

(I) Request for information on the mechanisms provided under the relevant statutes and rules whereby investors can seek compensation in Hong Kong for the financial losses sustained due to the default of a listed issuer incorporated in Mainland China or an overseas jurisdiction, and how the mechanisms are different before and after the commencement of the operation of the Securities and Futures Ordinance (Cap. 571)

A. Existing legislation and Securities and Futures Ordinance

Existing Legislation

1. A number of statutory provisions impose criminal liabilities on persons (including directors of listed companies) who release false or misleading information to the public. The relevant statutes also impose civil liabilities on these persons which enable investors to sue for the financial loss they have suffered as a result of relying on the false or misleading information.

Companies Ordinance (“CO”)

2. Under section 40, directors of listed companies are liable to pay compensation to investors who subscribe for shares on the faith of the prospectuses for the loss or damage caused by any untrue statement included in the prospectuses. Section 342E extends the liability to companies that are incorporated outside Hong Kong.

Securities Ordinance (“SO”)

3. Section 138 provides that a person shall not make any false or misleading statements or omissions with respect to the securities of a corporation or to the operation or performance of the corporation for the purposes of inducing the sale of the securities. “Corporation” includes companies incorporated outside Hong Kong. Contravention of section 138 is an offence.
4. Section 141 creates a statutory tort action which allows an investor who has suffered pecuniary loss as a result of a contravention under section 138 to sue for compensation by way of damages, notwithstanding that no person has been charged with or convicted of any offence under section 138. This statutory right of action is in addition to the investor’s common law rights.

Protection of Investors Ordinance (“PIO”)

5. Under section 8, an investor can sue any person who induces them to (amongst other things) buy or sell securities by any fraudulent, reckless, or negligent

misrepresentation for any pecuniary loss that the investor has sustained by reason of the investors' reliance on the misrepresentation.

6. Similar to section 141 of the SO, an investor can rely on this section notwithstanding that no person has been charged with or convicted of any offence under the PIO. This statutory right of action is also in addition to the investor's common law rights.

Common law negligent statements

7. An investor may have a common law right of action in negligence against a director who has made a negligent statement if it can be shown that in making the statement, the director was aware, or ought to have known that the investor would rely on the statement for the specific purpose for which the statement was made, and the investor suffered financial loss as a result of reliance on the statement.

Securities and Futures Ordinance ("SFO")

8. Under the SFO, a person shall not, amongst other things, disclose, circulate or disseminate false or misleading information recklessly or negligently, to induce the sale or purchase of securities. Sections 277 and 298 render such conduct market misconduct and a criminal offence respectively. Sections 281 and 305 provide that any person who has engaged in the misconduct or committed the offence is liable to pay compensation by way of damages to any other person who suffers pecuniary loss as a result of the market misconduct or the offence.
9. Section 391 imposes civil liability on a person who knowingly, recklessly or negligently makes or issues a false or misleading communication to the public, which concerns securities or futures contracts or which may affect their price. Such persons shall be liable to pay compensation to any other person for any pecuniary loss sustained as a result of the latter's reliance on the communication.
10. Under section 108, a person who makes any fraudulent, reckless or negligent misstatement by which another person is induced to (amongst other things) acquire or dispose of securities is liable to pay compensation by way of damages to the other person for any pecuniary loss that the other person has sustained as a result of the reliance by the other person on the misrepresentation.

B. Mechanism for seeking compensation

11. Investors who wish to rely on the above statutory provisions and/or their

common law rights of action to seek compensation from directors of listed companies (or related intermediaries) can make a civil claim in the Hong Kong courts. The same mechanism applies before and after the commencement of the SFO.

C. Jurisdiction/service of process

12. The Hong Kong courts have jurisdiction to entertain a claim if the defendant is served with process in Hong Kong or elsewhere as prescribed by law. Both the CO and the Listing Rules require an overseas company listed in Hong Kong to appoint and authorise a person who resides in Hong Kong to accept service of process and notices on behalf of the company. Service of process on this person is valid service. This means that an investor may not need to serve a writ on an overseas company in the country in which it is incorporated, which is a time consuming and expensive process.

(II) In connection with (I) above, how the mechanisms in Hong Kong are compared with those in other major overseas securities markets.

