

Bills Committee on Securities and Futures (Amendment) Bill 2011
Definition of “Price Sensitive Information”

Purpose

This paper provides a comparison of the definition of “price sensitive information” (“PSI”) under the Securities and Futures (Amendment) Bill 2011 (the Bill) with those under (a) the relevant legislation in comparable jurisdictions; and (b) the existing regulatory regime in Hong Kong including provisions on insider dealings under the Market Misconduct regime and the prevailing Listing Rules of the Stock Exchange of Hong Kong Limited (“SEHK”). It also responds to suggestions on measures to facilitate compliance with specific reference to points raised about changes in orders or contracts as part of a corporation’s daily transactions.

International Comparison

2. The table at Annex A sets out the definition of “PSI” under the proposed statutory regime under the Bill and the statutory requirements in the United Kingdom, Australia and Singapore.

3. It is noted that all the three comparable jurisdictions adopt a principle-based instead of a prescriptive approach in defining PSI and none of them use quantitative criteria for determining whether a piece of information is PSI. This is also the case for the European Union in general. The key elements of definition of PSI proposed under the Bill and those used in the comparable jurisdictions are very similar. Such key elements are –

- Information concerning the listed corporation and its securities
- Not generally available/ known
- If available/known, would likely to materially affect the price of the listed securities.

4. A suggestion was raised in the one of the deputations that PSI should be defined more simply and broadly as “all material information related to the issuer (subject only to safe harbours)”. This suggestion would amount to a very broad definition bordering on a catch all situation. As seen from Annex A, no other comparable jurisdiction adopts such a broad concept and it would pose compliance challenges.

Ready Reference from Existing Local Regimes

(a) Current Provisions on Insider Dealings

5. The proposed section 307A(1) of the Bill adopts the definition of “relevant information” currently used in the “insider dealing” regime in section 245 of the Securities and Futures Ordinance (“SFO”) (Annex A). As such, PSI to be disclosed will be the same set of information currently prohibited from being used for dealing in the securities of the listed corporation concerned, and such information would be known as “inside information”.

6. The market is familiar with the concept of “relevant information” as it has been used for some 20 years since the enactment of the now repealed Securities (Insider Dealing) Ordinance. The familiarity with the concept should facilitate listed corporations in determining whether a particular piece of information is PSI and hence the need for disclosure. The consultation paper published by the Financial Services and the Treasury Bureau in March 2010 listed insider dealing cases that had been handled by the Insider Dealing Tribunal (“IDT”) and the Market Misconduct Tribunal (“MMT”). Details of these cases are readily available in the websites of the Tribunals. During the consultation conducted in March to June 2010, respondents generally supported the adoption of the concept of “relevant information” under the insider dealing regime in the Bill. This approach is also same as that adopted by the European Union (including the United Kingdom), which has developed the insider dealing regime and the disclosure regime on the basis of the same concept of “inside information”.

(b) Listing Rules

7. The current Listing Rule 13.09 (Annex B) also adopts the “materiality” test. However, compared with the current definition of PSI adopted under Listing Rule 13.09, the scope of the proposed definition of PSI in the Bill is narrower. The major difference is that the former also covers information on any major new developments in the group’s sphere of activity (i.e. 13.09(1)) and any information necessary to avoid the establishment of a false market (i.e. 13.09(1)(b)). The Securities and Futures Commission (“SFC”) and the SEHK will work to revise Listing Rules 13.09 after the passage of the Bill.

Practical References and Guidelines

8. As regards whether information relating to the day-to-day operation of a listed corporation would be regarded as PSI, we note that the IDT report on Hanny Holdings Limited stated that, “earlier tribunals have cited with approval the distinction drawn in some texts between, on the one hand, day to day activities which may, by normal analysis and deduction, be an indicator of the health of a company and, on the other hand, important, singular events (or contemplated events) which are likely to change a company’s course”.¹

9. Similarly, we believe that the bulk of the information that “officers” have in the daily operations of a company would generally not be PSI and “officers” are not expected to come into knowledge of significant or dramatic events on a day-to-day basis. Having said that, “officers” should recognise that ordinary day-to-day activities might transform into irregular or unforeseen events due to the changes in the elements comprising these activities or the occurrence of matters impacting upon these activities. What begins as a normal day-to-day

