



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

**Report on the Securities and Futures Commission's  
2009 annual review of the Exchange's performance  
in its regulation of listing matters**

December 2009



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## Executive Summary

1. This report summarises the key findings and recommendations of the Securities and Futures Commission's 2009 annual review regarding the performance of The Stock Exchange of Hong Kong Limited (the "Exchange") in its regulation of listing matters during 2008.
2. This report records our assessment of the Exchange's performance for the year 2008.
3. We reviewed the Exchange's operational procedures and decision-making processes in each of the Listing Division's operational departments to assess whether they are adequate to enable the Exchange to meet its statutory obligation under section 21 of the Securities and Futures Ordinance (the "SFO"). The Exchange has a statutory obligation under section 21 to ensure, as far as reasonably practicable, an orderly, informed and fair market.
4. We also reviewed the Exchange's processes and procedures in respect of its powers to make rules under section 23(2) of the SFO to assess whether it is appropriate to enable the Exchange to fulfil its statutory obligation under section 23 of the SFO to make rules for such matters as are necessary or desirable for, inter alia, the proper regulation and efficient operation of the market which it operates.
5. We are of the view that the operational procedures and decision-making processes reviewed were appropriate to enable the Exchange to discharge its statutory obligation under sections 21 and 23 of the SFO during the period reviewed.
6. We are satisfied that the Exchange has taken steps to address the recommendations in our 2008 report. Since the period covered in our 2008 annual review, the Exchange has continued reviewing and refining its practices and procedures and has adopted new initiatives to further enhance its performance in respect of how it seeks and solicits market views during the process of making or amending the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules")<sup>1</sup>.
7. This report is divided as follows:
  - (a) Section 1 explains the purpose and focus of our review, its scope and the review process;
  - (b) Section 2 sets out our assessment and recommendations in respect of our review of Exchange's operational procedures and decision-making processes in each of the Listing Division's operational departments to assess whether they are adequate to enable the Exchange to meet its statutory obligation under section 21 of the SFO;
  - (c) Section 3 sets out our assessment and recommendations in respect of the Exchange's processes and procedures in respect of its powers to make rules under section 23(2) of the SFO to assess whether it is appropriate to enable the Exchange to fulfil its statutory obligation under section 23 of the SFO;

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1 References in this report to the "Listing Rules" refer to the Main Board Listing Rules and the GEM Listing Rules. For simplicity, references to a particular "Rule", "Rules", "Chapter" or "Chapters" refer to the Main Board Listing Rules only. The GEM Listing Rules contain broadly equivalent rules. As such, our observations and comments in this report apply equally to GEM.



- (d) Appendix A is a table summarising the results of a survey of the Listing Committee members and the market participants' view of the Exchange's performance; and
- (e) Appendix B is a table summarising the 15 policy issues and the relevant proposals that have been adopted in the Consultation Conclusions.



## Section 1

### Purpose and focus of our review

8. This is our report on our 2009 review of the Exchange's performance in its regulation of listing matters during 2008.
9. We have a statutory duty under section 5(1)(b) of the SFO to supervise, monitor and regulate the activities carried on by the Exchange. As set out in the Memorandum of Understanding between the Exchange and ourselves dated 28 January 2003 ("Listing Matters MoU"), we have agreed with the Exchange that we should periodically review the Exchange's performance in its regulation of listing-related matters. Our periodic review does not cover the other activities carried on by the Exchange, such as market and product development.
10. In March 2004, the Government published its Consultation Conclusions on Proposals to Enhance the Regulation of Listing. Amongst other matters, the Government recommended that we prepare annual reports on our review of the Exchange's performance of its listing functions and submit these reports to the Financial Secretary. This is our fifth report following the Government's recommendation.
11. As a recognised exchange under the SFO, the Exchange has statutory obligations to:
  - (a) ensure an orderly, informed and fair market, so far as reasonably practicable, and
  - (b) act in the interest of the public, having particular regard to the interest of the investing public<sup>2</sup>.

The Exchange is also required under section 21(6)(b) of the SFO to provide and maintain competent personnel for the conduct of its business. It has also agreed in the Listing Matters MoU to maintain an adequate level of staff strength in the Listing Division with an adequate level of professionalism and experience to discharge the responsibilities of the Listing Division.

12. Except for matters specifically reserved by the Listing Committee, most matters concerning the Listing Rules are dealt with by the Listing Division in the first instance. Matters dealt with by the Listing Division include processing listing applications, monitoring and enforcing listed companies' compliance with the Listing Rules.
13. As with our previous review, we reviewed the Exchange's operational procedures and decision-making processes to assess whether they are adequate to enable the Exchange to meet its statutory obligations under section 21 of the SFO.
14. In addition, we also reviewed the Exchange's processes and procedures in respect of its powers to make rules under section 23(2) of the SFO to assess whether it is appropriate to enable the Exchange to meet its statutory obligation under section 23 of the SFO.

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2 Section 21 of the SFO



15. The Exchange's statutory obligation under the SFO is ongoing, and whether it has made necessary arrangements to comply with its obligation in the future cannot be judged merely by reference to its past compliance. Therefore we use the review process to assess whether the Exchange has taken adequate steps to meet its statutory obligation and identify issues that, in our view, should be addressed to ensure ongoing compliance.
16. During the course of our review of the Exchange's performance, we may also make observations of the current issues and changes in the Exchange's operational procedures and decision-making processes. The review process is an on-going process and does not seek to review the Exchange's past performance without putting it into context the current economic environment and challenges.