13. The summary below sets out the major statutory provisions in the United Kingdom, Australia and the United States that impose civil liability upon persons who are responsible for releasing false or misleading information to the public in relation to securities. As in Hong Kong, all three jurisdictions have specific provisions that deal with false or misleading statements in prospectuses. In the United Kingdom and the United States, different approaches have been adopted in relation to the dissemination of false or misleading information in a wider context but the Australian position is similar to that in Hong Kong.

The United Kingdom

The Financial Services and Markets Act 2000 (“FSMA”)

14. Section 90 of the FSMA provides that a person who has acquired securities and suffered loss in respect of them as a result of any untrue or misleading statement in or omission from the listing particulars may seek compensation from any person who is responsible for the listing particulars.
15. There are no private rights of action under the FSMA comparable to those provided in sections 281 and 305 of the Securities and Futures Ordinance. Instead, the FSMA contemplates restitution orders being granted by the court or restitution being required by the Financial Services Authority (“FSA”). In essence, the Secretary of State or the FSA may seek a restitution order under

section 382 of the FSMA if a person has breached certain requirements under the FSMA and profits have accrued to the person or another person has suffered loss as a result of the breach. If granted, such a court order would require the person who has breached the FSMA to pay restitution to the FSA which in turn must then pay the money to those whom the court has determined have suffered loss or to whom the profits are attributable.

16. In addition, under section 383 of the FSMA, the FSA can apply to court to seek an order against a person who has engaged in, or encouraged or required another person to engage in, market abuse. If granted, such order would require the person to pay restitution to the FSA. The FSA must then pay the money to those whom the court has determined have suffered loss as a result of the market abuse. The definition of “market abuse” in the FSMA is wide. The concept of market abuse is further elaborated by the Code on Market Abuse issued by the FSA. Among the matters that the FSA considers market abuse is the dissemination of false or misleading information in order to create a false or misleading impression.
17. Furthermore, under section 384 of the FSMA, the FSA may itself order a person to pay restitution where circumstances similar to those outlined in sections 382 or 383 have occurred. The FSA must first give a warning notice, and consider any representations made in response. Before exercising the power to require a person to pay restitution, the FSA must give a decision notice stating, amongst other things, the amount to be paid and the person(s) to whom the amount is to be paid. Any such decision is appealable to the Financial Services and Markets Tribunal.
18. Finally, section 150(1) of the FSMA creates a limited right of civil action for a private person who suffers loss as a result of a breach by an authorised person of a rule made under the FSMA. Under section 150(4), rules do not include the listing rules or rules concerning financial resources.

Common law negligent statements

19. This common law right of action is the same as that available to investors in Hong Kong. See existing legislation under section A above.

Australia

Corporations Act 2001 (“CA”)

20. Section 728 of the CA provides (amongst other things) that a person must not offer securities under a disclosure document if it includes a misleading or

deceptive statement or an omission. A prospectus is a type of disclosure document under the CA. By virtue of section 729, a person who suffers loss or damage as a result of a contravention of section 728 may recover the amount of loss or damage from a variety of persons. Such persons include the person who makes the offer, each director of the body making the offer, a person named in the disclosure document as a proposed director, an underwriter to the issue or sale named in the disclosure document, and the person who contravened section 728. These persons are liable for the loss or damage even if they neither committed nor were involved in the contravention.

21. Section 1041E of the CA provides that a person who does not care whether a statement or information is true or false, or who knows or ought reasonably to have known that it is false or misleading, must not make the statement or disseminate the information if it is false or misleading and is likely to induce persons to apply for, dispose of or acquire financial products. Under section 1041I, a person who suffers loss or damage by the conduct of another person who has contravened section 1041E may recover the amount of loss or damage from that person or any person involved in the contravention.

The United States

22. Investors in the US can commence class actions to seek compensation. The availability of the contingency fee arrangement between lawyers and their clients also makes it easier for investors to take action against the directors of listed companies or related intermediaries. The statutory provisions in the US should be considered against this background.
23. Both the Securities Act 1933 (“SA”) and the Securities Exchange Act 1934 (“SEA”) provide express rights of action. Each of these express rights of action specifies, in varying degrees of detail, the measure of damages that a plaintiff may recover. Other elements of the cause of action (e.g. the defences available to the defendant and the applicable statute of limitation) are also spelt out. One example is section 12 of the SA which provides that a person who offers or sells a security by means of a prospectus or oral communication which includes an untrue statement or omission is liable to pay compensation to the person purchasing such security from him/her.
24. However, the bulk of US private securities litigation involves claims based on the alleged filing of misleading financial statements by public companies. These claims are normally brought under section 10(b) of the SEA in combination with rule 10b-5 made by the US Securities and Exchange Commission under the authority of section 10. These are general market misconduct provisions and do not expressly provide for a private remedy.