¹ The Tribunal quoted the saying of the UK Minister of Trade, when addressing the insider dealing provisions in the proposed Companies Act of 1980 on Parliament that, “I do not believe that the general body of information which a businessman has about his business for long periods in the year falls into the bracket of “unpublished price sensitive information”. Of course he knows more about his business than people outside do, but the kind of knowledge we are after is knowledge of dramatic events, major happenings, and things which will transform the company’s prospects. When someone has information about such matters, he should not be dealing. But I do not believe that day-to-day running of major enterprises is full of day-to-day dramas.”

activity may become into a non-routine or irregular event that changes the course of a company's business. If an "officer" reasonably expects that the event, once stripped of its confidentiality, would be likely to materially affect the share price, the disclosure duty arises.

10. Since the business nature, market capitalization and financial situation of each listed corporation is different, and market sentiment and sensitivity also change over time, it is unadvisable to adopt a single bright-line test or numerical figure for all listed corporations for determining PSI for continuous disclosure purposes.²

SFC's Guidelines to Facilitate Compliance

11. To facilitate compliance, the SFC will publish Guidelines on Disclosure of Inside Information, setting out the key aspects of what has been viewed by the IDT and MMT as constituting "relevant information" in assisting understanding of PSI and encourage compliance. A copy of the latest draft guidelines has already been passed to Members for reference via LC Paper No. CB(1)135/11-12. Specifically, paragraph 34 of the draft Guidelines gives a non-exhaustive list of common examples of events or circumstances where a corporation should consider whether a disclosure obligation arises. These are copied at Annex C for Members' reference.

12. In addition, the SFC will provide consultation service to assist corporations understand how to apply the disclosure provisions initially for a period of 2 years upon the enactment of the Bill.

Financial Services and the Treasury Bureau Securities and Futures Commission November 2011

² It is noted that under the Mainland Listing Rules, if a company expects its forthcoming annual results (a) change from a profit last year to a loss this year; (b) increase or decrease by more than 50% compared to last year's results; or (c) turnaround from a loss last year to a profit this year, the company has to issue a profit announcement within one month after the year end. Nevertheless, the Mainland Listing Rules retain a general obligation where a company needs to disclose on a timely basis any information the Exchange or the company considers that will have a relatively significant impact (較大影响) on the price of the securities.

Comparison of the Definition of “Price Sensitive Information”

Hong Kong (Existing under s.245 of SFO)	Hong Kong (Proposed)	United Kingdom	Australia	Singapore
<p>Relevant information, in relation to a corporation, means specific information about –</p> <ul style="list-style-type: none"> (a) the corporation; (b) a shareholder or officer of the corporation; or (c) the listed securities of the corporation or their derivatives, <p>which is not generally known to the persons who are accustomed or would be likely to deal in the listed securities of the corporation but which would if it were generally known to them be likely to materially affect the price of the listed securities</p>	<p>Inside information, in relation to a listed corporation, means specific information that –</p> <ul style="list-style-type: none"> (a) is about – <ul style="list-style-type: none"> i. the corporation; ii. a shareholder or officer of the corporation; or iii. the listed securities of the corporation or their derivatives; and (b) is not generally known to the persons who are accustomed or would be likely to deal in the listed securities of the corporation but would if generally known to them be likely to materially affect the price of the listed securities. 	<p>In relation to qualifying investments, or related investments, which are not commodity derivatives, inside information is information of a precise nature which –</p> <ul style="list-style-type: none"> a) is not generally available, b) relates, directly or indirectly, to one or more issuers of the qualifying investments or to one or more of the qualifying investments, and c) would, if generally available, be likely to have a significant effect on the price of the qualifying investments or on the price related investments. 	<p>any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity’s securities, provided that the information is</p> <ul style="list-style-type: none"> a) information which is not generally available; and b) information that a reasonable person would expect, if it were generally available, to have a material effect on the price or value of the securities of the entity; 	<p>any information known to the issuer concerning it or any of its subsidiaries or associated companies which: -</p> <ul style="list-style-type: none"> a) is necessary to avoid the establishment of a false market in the issuer’s securities; or b) would be likely to materially affect the price or value of its securities.

