all Designated Securities. This group also agreed that the reporting threshold trigger for collective investment schemes (CISs) be set only at the HK\$30 million threshold and that the SFC will determine the Designated Securities that will be subject to daily reporting in contingency situations. They also welcomed additional channels for reporting.
5. However, a number of the individual respondents opposed the proposal to expand short position reporting to all Designated Securities. They were of the view that the SPR Rules should be scrapped or, if they are maintained, the reporting threshold trigger should be raised.
6. After carefully considering all comments received, the SFC is of the view that the proposals as set out in the Consultation Paper are appropriate for the Hong Kong market and will proceed accordingly.
7. There was no substantive comment on the text of the amendments to the SPR Rules as proposed in the Consultation Paper. The SFC will therefore submit the proposed amendments to the SPR Rules to the Legislative Council for negative vetting.
8. Subject to the legislative process and to give the market reasonable lead time to get their reporting systems and procedures in place, our target is to implement the amended SPR Rules on 15 March 2017. The SFC will also make further announcements regarding any pilot run arrangements and provide additional FAQs.



SFC's responses to the comments received

Expanding the scope of reporting

9. The SFC proposed in the Consultation Paper to expand the scope of the short position reporting regime to all Designated Securities. A majority of the financial institutions and professional associations agreed with the proposal. The financial institutions requested for clarification on some operational details to assist their reporting, and that sufficient lead time be given for implementation. We have provided more information on the operational aspects of reporting in paragraphs 26 to 29.
10. A number of the individual respondents opposed the proposal. One respondent commented that the SPR Rules should be scrapped. He also indicated that if the SPR Rules are to be maintained, the short position reporting regime should (i) require a person who has a short position of 5% or more in listed shares to disclose to the market so as to be in line with the regime for disclosure of long position under Part XV of the Securities and Futures Ordinance (SFO), or (ii) alternatively, raise the reporting threshold trigger to 0.2% and remove the \$30 million threshold so as to be in line with the short position regime in the EU.
11. In response to the comment that the SPR Rules should be scrapped, we wish to reiterate that IOSCO recognises the merits of and supports enhancing transparency of short selling¹. Short position reporting is now a regulatory requirement in most major jurisdictions which include the US, EU, Japan and Australia. The SFC considers that Hong Kong, as an international financial centre, should have a short position reporting regime to enable the SFC to more effectively monitor short selling activities.

Objectives of disclosure of long position and short position reporting

12. With regards to the comment that the short position reporting regime should be in line with the disclosure of long positions under Part XV of the SFO, we would like to point out that the regulatory objectives of the reporting regimes under the SPR Rules and Part XV of the SFO are different. Hence, the reporting thresholds for the respective regimes differ. IOSCO noted in its Report on Transparency of Short Selling published in June 2003² that the logic behind disclosures for long and short positions is not symmetric and thus, disclosure regimes for long and short positions need not be identical. In particular, IOSCO noted that requirements for the disclosure of long positions normally flow from the perceived need for the management of issuers to be aware of who currently holds a significant interest in their voting capital. In the case of short positions, holders have no proprietary interest in voting shares. It is also worth noting that the European Securities and Markets Authority (ESMA) in its final report on its evaluation of the EU short position reporting regime released in 2013 stated³: "*In ESMA view, the different objectives of those two pieces of EU legislation⁴ justify the different thresholds applicable to net short positions and long positions.*" As is the case in most major markets, the disclosure regime for long positions was in place long before short position reporting became a global regulatory standard.

¹ IOSCO final report on Regulation of Short Selling, June 2009: <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD292.pdf>

² <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD147.pdf>

³ https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-614_final_report_on_ssr_evaluation.pdf

⁴ This refers to the Regulation 236/2012 on short selling and certain aspects of credit default swaps and the Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.