## **Our approach**

17. Our review process focussed on the Listing Division's laid down procedures and processes as a whole, supplemented by reviews of sample cases in order to understand how the division's policies work in practice and to verify whether the division's practices follow its policies. As part of the review process, each of the Heads of Departments were asked for their assessment of their respective department's goals, objectives and priorities for 2008 and the department's success in achieving its goals, objectives and priorities.

## **Scope of our review**

18. During our annual review of the Exchange's performance in its regulation of listing matters, we focussed on reviewing the decision-making process and operational procedures in each of the operational departments in the Listing Division including the Exchange's processes for consulting the market before bringing forward proposed changes to the Listing Rules. We also considered the Listing Division's self-assessment of its performance, the challenges faced when performing its duties, the steps taken to address these challenges and areas which it considers can be improved.
19. We did not review the quality of the Listing Division's decisions during the annual review process as this forms part of our regular oversight function of the Exchange under section 5(1)(b) of the SFO. We raise and discuss with the Exchange any particular matter which comes to our attention during the course of the year as and when such matter arises.
20. In 2009, we reviewed the operations of the following departments and teams under the Listing Division in the course of 2008:
  - (a) the Initial Public Offers Department (the "IPO Department") whose primary responsibility is to process new listing applications in respect of equity securities;
  - (b) the Compliance and Monitoring Department (the "C&M Department") which is responsible for monitoring listed companies' compliance with the Listing Rules;
  - (c) the Listing Enforcement Department (the "Enforcement Department") which investigates suspected breaches of the Listing Rules and institutes disciplinary action before the Listing Committee for such breaches by companies and their directors;
  - (d) the Accounting Affairs Section of the Policy and Support Department which is responsible for the Financial Statements Review Programme. Under this programme, the Section staff review listed companies' financial statements to



monitor whether financial information disclosed is in compliance with the Listing Rules, relevant statutory requirements and accounting and auditing standards; and

- (e) the Policy Department which coordinates the development and formulation of listing policies.

21. Our review on the Exchange's processes and procedures in respect of its powers to make rules was conducted by reference to the Combined Consultation Paper on Proposed Changes to the Listing Rules published by the Exchange on 11 January 2008, which was the largest public consultation in terms of the number of proposed rule changes in 2008. The review focussed on the processes followed, and materials generated, up to 28 November 2008, the date on which the Exchange announced the relevant consultation conclusions.

### **How we conducted the assessment**

22. In conducting our assessment, we considered:

- (a) the relevant internal Exchange materials, written policies, procedures and processes documented by the relevant operational departments in the Listing Division and any general practices that have not been documented;
- (b) sample cases, including the relevant operational departments' internal reports and case files;
- (c) information we receive from the Listing Division in the ordinary course of our dealings with the Division, including its monthly report to us, internal reports and case data;
- (d) the Hong Kong Exchanges and Clearing Limited 2008 annual report, the Exchange's quarterly newsletter called the "Exchange", and the 2008 Listing Committee Report;
- (e) the Exchange's published disciplinary procedures, listing decisions, rejection letters, guidance letters, and other related documents on the HKEx website;
- (f) discussions with senior management of the relevant operational departments in the Listing Division;
- (g) comments made in interviews or discussions with the relevant case officers;
- (h) our continuing interaction with the Exchange under the Listing Matters MoU;
- (i) a survey of market participants' views to gauge the market's perception of the Exchange's performance in its listing-related functions, as mentioned below.
- (j) a survey to gauge market participants' view on the Exchange's performance in its statutory obligation under section 23 of the SFO to make rules for such matters as are necessary or desirable for the proper regulation and efficient operation of the market which it operates; and



- (k) the Listing Division's senior management's assessment of each department's effectiveness and efficiency in meeting its goals and objectives, the challenges faced and the steps taken to address these challenges.

### **Gauging market perception of the Exchange's performance**

- 23. As part of the review process, we conducted a survey of a number of market participants, including sponsors, legal advisers, accountants, investors and listed companies, and Listing Committee members, on a private and confidential basis. The purpose of the survey is to establish how they view the Exchange's performance in its regulation of listing matters and to gauge changes in the market's perception of the Exchange's performance over a period of time.
- 24. We also conducted a specific survey of market participants, which included sponsors, legal advisers, accountants, investors and listed companies, and Listing Committee members, on a private and confidential basis, to gauge their view on the Exchange's consultation process in respect of how it seeks and solicits market views during the process of making or amending the Listing Rules.

### **The assessment process**

- 25. Our assessment of the Exchange's performance and our views expressed in this report are a combination of our on-site work, our consultation with market participants and Listing Committee members and our continuing interaction with the Exchange under the Listing Matters MoU.
- 26. We held an "exit" interview with the Head of the Listing Division and discussed our findings with him.
- 27. We also interviewed the 2008 and 2009 Chairpersons of the Listing Committees.
- 28. We sought the Exchange's comments on both the factual matters set out in this report and our conclusions.
- 29. The field work and review process were completed in August 2009. Where relevant, we have also made observations of the current issues and changes in the Exchange's operational procedures and decision-making processes in 2009.