However, the federal courts have determined that there is an implied private right of action which enables persons who have suffered loss because of such misleading financial statements to recover damages from those who have breached these provisions.

(III) Elaboration on the roles and responsibilities of each relevant party in the vetting and approving of issuers incorporated in Mainland China and overseas jurisdictions and in the monitoring of compliance of these issuers with the Listing Rules.

25. As the frontline regulator, the Stock Exchange of Hong Kong Limited (the Stock Exchange) is primarily responsible for providing a fair, orderly and efficient market for the trading of securities. The Stock Exchange carries out this function by making and enforcing the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the Listing Rules including both Main Board rules and GEM rules) pursuant to the Stock Exchanges Unification Ordinance (SEUO). The Securities and Futures Commission (the SFC) is responsible for approving the Listing Rules and overseeing the work of the Stock Exchange.
26. In the securities regulatory framework, the Listing Rules form part of the non-statutory requirements applicable to issuers and listed securities. Other non-statutory requirements include the Code on Takeovers and Mergers and the Code on Share Repurchases. There are also statutory requirements applicable to issuers and listed securities. They include the Companies Ordinance, Securities (Disclosure of Interests) Ordinance and Securities (Insider Dealing) Ordinance. Persons contravening relevant statutes may incur criminal as well as civil liabilities.
27. Against this background of statutory and other non-statutory requirements, the Listing Rules apply to all issuers alike. They apply as much to issuers incorporated in Hong Kong as they do to issuers incorporated in Mainland China and overseas jurisdictions, subject to the additional requirements and modifications designed to bring about similar shareholders' protection as available under the Companies Ordinance.

In the vetting and approving of listing applications

28. Information is provided to the Stock Exchange in this process by inclusion of the information or reports or expert statements in the prospectus; or by submission of relevant information or supporting documents to the Stock Exchange. Directors are primarily responsible for the information relating to

the issuer. The sponsor has a responsibility to satisfy itself that the issuer is suitable to be listed and to ensure that all material statements in the prospectus have been verified. Other experts take responsibility for the statements in their reports or views included in the prospectus.

29. The following sets out the primary roles and responsibilities of parties involved in the listing process under the Listing Rules:

Directors of issuer

30. The directors of an issuer, collectively and individually, are responsible for the accuracy of the information contained in the prospectus. They are obliged to make a number of specific material statements for disclosure purposes. Among others, a working capital statement, a statement of no material adverse change in the financial or trading position of the issuer since the date of the last published financial statements, and a statement in respect of material litigation and potential claims against the issuer.

Sponsor

31. A new applicant must be sponsored by a merchant bank or other similar person which will be able to give the new applicant impartial advice. The sponsor must observe the guidelines set out in the model code for sponsors issued by the Stock Exchange (a copy of which is set out in the Listing Rules). The purpose of the model code is to give guidance to sponsors on the Stock Exchange's minimum expectations of the sponsor's role.
32. In addition to the model code for sponsors, a sponsor is subject to the Corporate Finance Adviser Code of Conduct of the SFC. This code sets the benchmark against which a licensed corporate finance adviser's fitness and properness will be measured.¹

¹ Under the Corporate Finance Adviser Code of Conduct, a sponsor or financial adviser in other corporate finance transactions (Corporate Finance Adviser) should, in the preparation of any document for public dissemination, use all reasonable efforts to assist its client in ensuring that the document is prepared to the required standard and no relevant information has been omitted or withheld. Where information and representations are provided by a client for incorporation in a public document or submission to the regulators, the Corporate Finance Adviser should advise its client to take all reasonable steps to ensure, and obtain confirmation from the client, that the information and representations provided are true, accurate, complete and not misleading, and that no material information or facts have been omitted or withheld. Where reliance on the work of independent experts or other professionals is planned (other than the work performed by a property valuer in respect of a valuation of a real property, legal advisers in respect of legal advice rendered by them, and accountants in respect of the audit of results and accountants' reports derived therefrom), the Corporate Finance Adviser should, among others, review and discuss with its clients and the experts or other professionals the qualifications, bases and assumptions adopted by the experts or other professionals in the course of their work and satisfy itself that the qualifications, bases and assumptions have been made with due care and objectivity and on a reasonable basis.