13. The principal function of disclosure of long positions under Part XV of the SFO is to provide information to the market and to listed companies about persons who may influence or control a listed company's decisions. In this regard, persons who hold 5% or more of any class of voting shares in a listed corporation have to disclose their interests and their dealings in such interests, and directors and chief executives of a listed company must also disclose their interests and their dealings in such interests⁵.
14. A concern associated with short selling is the potential for exacerbating a downward spiral of stock prices in a volatile market. The pace and extent of stock prices declines, as a result of short sales, may happen very rapidly which could create disorder or induce panic. Therefore, one of the regulatory objectives of short position reporting under the SPR Rules, as explained in past consultation papers⁶, is to facilitate the SFC to monitor a build-up of large short positions that may potentially be disruptive to the orderly functioning or stability of the market. Another regulatory objective is to deter the use of short selling to manipulate the market in breach of SFO market misconduct provisions.

Reporting threshold

15. The existing reporting threshold trigger for stocks (i.e. 0.02% of the market capitalization of the listed issuer concerned or \$30 million, whichever is lower) was determined after studies conducted by the SFC of the unique characteristics of the Hong Kong market and consultation with market participants prior to implementation in June 2012.
16. As explained in past consultation conclusions papers, there is no "one-size-fits-all" threshold level. Any recommendation for adopting a reporting threshold used in another market must be predicated on a sound analysis taking into account differences in market structures and regulatory goals. Different starting points in terms of domestic market considerations, existing regulatory frameworks and regulatory goals will invariably result in differences in reporting requirements between markets. For example, in the EU, investors are required to report to the regulators their net short positions in a listed company if they represented 0.2% or more of the share capital. If the positions are more than 0.5%, investors have to disclose publicly. Whilst the EU reporting regime requires positions held through derivatives to be reported, our regime excludes derivatives. The inclusion of derivatives in a reporting regime is likely to result in much larger short positions. In Australia the notification threshold is set at AUD100,000 or 0.01% of the market capitalization of the listed issuer and in the US, brokers are required to report all short positions without being subject to any reporting threshold.
17. If the reporting threshold is set at a high level, an early build-up of large short positions would not be detected. Based on the above considerations, the SFC has decided to set the reporting threshold at the current level.

Comments on other areas related to short selling

18. We also received comments regarding removal of the "uptick" rule and the concept of Designated Securities. Although related to short selling, they fall outside the scope of the consultation and are not addressed in this paper.

⁵ Consultation paper on Amendments to The Securities (Disclosure of Interests) Ordinance, June 1998:

<http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=98CP4>

⁶ Consultation on Increasing short position transparency, 31 July 2009:

<http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=09CP2>



Threshold trigger for reporting short positions in relation to collective investment schemes

19. As explained in the Consultation Paper, the SFC proposed that the existing reporting threshold (i.e. 0.02% of the market capitalization of the listed issuer concerned or \$30 million, whichever is lower) will apply to all Designated Securities except CISs. Given that some CISs are open-ended, and for the reasons stated in the Consultation Paper, we proposed that the reporting threshold for CISs will be set only at the HK\$30 million threshold.
20. Most of the respondents who commented on this issue supported the proposal.

Designated Securities that are traded in currency other than Hong Kong dollars

21. In the Consultation Paper, we proposed to formalise an existing practice which is to convert the closing price of a Designated Security expressed in a currency other than Hong Kong dollars (i.e. US dollars or Renminbi) first into Hong Kong dollars for the purposes of determining the value of a net short position. The rate of exchange will be the buying rate for telegraphic transfers on the reporting day, as determined by the Hong Kong Monetary Authority (HKMA). There was no strong objection to our proposal.

Reporting in contingency situations

22. Under the SPR Rules, the SFC is empowered to change the reporting frequency from weekly to daily in a contingency situation. To reduce operational burdens for both the SFC and market participants, the SFC proposed that, in contingency situations, the SFC will determine which Designated Securities that will be subject to daily reporting.
23. Respondents who agreed with the proposal to expand the scope of short position reporting were of the view that daily reporting for all Designated Securities in contingency situations would be burdensome. In this regard, they were supportive of our proposal.