## Section 2

### Overall assessment

30. We are of the view during 2008 the Exchange's operational procedures and decision-making processes in each of the Listing Division's operational departments as described in the "Scope of our review" section above, were appropriate during the review period to enable the Exchange to discharge its statutory obligation to ensure, so far as reasonably practicable, an orderly, informed and fair market.

### Market perception of the Exchange's performance

31. We sent a questionnaire on the Exchange's performance to 157 (2008: 158) Listing Committee members and market practitioners and received 59 (2008: 61) responses. The response rate is 37.6% (2008: 38.6%).
32. The respondents were asked to rate the performance of the Exchange and each of the operating departments in the Listing Division in various key areas on a scale of 1 to 5 with "5" being wholly satisfied. Please refer to Appendix A for detailed summary of the result of the survey.
33. Overall, there is no significant change in the respondents' view of the Exchange's performance. The average overall score for 2008 is 3.6 compared with 3.7 in 2007. The respondents are generally satisfied with the efficiency and fairness of the Exchange in its vetting process.
34. There have been several calls for the Exchange to improve the transparency of its decision-making, to provide the principles behind the decisions, and to disseminate its guidance materials in a more systematic and timely manner. A few respondents suggested the Exchange should disclose on its website an organisation chart of each major department and the level of authority of each grade of staff. Several of the survey respondents also called for simplifying the listing documents and circulars to make them more user friendly and easy to understand by the general public. In June 2009, the Exchange consulted the public on measures to simplify and streamline the filing and checklist requirements for initial public offerings of equity securities<sup>3</sup>. It received overwhelming support for the proposals and implemented the rule changes on 2 November 2009<sup>4</sup>. In September 2009, the Exchange also consulted the public on proposed changes to the Listing Rules requirements for circulars and listing documents to make these documents more relevant for shareholders<sup>5</sup>.

### Observations on the Listing Division's performance

#### The Listing Division

35. As a whole, the Exchange's goals and objectives are aligned with their statutory duties under Section 21 of the SFO to ensure the operation of a fair, orderly and informed market. The Listing Division's goals, objectives and priorities for 2008 in respect of its regulation of listing related matters is to effectively administer the Listing Rules so as to discharge the

<sup>3</sup> See [http://www.hkex.com.hk/consul/paper/cp200906\\_e.pdf](http://www.hkex.com.hk/consul/paper/cp200906_e.pdf)

<sup>4</sup> See [http://www.hkex.com.hk/consul/conclusion/cp200906cc\\_e.pdf](http://www.hkex.com.hk/consul/conclusion/cp200906cc_e.pdf)

<sup>5</sup> See [http://www.hkex.com.hk/consul/paper/cp200909cr\\_e.pdf](http://www.hkex.com.hk/consul/paper/cp200909cr_e.pdf)



Exchange's statutory duty to ensure an orderly, informed and fair market under Section 21 of the SFO.

36. Each of the functional department within the Listing Division further refined the Exchange's goals and objectives to their departmental job functions. Each department's priorities for 2008 are:

- (a) The IPO Department focused its priorities to maintain the efficiency, quality and consistency of the IPO vetting process, and to enhance the transparency of the IPO vetting process to the market;
- (b) The C&M Department focused its priorities to improve the efficiency and effectiveness of its monitoring process to result in better use of regulatory resources and more efficient dissemination of listed companies' information;
- (c) The Enforcement Department's focus is to detect rule breaches in a timely manner and to apply appropriate actions to minimise the impact of breach by disclosure.

37. The Listing Division assesses its efficiency or the timeliness of its actions primarily by measuring its turnaround time. Each department has put instituted performance pledges as to when they will complete a particular task to improve and ensure efficiency:

- (a) Whilst the IPO Department has put in place its performance pledges a number of years ago, it has strived to continually improve its performance and benchmarks the time it takes to process a listing applications against the SEC. The department handled 172 listing applications in 2008, a significant increase from 149 and 129 in 2007 and 2006. However, while the number of listing applications decreased every quarter as the year progressed, the average waiting period from date of application to listing increased from 22 weeks in 2007 to 26 weeks in 2008. The department attributed the overall slow down of the listing process to poor market sentiment;
- (b) Over the past few years, the C&M Department has incrementally shifted its regulatory focus from vetting listed companies' announcements and circulars before they are issued (frequently referred to as "pre-vetting") to a post-vetting regime where the department staff post-vets these documents after they are issued<sup>6</sup>. In 2008, the department made enquiries in 8% of the post-vetted announcements, of which 93% were made within 1 business day of the announcement. Over 90% of the announcements and circulars published were commented on within 1 and 5 days respectively;
- (c) The Enforcement Department made certain changes to its supervisory and case management process to improve the focus of its investigations and to facilitate early decision-making and disposal of cases. This has resulted in reducing the backlog of cases with the ongoing investigation cases being more current. 76% of the cases handled by the department were completed within two years in 2008, of which 42% were completed within one year. 75

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<sup>6</sup> This culminated in Listing Rules changes to remove the pre-vetting requirements of announcements and circulars except for certain more significant transactions. These rules became effective from 1 January 2009.



cases (83%) were dealt with by way of warning or caution letters and closed without further action.

