

Consultation Conclusions on the Proposed Statutory Codification of Certain Requirements to Disclose Price Sensitive Information by Listed Corporations

Financial Services and the Treasury Bureau

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Objectives

- Cultivate a continuous disclosure culture among listed corporations
- Enhance market transparency and quality
- Sustain HK's position as China's global financial centre and a premier capital formation centre

Consultation Results - Overview

- Consultation launched on 29 March 2010
- Received 110 written submissions
- About half from listed corporations
- Others mainly from trade bodies of the financial services, accounting and legal sectors, as well as investor/consumer groups
- Conducted 8 briefings: 460 attendees

Consultation Results - Overview

- Respondents generally supported the objective of cultivating a continuous disclosure culture among listed corporations
- Certain professional bodies of the legal, accounting and financial services sectors and consumer group supported the proposed statutory regime
- Listed corporations generally did not object to a statutory regime, but suggested revised proposals on liabilities
- About 20% of the written submissions (mostly from listed corporations) did not support a statutory regime
- Improved the legislative proposal in light of comments received: strike a reasonable balance between upholding investor protection and facilitating compliance by listed corporations

Price Sensitive Information (“PSI”)

- “Inside information” - borrowed from the concept of “relevant information” in the insider dealing regime (used since 1990)
- Same as the approach adopted by UK and other EU countries
- Generally agreed among respondents

Disclosure Requirements

- Listed corporation must disclose PSI as soon as practicable that has come to its knowledge
- Some respondents suggested: “as soon as reasonably practicable”; immediate disclosure
- **We will amend to “as soon as reasonably practicable” to allow time for listed corporations to verify the facts and seek professional advice as appropriate and reasonable**

Safe Harbours

- (A) when the disclosure would constitute a breach against an order made by a Hong Kong court or any provisions of other Hong Kong statutes;
 - (B) when the information is related to incomplete negotiations or proposals the outcome of which may be prejudiced if the information is disclosed prematurely
 - (C) when the information is a trade secret
 - (D) when the Government's Exchange Fund or a central bank provides liquidity support to the listed corporation
- Use of safe harbours are subject to the confidentiality pre-requisites
 - Securities and Futures Commission ("SFC") may prescribe further safe harbours through subsidiary legislation

Safe Harbours

- Respondents generally agreed that the four safe harbours were necessary
- **In light of respondents' comments, we will make the following amendments –**
 - **Confidentiality pre-requisites will not be applicable to Safe Harbour (A)**
 - **Remove “outcome of which may be prejudiced if the information is disclosed prematurely” from Safe Harbour (B), to make it more consistent with existing Listing Rules and takeovers regime**
 - **Where a piece of information has been leaked and hence a safe harbour falls away, it would be a defence to prove that the corporation has taken reasonable measures to monitor the confidentiality and it has made disclosure as soon as reasonably practicable when it became aware of the leakage**

Waiver

- SFC may grant waiver if face disclosure prohibition arising from court orders or legislation of a jurisdiction outside Hong Kong
- Generally welcomed by respondents. Some proposed that the allowable scope of the waiver should also cover rules made by administrative agencies
- **Will extend the grounds for applying for waivers, to cover restrictions imposed by a law enforcement authority of a place outside Hong Kong or a government authority of a place outside Hong Kong exercising a power conferred by the legislation of that place**

Obligations of the Listed Corporations

- Listed corporation must disclose PSI that has come to its knowledge. “Come to knowledge”: if an “officer” has, or ought reasonably to have, come into possession of the information
- SFO already defined an “officer” to mean a director, manager or secretary of, or any other person involved in the management of, the corporation
- Some respondents suggested removing “ought reasonably to have come into possession”
- **Intention is to avoid evasion of the disclosure obligation in 2 circumstances: arguing that the PSI has been channelled to the “officers” but has not been read; or deliberately keeping PSI away from being accessed by “officers”**
- **Under common law, an “officer” has to exercise reasonable care in the discharge of his duties owed to a company**

Obligations of “Officers”

- “Officers” must take all reasonable measures from time to time to ensure that proper safeguards exist to prevent a breach in relation to the corporation of a disclosure requirement in relation to the corporation
- Some respondents concerned that “officer” is too broad
- **Cover directors and high-level individuals responsible for managing the listed corporation, not middle management or low ranking staff**
- **SFC would explain in guidelines**