33. The sponsor to an issuer should be closely involved in the preparation of the prospectus and in ensuring that all material statements therein have been verified and that it complies with the Listing Rules and all relevant legislation. In discharging their responsibility², some sponsors engage other professionals to provide advice and guidance. The sponsor has a responsibility under the Listing Rules to satisfy itself, on all available information, that the issuer is suitable to be listed, and that its directors appreciate the nature of their responsibilities and can be expected to honour their obligations under the Listing Rules. In addition, the sponsor takes responsibility under the Companies Ordinance for a statement it makes in the prospectus, if any.

Reporting accountants

34. The reporting accountants are responsible for the accountants' report on the profits and losses, assets and liabilities of the issuer, and other financial information on the issuer for inclusion in the prospectus.
35. All accountants' reports must be prepared by independent professional accountants³. The reporting accountants are required to draw up the financial history of results and the statement of assets and liabilities included in the accountants' report in accordance with the standards approved by the Hong Kong Society of Accountants (HKSA) or promulgated by the International Accounting Standards Board.
36. The reporting accountants are also responsible for:

² The duties of a sponsor include, among others:

- preparing the new applicant for listing;
- signing and lodging the formal application for listing together with all supporting documents with the Stock Exchange;
- dealing with the Stock Exchange on all matters arising in connection with the application which are raised by the Stock Exchange; and
- providing a comfort letter in respect of the profit forecast of an applicant for inclusion in the prospectus, in which the sponsor states its opinion that the forecast has been made after due and careful enquiry.

³ Under the Listing Rules, reporting accountants are required to be:

- qualified under the Professional Accountants Ordinance for appointment as auditors of a company;
- independent both of the issuer and of any other company concerned to the same extent as that required of an auditor under the Companies Ordinance and in accordance with the guideline on independence (Statement 1.203) issued by the Hong Kong Society of Accountants; and
- a firm which normally has an international name and reputation and is a member of a recognised body of accountants.

- expressing an opinion as to whether or not the relevant information gives, for the purposes of the accountants' report, a true and fair view of the results for the period reported on and of the assets and liabilities at the end of that period⁴;
 - expressing an opinion on the appropriateness of adjustments⁵ made to historic financial statements for the purposes of the prospectus; and
 - providing a comfort letter in respect of the profit forecast of an applicant for inclusion in the prospectus. The comfort letter states their opinion that, so far as the accounting policies and calculations are concerned, the forecast has been properly compiled in accordance with the bases and assumptions made by the directors, and is presented on a basis consistent in all material respects with the accounting policies normally adopted by the issuer as set out in the accountants' report.
37. In addition, reporting accountants may but are not always requested to perform additional verification work on behalf of the sponsor and issuer in relation to financial disclosures, such as work on indebtedness and change in financial position. The Listing Rules do not require reporting accountants to perform these additional tasks.
38. The reporting accountants should perform their work by exercising due skill, care and diligence as required by the professional standards of HKSA. The work performed by reporting accountants is subject to the quality standards and monitoring of HKSA.

Legal advisers

39. The Listing Rules do not require legal advisers to provide any specific opinions. However, the circumstances of the issuer may be such that the Stock Exchange seeks for confirmation and/or opinions in respect of certain disclosures. By custom and practice, legal advisers are expected to give opinions on whether the issuer and its operations comply with all relevant applicable law and regulations.

⁴ Also stating that the accountants' report has been prepared in accordance with the Auditing Guideline – Prospectuses and the reporting accountant (Statement 3.340) issued by HKSA.

⁵ In preparing the accountants' report, the reporting accountants should make such adjustments (if any) as are in their opinion appropriate for the purposes of the accountants' report and state therein that all adjustments considered necessary have been made, or (where appropriate) that no adjustments were considered necessary. This written statement (the statement of adjustments) is required to be made available for public inspection, and should be signed by the reporting accountants

40. Legal advisers are qualified solicitors under the Legal Practitioners Ordinance holding a practising certificate. Their professional conduct is governed by The Hong Kong Solicitors' Guide to Professional Conduct issued by The Law Society of Hong Kong.
41. They take responsibility, among others, for their views included in the prospectus in respect of:
- validity of permits and/or licences required for operations of the issuer's group;
 - validity and enforceability of material contracts;
 - compliance with applicable tax law; and
 - legal title to properties.
42. Legal advisers should perform their work with due care, skill and competence. Their work is subject to the monitoring of the relevant professional body including The Law Society of Hong Kong.