38. The Exchange also considers market feedback by listed companies and their advisers' experience in dealing with the Listing Division when assessing the effectiveness and efficiency of its performance and consistency of interpretation and application of the Listing Rules. The Division has sought to be more market friendly and started hosting breakfast meetings with listed companies' representatives and market practitioners with a view to initiate and maintain a dialogue with its stakeholders. Between Sept 2008 and September 2009, the Exchange has organised or planned 24 breakfast and lunch meetings with 91 market practitioners and listed companies' representatives.
39. The Listing Division regularly reviews its processes and procedures to make more effective use of its available resources and to streamline the vetting process and documentary requirements. For instance, the C&M Department has significantly reduced the number of pre-vetted announcements and circulars in 2009 from 2008. It is also reviewing its parameters when it will make enquiries on unusual price and trading volume movements so that they only make more meaningful enquiries as indicated by the hit rate (as measured by the number of suspensions and qualified announcements). Its hit rate increased from 12.5% in 2008 to 16.0% for the first five months in 2009. The Exchange has also reviewed the documentary and filing requirements for IPOs and listing of shares. It issued a consultation paper on 26 June 2009 on proposals to further streamline the filing procedures and removing requirements to file unnecessary documents under the Listing Rules.

#### Level of activities

40. The following table indicates the level of activity in the four operational departments of the Listing Division in 2006, 2007 and 2008<sup>7</sup>.

	2006	2007	2008
Number of listing applications accepted by the IPO Department	88	125	137
Number of compliance and monitoring actions handled by the C&M Department	25,591	38,265	35,215
Number of investigations handled by the Enforcement Department	216	167	171
Number of listing applications processed by the Listing Operations Department	3,177	7,426	9,312
- derivative warrants	3,094	7,025	5,031
- Callable Bull/Bear Contracts (more commonly known as CBBCs)	83	401	4,811

\* The first CBBC was listed on 12 June 2006.

41. Notwithstanding poor market sentiment in 2008, the number of listing applications accepted by the IPO Department increased by 9.6% (2007: 125; 2008: 137) from 2007 to

<sup>7</sup> Source: HKEx 2008 Annual Report, pages 37-42



2008. The average processing time for vetting listing applications prior to Listing Committee hearing increased slightly by 1 week to 17 weeks in 2008 (2007: 16 weeks). The IPO Department attributed the slight slow down of the listing process to the poor sentiment and a more difficult market environment.

42. In the course of 2008, the C&M Department saw a 7.97% (2007: 38,265; 2008: 35,215) decrease in the number of compliance and monitoring actions. This excludes the 350 written enquiries by listed companies.
43. The number of investigations handled by the Enforcement Department increased by 2.4% from 167 in 2007 to 171 in 2008. The department completed 15 disciplinary cases, issued 68 warning and caution letters (in 34 cases) and closed a further 41 cases by way of “no further action”. The enforcement actions in recent years have grown in complexity and in the numbers of directors who have been the subject of disciplinary action and sanction.

	Warning/Caution letters issued	Cases closed by way of “no further action”	Disciplinary cases	Total
2007	63	34	16	113
2008	68	41	15	124

44. The Debts and Derivatives Team saw an increase of 25.4% (2007: 7,426; 2008: 9,312) in the total number of derivative warrants and CBBCs listing applications processed. Interestingly, the number of CBBCs listing applications increased by 1,100% (from 401 in 2007 to 4,811 in 2008), whilst the number of derivative warrants listing applications decreased by 28.4% (from 7,025 in 2007 to 5,031 in 2008).
45. The Accounting Affairs Section of the Policy and Support Department reviewed 100 reports of listed companies covering the annual, interim and quarterly reports released between July 2007 and September 2008. It issued 98 letters to listed companies with more than 500 enquiries and observations. The department also issued a report on its major findings and observations from its review. A copy of the Financial Statements Review Programme Report 2009 can be accessed at <http://www.hkex.com.hk/listing/staffint/FRM2-09.pdf>.

### **Monitoring compliance and taking follow up actions**

46. The work of monitoring compliance with the Listing Rules primarily falls within the purview of the C&M Department. The department monitors compliance with listed companies’ obligations to disclose price sensitive information to the market in a timely manner and the Listing Rules generally by:
  - (a) monitoring market activities as represented by changes in a company’s share price and trading volume movements and comments and articles about a particular company in the media;
  - (b) complaints against listed companies and their directors;



- (c) post vetting of announcements, circulars and periodic disclosures published by listed companies in the form of results announcements and other documents.

47. In addition, the Exchange conducted reviews of listed companies' disclosure for their compliance with the Listing Rules on a thematic basis, focusing on compliance with particular Listing Rules. In 2008, the C&M Department reviewed listed companies' compliance with:

- (a) the annual report disclosure requirement under the Listing Rules and other related Listing Rules requirements;
- (b) in the case of newly listed companies listed in or after 2005, the additional annual report disclosure requirements and the agreed arrangements made prior their listings (e.g. non-competition undertakings by directors, controlling shareholders given to the companies prior their listings); and
- (c) the general disclosure obligation by companies with overseas listed controlling shareholders and substantial shareholders under Rule 13.09(2).

48. The Exchange can take various follow up actions depending on the nature and seriousness of the non-compliance:

- (a) cases of more serious breaches where the facts of the case raises significant regulatory impact are referred to the Enforcement Department for further investigation and action. In 2008, the C&M Department referred 86 cases for further investigation and action;
- (b) for more minor breaches where the facts do not have significant regulatory impact, the Exchange may give verbal or written guidance, warning or caution letters, and in particular circumstances general guidance to all listed companies. In 2008, the Exchange issued 284 written guidance and 68 warning and caution letters.