Reporting through SFC designated electronic system

24. Currently, market participants must report short positions using an electronic system developed by the SFC specifically for this purpose. In view of the pace of technological development, the SFC consulted on providing flexibility in the SPR Rules such that the SFC may adopt more than one electronic system for reporting in the future. Respondents welcomed additional channels for short position reporting. Some also provided suggestions on how to introduce a new reporting system.
25. We will be conducting a thorough study in this area. Further details will be announced once the study is complete. Until then, market participants are expected to continue using the existing channel for reporting short positions.



Operational arrangements for reporting

26. At present, the list of specified shares is published on the SFC's website for each report date, including the stock code and stock name of the specified shares in Comma Separated Value (CSV) and PDF formats. In view of the expanded scope of reporting, a number of respondents suggested that the SFC publishes a similar CSV file that covers all the Designated Securities. In addition, they would like the CSV file to contain information including:
- (a) the security type of a Designated Security;
 - (b) the currency that the Designated Security is traded in (i.e. HKD, USD or RMB for the time being); and
 - (c) if applicable, the exchange rates for currencies other than Hong Kong dollars.

The respondents considered that the CSV file together with the additional information would facilitate their reporting process in view of the larger number of short positions to report and the different reporting threshold for CISs.

27. We understand that it is the current practice of some market participants to automate their reporting process using the list of specified shares published on the SFC's website. Market participants are expected to monitor closely any changes to the list of Designated Securities once the proposed Rules take effect. That said, the SFC will consider how to facilitate the reporting process.
28. The SFC agrees with the suggestion to include the security type of a Designated Security and the currency in which it is traded in the CSV file. However, we are of the view that it is not necessary to include exchange rates as determined by HKMA in the CSV files, as they are published on HKEX's website and we understand that the practice of some market participants is to automatically extract these rates. In any event it would be impractical to include exchange rates otherwise the CSV file will need to be updated to reflect the most current exchange rates on a daily basis.
29. Further information in relation to the proposed CSV file (file specification, sample file, when and where the file be published, etc.) will be announced in due course. Those interested are encouraged to subscribe to the short position reporting email alert service available at <https://www.sfc.hk/CampaignHelper/campaignForm.jsp?lang=EN>

The way forward

30. After considering all the comments received and suggestions put forward, we conclude that the proposals as set out in the Consultation Paper are appropriate for the Hong Kong market and will proceed accordingly.
31. Since there were no substantive comments on the text of the proposed amendments to the SPR Rules, we will adopt the amendments as proposed in the Consultation Paper.



Concluding Remarks

32. The SFC will submit the amendments to the SPR Rules to the Legislative Council for negative vetting. Subject to the legislative process and to give the market reasonable lead time to reconfigure their reporting systems and procedures, our target is to implement the amended SPR Rules on 15 March 2017. The SFC will also make further announcements regarding any pilot run arrangements and provide additional FAQs.



Appendix A

Lists of non-confidential respondents

(in alphabetical order)

1. Alternative Investment Management Association
2. Alex Wallis
3. Apollo Investment Management Ltd
4. Asia Securities Industry & Financial Markets Association
5. BlackRock
6. CompliancePlus Consulting Limited
7. Complyport (HK) Limited
8. David Gunson
9. Eric Woo
10. Fraser Howie
11. GMX
12. Hong Kong Investment Funds Association
13. Jack Kwan
14. Kevin Chan
15. Law Society of Hong Kong, The
16. Liam McDonald
17. Paul Whitaker
18. Rex Lee
19. Richard A Witts
20. RJC Harding
21. Webb-site.com
22. WK Chan
23. Anonymous – twenty-seven respondents requested that their identities not be published



24. Anonymous – two respondents requested that their identities and contents of their submissions not be published