Valuer

43. Valuations of and information on all the issuer's interests in land or buildings ("properties") are required to be included in the prospectus under the Listing Rules. Independent qualified valuers provide reports on properties for publication in the prospectus. The Listing Rules address questions of interpretation of independence and the qualification of valuers.
44. Valuation reports must contain all material details of the basis of valuation which must follow the "Hong Kong Guidance Notes on the Valuation of Property Assets" published by The Royal Institution of Chartered Surveyors (Hong Kong Branch) and The Hong Kong Institute of Surveyors.

Stock Exchange

45. Listing applications are first reviewed by the Listing Division of the Stock Exchange. The focus of the Stock Exchange's approval is on ensuring that an applicant meets all the prescribed initial listing criteria and the adequacy of disclosure. In assessing whether the relevant initial listing criteria are met, the Listing Division attaches great importance to the role and responsibility of the sponsor, the views and reports of other professional advisers and the due diligence work they performed in relation to independent verification of the

accuracy of the information contained in the prospectus. In reviewing the prospectus and the supporting documents, the Listing Division would raise questions as appropriate about adequacy of the information disclosed and satisfaction of initial listing criteria, obtain additional assurances from relevant professional advisers in respect thereof as necessary and require additional disclosure in the prospectus, if appropriate.

46. After the queries raised have been satisfactorily addressed, the Listing Division prepares a report and makes recommendations on the application to the Listing Committee for consideration. Save for the Chief Executive of HKEx, who is an ex officio member, members of the Listing Committee are independent external people from the market. They comprise investors, listed company representatives, stock brokers, investment bankers, and legal and accounting professionals. The Listing Committee considers whether the issuer has met the initial listing criteria and whether disclosure is adequate, and then approves or rejects the application and imposes further conditions for listing where appropriate. The listing applicant has a right to request a review of any decision made by the Listing Committee.

In the monitoring of ongoing compliance with the Listing Rules

47. In response to enquiries made by the Stock Exchange for the purpose of ensuring compliance with the Listing Rules or in the process of vetting announcements, circulars or listing documents (such as a rights issue prospectus), listed issuers and their advisers provide information or supporting documents to the Stock Exchange. Directors are primarily responsible for the information relating to the issuer. Other experts take responsibility for the accuracy and reliability of their reports or opinions included in the announcements, circulars or listing documents.
48. The following sets out the primary roles and responsibilities of parties involved in ongoing compliance with the Listing Rules:

Directors of issuer

49. The board of directors of an issuer is collectively responsible for the management and operations of the issuer and is accountable to the issuer's shareholders. Compliance with the Listing Rules requires directors to fulfil their fiduciary duties and to exercise due skill, care and diligence in carrying out their duties. More specifically, every director signs an undertaking to the Stock Exchange to comply to the best of his ability with the Listing Rules; and to use his best endeavours to procure that the issuer shall comply with the Listing Rules.

50. It is implicit that in order to comply with the disclosure obligations placed on issuers, the board must ensure that the issuer has adequate financial and compliance reporting procedures in place. In addition, the board must ensure that the information it discloses to the market is complete and not false, deceptive or misleading.

Auditors

51. Each set of financial statements presented in an annual report, listing document or circular shall provide a true and fair view of the state of affairs of the listed issuer and of the results of its operations and its cashflows. The minimum disclosure requirements are set out in the Listing Rules.
52. Annual accounts of a listed issuer are required to be audited⁶ and conform with accepted accounting standards⁷.
53. In respect of major transactions and very substantial acquisitions undertaken by a listed issuer, accountants' reports are also required on the profits and losses, assets and liabilities of, and other financial information on the business or company to be acquired by the issuer for inclusion in listing documents or circulars.

Sponsor

54. It is recommended good practice for an issuer on the Main Board to retain the services of a sponsor for at least one year following listing although there is no requirement in the Listing Rules. A PRC issuer is obliged to retain the

⁶ Under the Listing Rules, the annual accounts must be audited by a person, firm or company who must be a practising accountant of good standing and independent of the issuer to the same extent as that required of an auditor under the Companies Ordinance and in accordance with the statements on independence issued by the International Federation of Accountants and, if the issuer's primary listing is or is to be on the Stock Exchange, must be either:-

- qualified under the Professional Accountants Ordinance for appointment as an auditor of a company; or
- a firm of accountants acceptable to the Stock Exchange which has an international name and reputation and is a member of a recognised body of accountants.