What Constitute Breach of Disclosure Requirement

- Listed corporations would be in breach in case of non-disclosure or late disclosure
- Individual “officers” would be in breach if -
 - The listed corporation has breached the disclosure requirements; and
 - The breach in relation to the listed corporation is a result of the intentional, reckless or negligent act of the individual “officer” or the individual “officer” has not taken reasonable measures to prevent the breach in relation the listed corporation
- Some respondents suggested that “officers” should not be held liable so long as they have acted in good faith in considering whether a piece of information should be disclosed
- **Threshold of “in good faith” too low. Should consider whether they have acted reasonably (objective test)**
- **A breach on the part of an individual “officer” does not amount to a breach on the part of other “officers”, so long as they have acted reasonably and have taken reasonably measures to prevent the listed corporation from breaching the disclosure requirement**

Guidelines

- SFC will promulgate guidelines on what may constitute inside information and when would safe harbours be applicable, to facilitate compliance
- SFC to initially provide informal consultation service for 12 months
- Respondents generally welcomed SFC promulgate guidelines. Some requested a longer or permanent consultation service
- **SFC will revise its guidelines and update them from time to time, and issue FAQs**
- **SFC's informal consultation service be extended to 24 months initially**

Civil Sanctions

- The Market Misconduct Tribunal (“MMT”) may impose-
 - (1) regulatory fine up to \$8 million on the listed corporation and/or each director
 - (2) disqualification of the “officer” from being involved in the management of a listed corporation for up to five years
 - (3) “cold shoulder” order on the “officer” for up to five years
 - (4) “cease and desist” order on the listed corporation or “officer”
 - (5) a recommendation order that the “officer” be disciplined by any body of which that person is a member
 - (6) payment of costs of the civil inquiry and/or the SFC investigation by the listed corporation or “officer”

Civil Sanctions

- Persons suffering pecuniary loss as a result of others breaching the disclosure requirements may rely on the results of the MMT proceedings to take civil actions for compensation
- Most of the respondents agreed with a civil regime, and having MMT to handle the cases
- Diverse views on the ceiling for the regulatory fine: \$3 million to unlimited fine level
- Some listed corporations commented that the various orders were strong measures

Civil Sanctions

- Ceiling of \$8 million allows sufficient scope for MMT to determine the exact level of fine
- New MMT powers for PSI cases (added with reference to remedies imposed by Listing Committee):
 - Order an “officer” to undergo training
 - Order a corporation to appoint an independent professional adviser to review its compliance procedure
 - Order a corporation to appoint an independent professional adviser to advise on compliance matters

Enforcement

- SFC as the enforcement authority, with existing investigation power under SFO
- SFC may institute proceedings before the MMT direct, without referring a case to the Financial Secretary
- General consensus among respondents for SFC to be the enforcement authority
- Some respondents concerned that giving SFC direct access to MMT would amount to loss of checks and balances
- **MMT proceedings already provide for appropriate checks and balances**
- **Streamlined procedures can enhance the effectiveness of enforcement**

Effects of the Revised Proposal

- Facilitate listed corporations in compliance
 - Revised timing of disclosure
 - Revised safe harbours, extended grounds for applying for waivers
 - Explain the coverage of “officer” in SFC’s guidelines
- No compromise of investor protection
 - “Officers” should act reasonably, to adopt objective test instead of the subjective test of “in good faith”
- Reinforce the cultivation of a continuous disclosure culture among listed corporations
 - Added training and appointment of independent professional advisers as remedies

Compared with Existing Listing Rules of the Stock Exchange of Hong Kong

- (1) Create a formal statutory obligation for compliance
- (2) Provide a clear set of PSI disclosure requirements with obligations and safe harbours explicitly set out in the law and SFC's guidelines to facilitate compliance
- (3) Allow SFC to resort to its powers under the SFO to conduct more effective investigation
- (4) Enable all alleged breaches to be heard by an independent statutory body (the MMT)
- (5) Allow a streamlined process for handling alleged breaches

Compared with Existing Listing Rules of the Stock Exchange of Hong Kong

- (6) Enable persons suffering pecuniary loss to rely on the results of the MMT proceedings to take civil actions for compensation
- (7) Impose a wide range of statutory civil sanctions
 - Demonstrate our commitment to enhancing market transparency and quality
 - Enhance HK's position as China's global financial centre

Legislative Timetable

- Plan to introduce a bill into Legislative Council to amend the SFO in the 2010/11 legislative session



Thank You

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