Extract of Listing Rule 13.09 of Stock Exchange of Hong Kong

13.09 (1) Generally and apart from compliance with all the specific requirements in this Chapter, an issuer shall keep the Exchange, members of the issuer and other holders of its listed securities informed as soon as reasonably practicable of any information relating to the group (including information on any major new developments in the group's sphere of activity which is not public knowledge) which:—

- (a) is necessary to enable them and the public to appraise the position of the group; or
- (b) is necessary to avoid the establishment of a false market in its securities; or
- (c) might be reasonably expected materially to affect market activity in and the price of its securities.

Extract of SFC's Latest Draft Guidelines

Examples of Possible Inside Information concerning the Corporation

34. There are many events and circumstances which may affect the price of the listed securities of a corporation. It is vital for the corporation to make a prompt assessment of the likely impact of these events and circumstances on its share price and decide consciously whether the event or the set of circumstances constitutes inside information that needs to be disclosed. The following are common examples of such events or circumstances where a corporation should consider whether a disclosure obligation arises.

- Changes in performance, or the expectation of the performance, of the business;
- Changes in financial condition, e.g. cashflow crisis, credit crunch;
- Changes in control and control agreements;
- Changes in directors and (if applicable) supervisors;
- Changes in directors' service contracts;
- Changes in auditors or any other information related to the auditors' activity;
- Changes in the share capital, e.g. new share placing, bonus issue, rights issue, share split, share consolidation and capital reduction;
- Issue of debt securities, convertible instruments, options or warrants to acquire or subscribe for securities;
- Takeovers and mergers (corporations will also need to comply with the Takeovers Codes that include specific disclosure obligations);
- Purchase or disposal of equity interests or other major assets or business operations;
- Formation of a joint venture;
- Restructurings, reorganizations and spin-offs that have an effect on

the corporation's assets, liabilities, financial position or profits and losses;

- Decisions concerning buy-back programmes or transactions in other listed financial instruments;
- Changes to the memorandum and articles (or equivalent constitutional documents);
- Filing of winding up petitions, the issuing of winding up orders or the appointment of provisional receivers or liquidators;
- Legal disputes and proceedings;
- Revocation or cancellation of credit lines by one or more banks;
- Changes in value of assets (including advances, loans, debts or other forms of financial assistance);
- Insolvency of relevant debtors;
- Reduction of real properties' values;
- Physical destruction of uninsured goods;
- New licenses, patents, registered trademarks;
- Decrease or increase in value of financial instruments in portfolio which include financial assets or liabilities arising from futures contracts, derivatives, warrants, swaps protective hedges, credit default swaps;
- Decrease in value of patents or rights or intangible assets due to market innovation;
- Receiving acquisition bids for relevant assets;
- Innovative products or processes;
- Changes in expected earnings or losses;
- Orders received from customers, their cancellation or important changes;

- Withdrawal from or entry into new core business areas;
- Changes in the investment policy;
- Changes in the accounting policy;
- Ex-dividend date, changes in dividend payment date and amount of dividend; changes in dividend policy;
- Pledge of the corporation's shares by controlling shareholders; or
- Changes in a matter which was the subject of a previous announcement.

35. However, the above list of events or circumstances should not be treated as definitive in terms of meaning that the information in question, if disclosed, will have a material price effect. It is a *non-exhaustive and purely indicative* list of the type of events or circumstances which might constitute inside information. The fact that an event or a set of circumstances does not appear on the list does not mean it cannot be inside information. Nor does inclusion in the list mean that it automatically is inside information. It is the materiality of the information in question that needs to be considered. Information which is likely to materially affect the price of the securities should be disclosed.

36. Moreover, corporations should take into account that the materiality of the information in question will vary widely from entity to entity, depending on a variety of factors such as the entity's size, its course of business and recent developments, the market sentiment about the entity and the sector in which it operates. What may constitute material information to one party to a contract may be immaterial to another party. A cancellation of credit line by a bank which is material to an entity facing liquidity problems may be immaterial to another entity which is highly liquid.