⁷ The accepted accounting standards are either:

- accounting standards approved by HKSA and laid down in the Statements of Standard Accounting Practice issued from time to time by HKSA; or
- International Accounting Standards as promulgated from time to time by the International Accounting Standards Board.

The accounts must be audited to a standard comparable to that required by HKSA or by the International Auditing Practices Committee of the International Federation of Accountants.

services of a sponsor for at least one year following listing to provide advice on compliance with the Main Board Rules, and to act as the issuer's principal channel of communication with the Stock Exchange.

55. All GEM listed issuers are required to appoint a sponsor for the duration of their business objective period (that is the remainder of the financial year after listing and the two subsequent financial years). The sponsor's role is of particular importance to the successful operation of GEM since the sponsor is expected to advise the issuer on its responsibilities under the GEM Rules and to guide and assist such issuer to comply with and discharge its responsibilities.
56. Where listed issuers on the Main Board do not retain the services of a sponsor after listing, they may engage a financial adviser to advise them on individual transactions regarding compliance with the Listing Rules. Such adviser is subject to the Corporate Finance Adviser Code of Conduct of the SFC.

Legal advisers

57. The Listing Rules do not require legal advisers to provide any specific opinions in respect of transactions undertaken by listed issuers. However, the circumstances of the issuer may be such that the Stock Exchange seeks for confirmation and/or opinions in respect of certain disclosures in the announcements, listing documents or circulars. In such circumstances, legal advisers are expected by custom and practice to give opinions on relevant legal issues.
58. They take responsibility, among others, for their views included in the announcements, listing documents or circulars.

Valuer

59. In the case of an acquisition or realisation of any property, or a company whose assets consist solely or mainly of property, which constitutes at least a major transaction, then a valuation of and information on such property must be included in the circular issued to shareholders in connection with the acquisition or realisation.
60. In the case of an acquisition or a realisation of any property from or to a connected person, a valuation of and information on such property must be included in any circular issued to shareholders in connection with the acquisition or realisation.

61. The requirements on valuers and valuation reports are similar to those applicable to listing applications.

Stock Exchange

62. Through the Listing Rules, the Stock Exchange seeks to promote timely and accurate disclosure by issuers of all relevant information as well as to ensure even dissemination of such information to the market.
63. To monitor compliance with the Listing Rules, the Stock Exchange reviews media reports, monitors share price/turnover movements, vets listed issuers' announcements and circulars before they are issued, monitors financial reporting, reviews complaints about issuers and/or their management and considers disclosures made by whistleblowers.

Enforcement actions and sanctions

64. Where there are grounds to suggest that an issuer has failed to comply with the Listing Rules, the Stock Exchange will look into the matter and consider what actions to take, including disciplinary action against the issuer and its directors.
65. In addition, where there are grounds for concern about the performance of a sponsor, the Stock Exchange will look into the matter and consider what actions to take, including disciplinary action under the Listing Rules. As sponsors are firms licensed by the SFC, the Stock Exchange may also refer its concerns to the SFC.
66. The SEUO provides that the Stock Exchange shall refer breaches of the Listing Rules which are alleged to have been committed by a solicitor or professional accountant in private practice; and which may also constitute a breach of duty imposed by law or by virtue of rules of professional conduct, to The Law Society of Hong Kong or HKSA for determination of whether to make a finding, impose a penalty or sanction or take other disciplinary action. In this connection, the Stock Exchange has entered into a memorandum of understanding with The Law Society of Hong Kong, which provides a framework for referral of appropriate cases. From time to time, the Stock Exchange may also refer problematic cases involving the conduct of accountants and failure to comply with accounting standards to HKSA for investigation. For overseas professional advisers, the Stock Exchange may refer cases to overseas securities regulators and/or professional societies for appropriate action.

67. There are a number of ordinances providing legislative backing for enforcement of legal obligations. For example, under the Companies Ordinance, where a prospectus issued in Hong Kong includes any untrue statements, any person who authorised the issue of the prospectus shall be potentially liable to imprisonment and a fine⁸ and to pay compensation to all persons who have sustained a loss or damage⁹. In respect of the aforesaid civil liability, the persons liable include, among others, directors of the issuer and an expert who made an untrue statement as an expert and gave consent to the issue of the prospectus.
68. Under the SEUO, it is an offence if a person knowingly provides to the Stock Exchange, in its regulatory capacity, any information and documentation that is false or misleading in a material particular¹⁰.
69. While the Stock Exchange does not have statutory power, if there is a material breach of the Listing Rules, the relevant parties may also have breached relevant applicable law. In such case, the law enforcement bodies such as the SFC and CCB may prosecute them for relevant offences pursuant to their statutory powers. Civil actions may also be taken against the relevant parties.
70. Under the dual filing system as proposed in the consultation paper of the SFC published in May 2002, filing of documents relating to a listing applicant or listed issuer must be made to both the Stock Exchange and the SFC. It will be a criminal offence for any inaccuracy contained in the documents so filed. Such enhanced statutory backing, coupled with the Stock Exchange's plan to strengthen the sponsor regime, will help provide a more robust regulatory