49. The Exchange takes a combination of guidance (including verbal and written guidance letters to individual companies, and publication of guidance materials on the HKEx website) and enforcement actions to encourage voluntary self-compliance with the Listing Rules by listed companies. In addition to the guidance material published on HKEx website, the Exchange also organises seminars and training sessions for listed companies and market participants on listing rules related matters, usually following substantial changes to the Listing Rules.

50. The Exchange has also set up a new cross-divisional Disciplinary Coordination Meeting to discuss inter-departmental issues in respect of disciplinary matters. The Enforcement Department has commented that the scope and substance of investigations have broadened in terms of complexity and have become more challenging in terms of the increase in the number of parties involved in each case. The numbers of directors, particularly non-executive directors who have been the subject of disciplinary action and sanction have grown in recent years from 67 in 2006 to 110 in 2008. Further, we noted that there have been more challenges to and appeals against the Exchange's decisions in recent years.



## Transparency

51. We have commented on the transparency of the Exchange's practices and procedures, and interpretation and application of the Listing Rules in all of our previous reports on our annual review of the Exchange's performance. The Exchange has made significant efforts over the past five years to improve the transparency of its work.
52. To provide guidance on how the Listing Rules are interpreted by the Listing Division in particular instances, the Listing Division has from time to time issued various additional guidance materials, including Listing Decisions, guidance letters, FAQs and letters to issuers. In 2004, it started to publish its rejection and guidance letters to listing applicants and listed companies, and Listing Rules changes and supplementary materials to the Listing Rules (e.g. seminar materials and frequently asked questions) on the HKEx website.
53. In 2008, the Enforcement Department started publishing listing enforcement guidance letters to provide more transparency in the decision making process relating to listing enforcement matters and the interpretation given to various provisions of the Listing Rules by the Listing Division. It has published seven letters in 2008. The Enforcement Department also launched a new series called Request for Assistance Announcements on the HKEx website seeking assistance from directors of listed companies who may be able to assist the Exchange in its efforts to clarify facts and to inform the market. It has published five of such announcements in 2008.
54. We commend the Exchange's practice of publishing more guidance materials on how it interprets and applies the Listing Rules as it raises market awareness and improves transparency. However, the benefits of this greater transparency could be enhanced if these materials were organised in a more systematic and user-friendly manner to facilitate easier search and access to all relevant material.
55. For instance, a person wishing to find out more about the regulation of and guidance about price sensitive information may miss the various documents on price sensitive information unless he is familiar with the HKEx website or conducts a thorough search through the website. Guidance materials and letters to issuers about price sensitive information are posted under four sections in the HKEx website. These documents do not always make any cross-reference to the other relevant documents and are posted in various sections of the HKEx website – under "*Regulatory Framework and Rules - Guidelines and other documents - Letter to Issuers*", "*Regulatory Framework and Rules - Guidelines and other documents*", "*Regulatory Framework and Rules - Guidelines and other documents - Staff Interpretations and Commentaries – NFA letters*", and "*News Room - 2006*".
56. A few respondents to our survey suggested that the information relating to listing matters could be presented more effectively. Suggestions made included:
  - (a) all the various guidance materials should be organised in a more user-friendly manner, e.g. consolidated into one single document and indexed according to the specific Listing Rules concerned;
  - (b) more explanation should be provided by the Exchange as to why a particular decision was made in that manner;
  - (c) some of the guidance materials should be codified and incorporated into the Listing Rules; and



- (d) the Exchange should communicate more effectively with the market regarding newly published guidance materials, e.g. provide notice to each issuer and practitioner directly by email.

57. There does not appear to be a consistent approach as to how regulatory information is published on the HKEx website. A reader who is not familiar with the format and layout in the HKEx website may find it difficult to navigate through the website to find a particular piece of information regarding listing rules related matters.

## **Recommendations**

- 58. We recommend that the Exchange reviews how to make the information it discloses about its practices, procedures and decisions more readily accessible to both experienced market professionals and less frequent users of its many disclosures.
- 59. The Exchange has taken steps in 2009 to revamp the HKEx website as regards the section containing rules and guidance on listing matters. Upon completion of this exercise, the Exchange is confident that information regarding listing related matters will be organised in a more systematic and user friendly manner. Over the medium term the Exchange is developing an email alert function to notify subscribers of the latest publications. As at the date of this report, the project is in progress.



## Section 3

### Overall assessment

60. We are of the view during 2008 the Exchange's processes and procedures in respect of its powers to make rules under section 23(2) of the SFO were appropriate to enable the Exchange to discharge its statutory obligation under section 23 of the SFO to make rules for such matters as are necessary or desirable for, inter alia, the proper regulation and efficient operation of the market which it operates.

### Background

61. On 11 January 2008, the Exchange published a Combined Consultation Paper ("Combined Consultation Paper") on proposals to address 18 substantive policy issues which covered a range of matters designed to enhance corporate governance standards as well as to facilitate the daily operations of the listed issuers and reduce costs of compliance.
62. The consultation period ended on 7 April 2008. The Exchange received a total of 105 submissions from a wide spectrum of respondents including listed issuers, market practitioners, and professional and industry associations. Except for one respondent who requested the Exchange not to publish his submission, all the submissions were posted on the HKEx website.
63. On 28 November 2008, the Exchange published the "Consultation Conclusions on Proposals in the 2008 Combined Consultation Paper" ("Consultation Conclusions") to finalise 15 of the 18 substantive policy issues. The remaining three issues, namely Issue 5 (public float), Issue 11 (general mandate) and Issue 15 (self-constructed fixed assets) remained under assessment at the time.
64. Details of the Combined Consultation Paper, the public submissions to the consultation and the Consultation Conclusions can be found on the HKEx website at: <http://www.hkex.com.hk>. A summary of the 15 policy issues and the relevant proposals that have been adopted in the Consultation Conclusions is set out in Appendix B.