⁸ Such person shall be liable unless he proves either that the statement was immaterial or that he had reasonable grounds to believe and did up to the time of the issue of the prospectus believe that the statement was true.

⁹ Such claimants having subscribed for any shares on the faith of the prospectus may claim for the loss or damage they may have sustained by reason of any untrue statement included in the prospectus.

¹⁰ Under SEUO, it is an offence if a person, in purported compliance with a requirement to provide information imposed by the ordinance, provides to the Stock Exchange any information that is false or misleading in a material particular and he knows it to be false or misleading in a material particular; or is reckless as to whether it is false or misleading in a material particular. It is also an offence if a person in other circumstances provides to the Stock Exchange a record or other document that is false or misleading in a material particular and

- either he knows it to be false or misleading in a material particular; or is reckless as to whether it is false or misleading in a material particular; and
- the record or other document is provided in connection with the performance of a function of the Stock Exchange under the ordinance; and
- he has received prior written warning from the Stock Exchange to the effect that provision of false or misleading information shall render him liable for prosecution for an offence.

regime. The dual filing system is targeted for implementation on commencement of the SFO in April 2003.

(IV) The responsibilities of each relevant party in respect of a substantiated breach of the Listing Rules by a listed issuer incorporated in Mainland China and overseas jurisdictions, and whether there are possible circumstances under which no enforcement action or litigation can be taken in Hong Kong in respect of such a listed issuer.

71. The Stock Exchange pursues breaches of Listing Rules against all issuers alike, regardless of their place of incorporation.
72. Where an issuer has failed to comply with the Listing Rules, the Stock Exchange would look into the matter and consider what actions to take, including disciplinary action against relevant parties. The disciplinary procedures are clearly prescribed in the Listing Rules to ensure that a fair hearing will be given to all parties concerned.
73. As the board of directors of an issuer is collectively responsible for the management and operations of the issuer, they take responsibility for the issuer's breach of the Listing Rules. More specifically, each and every director has signed an undertaking to the Stock Exchange to comply to the best of his ability with the Listing rules; and to use his best endeavours to procure that the issuer shall so comply.
74. In general, where there have been frequent changes to the board of directors and the directors reside outside Hong Kong, it may be difficult to locate the directors responsible for the relevant breach even with the assistance of new management rendering enforcement action problematic.
75. While the Stock Exchange does not have statutory power, if there is a material breach of the Listing Rules, the relevant parties may also have breached relevant applicable law, the major provisions of which have been discussed in (III) above. In such case, the law enforcement bodies such as the SFC and CCB may prosecute them for relevant offences pursuant to their statutory powers. Civil actions may also be taken against the relevant parties.

(V) In the above processes, the extent of reliance on the information and assurances from the relevant authority of Mainland China or an overseas jurisdiction, and whether there are possible circumstances under which the Stock Exchange of Hong Kong Limited and/or the Securities and Futures Commission can only rely on the information or assurances from such an authority

76. The Listing Rules require that the issuer must be duly incorporated or otherwise established under the laws of the place where it is incorporated or otherwise established and must be in conformity with those laws and its memorandum and articles of association or equivalent documents. To demonstrate that listing applicants are able to comply with this requirement, it is customary for legal advisers of a listing applicant to confirm that the issuer and its operations comply with relevant applicable law and regulations. In this respect, issuers are required to furnish supporting documents including the approval or “no-comment” letter from the CSRC¹¹ where they have substantial operations or shareholding interests in Mainland China, and business licences/approvals granted by relevant authorities.
77. Where there are concerns about the legality of transactions undertaken by listed issuers, the Stock Exchange would request issuers to seek similar confirmations from their legal advisers and ensure that issuers disclose the relevant opinions to the market.
78. The Listing Rules govern the obligations of issuers to the Stock Exchange. As such, the Stock Exchange primarily relies on the information and assurances provided by issuers. Where an issuer has a primary listing on another exchange, it would be subject to regulation by the other relevant regulatory authorities as well as the Stock Exchange. Issuers may also operate in overseas jurisdictions. Accordingly, there are arrangements to facilitate regulatory co-operation on policy matters in general and sharing of information on specific cases where necessary.
79. In respect of issuers incorporated in Mainland China and issuers with substantial operations in Mainland China, there is a memorandum of regulatory co-operation in place among the Stock Exchange, the Securities and Futures