### Market comments

65. We sent a questionnaire to market participants, which include sponsors, legal advisers, accountants, investors and listed companies, and Listing Committee members regarding the Exchange's performance in its consultation process. A total of 42 respondents<sup>8</sup> took part in this survey.
66. The respondents were asked to rate the performance of the Exchange in the Consultation Process on a scale of 1 to 5 with "5" being wholly satisfied. The overall score is 3.5.
67. Most respondents were satisfied with the quality of the drafting of the Combined Consultation Paper, which set out the issues in a clear and concise manner supported by comprehensive background and well researched information. The Combined Consultation Paper was written in plain language and presented in a way which was easy to understand. Most respondents pointed out that the information about overseas regulation was

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<sup>8</sup> A majority of the participants in this survey were also respondents to the Combined Consultation Paper issued by the Exchange.



particularly useful and assisted readers to form their views on an informed basis and with a broader perspective.

68. The majority of respondents commented that the Combined Consultation Paper was too lengthy containing a large amount of information which was difficult for many readers to digest for a single consultation.
69. A number of respondents considered that there was insufficient communication between the Exchange and the market especially during the early stage of the consultation process. They expected further efforts from the Exchange to raise the public awareness of the consultation.
70. Most respondents were of the view that the Exchange generally took adequate measures to facilitate the market's transition to the amended rules although some respondents considered that the lead time between the date of announcement of the Consultation Conclusions and the date of implementation of the amended rules inadequate.

### **Composite document**

71. The Combined Consultation Paper covered 18 substantive policy issues ("Issues"), which were further divided into sub-issues, to deal with more than forty proposals that had emerged over a long period. In order to maximize the efficiency in consulting the market, the Exchange grouped the different proposals into a composite document to seek market input.
72. The consultation proposals covered a wide range of matters from housekeeping amendments and the codification of existing practices to the introduction of substantive policy changes. They were arranged in a manner which followed the order of the relevant chapters of the Listing Rules to which the issues related. The controversial proposal to extend the black out period (Issue 18) was presented as the last item of the document simply due to the ordering of the relevant rules.
73. According to our survey results, the market was satisfied that the Combined Consultation Paper was a well written and comprehensive document in which the Issues were explained adequately. There were detailed background, analyses of the arguments for and against the proposals and examples of overseas market practices. The consultation questions posed in the Consultation Paper were clear and concise.
74. Notwithstanding the above, a common complaint was that the Combined Consultation Paper contained an excessive amount of information, which many readers found difficult to digest at the same time. There were concerns that the voluminous document might have submerged the more important and novel issues along with numerous other ideas and the bundling of discrete proposals into a single document might have distracted readers' focus on the more contentious topics. Some felt that the Issues should have been ordered by reference to the relative importance of the proposals.
75. We understand that it is not the Exchange's ordinary practice to group issues of different topics in a single document. The previous composite document published by the Exchange was the "Consultation Paper on Proposed Amendments to the Listing Rules relating to Corporate Governance Issues" issued in 2002 in relation to a number of corporate governance matters. In general, the Exchange issues a consultation paper to consult on a specific topic on a standalone basis.



76. The Exchange advised us that they would continue to conduct consultations on a standalone basis in future so that the relevant issues would receive wider public attention. Where a number of issues are interrelated (such as public float) they would consider adopting a thematic consultation to facilitate the market to consider the issues as a package holistically. We encourage the Exchange to give due consideration to the appropriate packaging of subjects for consultation to maximise the effectiveness of communication when seeking market input.

### **Public awareness**

77. A majority of respondents to our survey considered that there was insufficient communication between the Exchange and the market especially during the early stage of the consultation process. Although the Exchange issued a letter to all listed issuers and posted the consultation documents on the Exchange's website at the start of the consultation process, the respondents expected further efforts to raise the awareness and profile of the consultation.
78. Some survey respondents considered that the overall response rate to the Combined Consultation Paper, to which the Exchange received 105 submissions, was low, noting that only 58 issuers out of a total of more than 1,200 listed companies responded to the consultation. This is compared to a total of 167 submissions the Exchange received in its "Consultation Paper on Proposed Amendments to the Listing Rules relating to Corporate Governance Issues" issued in 2002, including responses from 110 listed issuers.
79. We note that the Exchange participated in several public seminars, including the Annual Corporate and Regulatory Update 2008 organised by the Hong Kong Institute of Chartered Secretaries in May 2008 and the forum organised by the Hong Kong Institute of Certified Public Accountants in April 2008, during and after the consultation period to explain the policy proposals in relation to the Combined Consultation Paper.
80. However, the timing of these seminars was regarded as sub-optimal since they took place towards the end of, or even after, the consultation period. It would appear that these seminars might not have aroused the same level of public attention as they would otherwise have if they had been organised by the Exchange itself. It would help enhance market awareness of, and participation in, the consultation exercises if the Exchange could conduct promotional programs during the early stage of the consultation.
81. The Exchange has advised us that it has noted comments expressed by the market after the issue of the Consultation Conclusions, and has since put in place new measures and programs to canvass views from, and interact with, the market.
82. We note that, subsequent to the review period, the Exchange organised 7 public seminars targeting a wide spectrum of audiences to explain the application and implication of the amended rules adopted in the Consultation Conclusions as well as on new policy proposals upon the issue of relevant consultation papers.
83. We understand that this is part of the Exchange's recent initiative to engage different sectors of the market via formal and informal channels in consultation, further details of which are discussed in paragraph 91 below.



## Evaluation of consultation responses and soft consultation

84. The modus operandi of the Listing Committee is largely guided by the agenda determined by the Listing Division and the information papers provided by the Listing Division. While the Listing Division is responsible for all the ground work, including identifying issues, preparing analyses, conducting research where applicable and formulating options and / or recommendations, the Listing Committee is the decision making body for listing policies. The Listing Committee makes decisions based on the information papers prepared by the Listing Division.
85. Following the close of the consultation period, for each of the Issues, the relevant Department within the Listing Division responsible for a particular proposal prepared a summary of responses for the proposal, which set out the substantive comments received from the respondents as well as the Listing Division's views and observations in light of these responses. The summary of responses was typically attached as an appendix to the listing report prepared for the Listing Committee's deliberation.
86. A majority of the comments gathered in the consultation process related to clarification of the rules, concerns about implementation and other technical and procedural issues. The Exchange has followed up on these comments to ensure that the final proposals are appropriate and practicable. The Exchange has also devised detailed guidance on practice and procedures to facilitate an orderly transition to the new regime in light of respondents' comments.
87. In relation to a number of Issues (such as Issues 3, 4, 12, 13 and 17) where a large number of respondents expressed dissenting views, the Exchange has proposed adjustments to the original proposals or devised alternative options. Nonetheless, in some of the Issues, including the proposal to extend the black out period under Issue 18, the Exchange did not seek to modify the original proposal when publishing its consultation conclusions even though full market consensus was not reached.
88. The Exchange explained that the majority of the arguments put forward by the opponents had already been identified and considered at length in the preparation of the consultation paper and there were no significant new points added to the debate.
89. While the consultation process is not meant to be one whereby responses wholly determine the eventual regulatory outcome, for proposals which encounter significant divided views, the Exchange is encouraged to undertake further enquiries to better gauge the market opposition and to clarify the proposals. Apart from the formal consultation process which solicits written submissions during the consultation period, soft consultation with the key stakeholders is an effective and useful means to collect substantive market input and comments directly, in particular on controversial issues. This would facilitate the formulation of policies which address the practical needs and concerns of the key stakeholders.
90. There was no standard policy for the Exchange to carry out soft consultation in listing policy making during the review period. The relevant team responsible for a designated policy proposal determined in the circumstances whether it was necessary to meet with interested groups.
91. The Exchange has advised us of its new initiative to engage different sectors of the market through different channels at various stages of listing policy making. In general, the Exchange will seek to conduct focus group meetings before a consultation to gather direct



feedback from key stakeholders to identify any significant issues and controversial aspects at an early stage. The Exchange will consider input from these discussions in formulating proposals for formal consultation. Based on the formal comments collected, the Exchange will finalise the proposals and, before concluding on the policy, will seek to engage the key parties and relevant groups again to ensure that the proposed final policy is appropriate and practicable.

92. We are pleased to note that, subsequent to the review period, the Exchange has stepped up its efforts to strengthen communication with the market. The Exchange has held regular breakfast and lunch meetings with listed issuers and market practitioners to solicit their views on listing-related issues. It has also organised separate sessions with focus groups or key stakeholders to discuss issues and proposals about specific subjects that the Exchange intends to work on. We understand that these exercises have been very well received by the market.

### **Checks and balances**

93. Under section 24 of the SFO, any rule amendment proposed by the Exchange is required to be approved by the SFC.
94. The Listing Division will from time to time review, and where appropriate, propose amendments to the Listing Rules. The Listing Division will seek, and the SFC staff will in response provide, policy advice and comments, in relation to the policy proposals. The Listing Division will then proceed with the policy proposals which might or might not be altered after taking into account the views and comments of the SFC staff.
95. The Listing Division has put the Combined Consultation Paper, the recommended consultation conclusions and recommended amendments to the Listing Committee for approval. The final proposals for amendments as decided by the Listing Committee were endorsed by the board of the Exchange and approved by the SFC.
96. While we have recommended that the Exchange enhances its processes to consult on controversial issues, we are of the view that the Exchange conducted the amendments to the Listing Rules as proposed in the Combined Consultation Paper in accordance with the established procedures and practices. We have not identified any exception in the operational processes and procedures under which these policy proposals were handled. As noted above the Exchange has already taken steps to address the concerns which have been raised by market participants in this area.



## Appendix A

The table below sets out the weighted average scores given by the survey respondents. The respondents were asked to rate the Exchange's performance in various key areas on a scale of 1 to 5 with "5" being wholly satisfied and "1" being wholly dissatisfied.