¹¹ It is HKEx’s understanding that the CSRC requires, under Mainland regulations, approval of listing overseas (including Hong Kong) in respect of H-share issuers incorporated in Mainland China. The CSRC also requires filing of PRC legal opinions in respect of issuers incorporated overseas but with substantial operations in Mainland China seeking a listing overseas (including Hong Kong), in response to which they may or may not issue a “no-comment” letter. It is also HKEx’s understanding that the relevant application for approval or PRC legal opinion submitted to the CSRC would cover issues like validity of licences. However, the CSRC clearance simply means that the CSRC approves, or has no comments on, the issuer’s proposed listing overseas.

Commission, the CSRC and the two Mainland exchanges. Under this memorandum, there is a mechanism to maintain regular liaison with HKEx's Mainland counterparts. In respect of issuers incorporated overseas, the Stock Exchange through its membership of international organisations and entering into of memoranda of understanding with individual exchanges has appropriate arrangements for sharing of regulatory information and obtaining co-operation from regulators in overseas jurisdictions.

(VI) In view of the importance of the role and responsibilities of the sponsor of a listed issuer, whether the regulatory authorities are satisfied with the current arrangements for ensuring that the sponsor has the financial capability, competence etc. to fulfil its responsibilities

80. Securities regulators have been taking various initiatives to ensure that the quality of sponsors and financial advisers are at a high standard and in line with international practice.
81. GEM rules prescribe standards of competence and experience for sponsors and their staff as well as capital requirements for sponsors¹². GEM sponsors, after admitted as GEM sponsors, are subject to annual review by the Stock Exchange. Any disciplinary action taken against them would be taken into account in an annual review of eligibility.

In 2000 the Stock Exchange and the SFC initiated two separate consultation exercises aimed at strengthening the sponsor regime in Hong Kong. The Stock Exchange proposed to introduce requirements on Main Board sponsors and financial advisers to mirror substantially the requirements of GEM rules. The market responses were in general not supportive of the proposal and the proposal was not introduced subject to further review.

82. In response to its consultation the SFC introduced, as a first step, the Corporate Finance Adviser Code of Conduct which is used as a benchmark against which a licensed corporate finance adviser's fitness and properness will be measured.
83. In May 2002, the SFC published for public consultation legislation to regulate effectively information disclosed by listed companies and listing applicants. Under the proposed dual filing system, filing of documents relating to a listing applicant or listed issuer must be made to both the Stock Exchange and the SFC. It will be a criminal offence for any false or misleading disclosure contained in

¹² Factors in considering sponsor's eligibility include, among others, licensing requirements, corporate finance experience of the firm and its supervisors, capital requirements, and past records of public censure and other disciplinary action.

the documents so filed with the SFC. Such enhanced statutory backing is expected to come into operation on the commencement of the SFO in April 2003. This, coupled with the Stock Exchange's plan to strengthen the sponsor regime, will help provide a more robust regulatory regime.

84. In July 2002, the Stock Exchange also announced its work on proposals establishing a more uniform approach regarding sponsors for both the Main Board and GEM as it was noted that the requirements in relation to sponsors for the Main Board were less detailed than those for GEM.
85. It is proposed to set out some uniform and minimum standards, and the duties and responsibilities expected of corporations and individuals engaged in sponsorship activities and the provision of corporate finance advisory services.
86. In order to ensure that similar sets of standards are imposed on sponsors for both the Main Board and GEM, the review on the requirements for sponsors and financial advisers will include both the Main Board rules and GEM rules. Findings of this review will form the basis of a further HKEx consultation paper on proposed listing rules regarding sponsors and financial advisers.
87. It is intended that this consultation paper will be released for market consultation in the first half of 2003.

Source:

Securities and Futures Commission (for paragraphs 1 – 24)
Hong Kong Exchanges and Clearing Limited (for paragraphs 25 – 87)
6 January 2003