		2006	2007	2008	2009
<b>Views on the Exchange's performance in its regulation of listing related matters</b>					
1.	Communications to the market of the Exchange's policies and practices under the Listing Rules	3.0	3.4	3.8	3.7
2.	Timely response to the market developments	3.1	3.3	3.4	3.5
3.	Acting in the interests of the investing public	3.6	3.9	4.0	3.8
4.	Provision of a fair, orderly and efficient market for the trading of the securities	4.0	3.9	4.0	3.9
5.	Ensuring that investors are kept fully informed of price sensitive information by listed companies on a timely basis	3.9	3.9	4.0	3.8
6.	Equal and fair treatment of all holders of listed companies	3.7	3.6	3.7	3.7
7.	Quality of companies listed in 2007	3.5	3.9	3.8	3.6
<b>Views on the Listing Division's performance</b>					
8.	Consistency in decision-making	3.5	3.5	3.7	3.6
9.	Impartiality	3.9	3.8	3.8	3.8
10.	Timeliness of responses	3.3	3.6	3.6	3.6
11.	Pertinence of enquiries and comments raised during the vetting process or investigation process	3.3	3.5	3.6	3.5
12.	Experience and knowledge of the Listing Rules as regards its understanding of the policy issues behind the Listing Rules	3.6	3.9	3.9	4.0
13.	Experience and knowledge of the Listing Rules as regards its understanding of the requirements of the relevant provisions in the Listing Rules	3.9	3.9	4.0	4.1



		2006	2007	2008	2009
<b>Views on the various aspects of the IPO and C&amp;M Departments' work</b>					
14.	Handling general enquiries	3.3	3.6	3.7	3.6
15.	Handling requests for guidance on the application of a particular Listing Rule	3.1	3.5	3.5	3.6
16.	Processing applications for waivers	3.4	3.6	3.8	3.7
17.	Processing listing applications	3.5	3.6	3.8	3.7
18.	Clearing draft announcements, circulars and other corporate information	3.4	3.7	3.7	3.7
19.	Handling complaints	3.2	3.5	3.6	3.5
20.	Handling short term suspension	3.2	3.4	3.6	3.7
21.	Handling long term suspension	3.2	3.3	3.2	3.6
<b>Views on the quality of disclosure documents vetted by the Exchange</b>					
22.	Clarity of prospectuses, announcements, circulars and other corporate information	3.4	3.6	3.9	3.6
23.	The relevant documents provide sufficient information to enable investors and shareholders (where relevant) to make properly informed assessment of the relevant issuer	3.6	3.7	3.9	3.7
24.	The relevant documents are easy to understand	3.1	3.2	3.5	3.5
25.	Timely issue of announcements and circulars	3.6	3.7	3.8	3.8
<b>Views on the Exchange's performance in monitoring compliance with and enforcement of the Listing Rules</b>					
26.	Monitoring compliance with the Listing Rules by listed companies and directors	3.5	3.6	3.7	3.6
27.	Timeliness of disciplinary action taken against listed companies and directors	2.5	2.9	3.0	3.0
28.	Transparency of policy on disciplinary actions	2.8	3.1	3.3	3.3



		2006	2007	2008	2009
<b>Views on the Exchange's policies and practices under the Listing Rules</b>					
29.	The Exchange's short term suspension policy is appropriate	3.5	3.7	3.7	3.6
30.	The Exchange's long term suspension policy is appropriate	3.2	3.5	3.7	3.3
31.	The Listing Division has clearly communicated its approach to pre-vetting listed companies' announcements, circulars and listing documents.	3.1	3.4	3.9	3.6
<b>Overall average scores</b>		3.4	3.6	3.7	3.6



## Appendix B

The following is a summary of the 15 policy issues and the relevant proposals that have been adopted in the Consultation Conclusions.

Issue No.	Subject	Proposals adopted with no changes or only minor amendments	Adopted in modified form
1.	Use of websites for communication with shareholders	Yes	
2.	Information gathering powers	Yes	
3.	Qualified accountants		<i>Modified to expand the Code Provisions regarding internal controls in the Code on Corporate Governance Practices to make specific references to the responsibility of the directors to conduct an annual review of the adequacy of staffing of the financial reporting functions and the oversight role of the audit committee</i>
4.	Review of sponsor's independence		<i>Modified so that Sponsors will only need to demonstrate independence from the date of submission of Form A1 to the date of listing</i>
6.	Bonus issues of a class of securities new to listing	Yes	
7.	Review of the Exchange's approach to pre-vetting public documents of listed issuers	<i>Largely yes, with the following modifications:  Guidance devised on practice and procedures to ensure orderly transition to the new regime  Amendments made to require confirmation of Memorandum and/or Articles of Association in</i>	



Issue No.	Subject	Proposals adopted with no changes or only minor amendments	Adopted in modified form
		<i>compliance with the Listing Rules and applicable laws to be addressed by individual listed issuers</i>	
8.	Disclosure of changes in issued share capital	Yes	
9.	Disclosure requirements for announcements regarding issues of securities for cash and allocation basis for excess shares in rights issue	Yes	
10.	Alignment of requirements for material dilution in major subsidiary and deemed disposal	Yes	
12.	Voting at general meetings - Voting by poll - Notice periods	Yes	<i>Modified so that a new Code Provision instead of a listing rule is introduced to provide for a minimum notice period for convening general meetings</i>
13.	Disclosure of information about and by directors		<i>The proposed Rule is amended to make the information required under Rule 13.51(2)(a) to (e) and (g) be disclosed periodically instead of continuously</i>
14.	Codification of waiver to property companies	Yes	
16.	Disclosure of information in	Yes	

