

LEGISLATIVE COUNCIL BRIEF

SECURITIES AND FUTURES ORDINANCE (CAP. 571)

SECURITIES AND FUTURES (SHORT POSITION REPORTING) (AMENDMENT) RULES 2016

INTRODUCTION

At its meeting on 22 February 2016, the Securities and Futures Commission (“SFC”), under section 397(1) and (2) of the Securities and Futures Ordinance (Cap. 571) (“SFO”), after consultation with the Financial Secretary, made the Securities and Futures (Short Position Reporting) (Amendment) Rules 2016 (“the Amendment Rules”), at **Annex**.

BACKGROUND AND ARGUMENT

2. Following the collapse of Lehman Brothers in September 2008, regulators in a number of overseas markets took steps to enhance the effectiveness of regulation of short selling as part of the global regulatory reforms to restore investor confidence and to reduce systemic risk. In view of the global regulatory developments, the SFC made the Securities and Futures (Short Position Reporting) Rules (Cap. 571AJ) (“SPR Rules”), which came into effect on 18 June 2012, to introduce a short position reporting regime in Hong Kong.

3. The object of the SPR Rules is to impose a duty on a person who has a net short position in specified shares that amounts to or exceeds certain thresholds to report the short position to the SFC on or before a reporting deadline.

4. The reporting threshold is 0.02% of the market capitalisation of the listed company concerned or \$30 million, whichever is lower. In normal market conditions, short positions are reported on a weekly basis. In contingency situations, the SFC is empowered to require daily reporting on short positions.

5. The current short position reporting regime covers the constituent stocks of the Hang Seng Index, Hang Seng China Enterprises Index and other financial stocks specified by the SFC (collectively referred to as “specified shares”). As of 30 October 2015, a total number of 127 stocks were subject to short position reporting.

Expanding the scope of reporting

6. As of 30 October 2015, there were 889 securities that could be short sold under the rules of The Stock Exchange of Hong Kong Limited, known as Designated Securities.¹ In general, the list of Designated Securities comprises stocks and collective investment schemes (“CISs”) which include exchange traded funds, Real Estate Investment Trusts and other Unit Trusts/Mutual Funds.

7. The 127 specified shares that were subject to short position reporting as of 30 October 2015 were a subset of the 889 Designated Securities. Under the SPR Rules, reporting on short positions in the remaining 762 Designated Securities is not required.

8. In view of the fact that short selling activities of these 762 Designated Securities have grown to become significant, the SFC proposed to expand the scope of the short position reporting regime to cover all Designated Securities in order to enhance the transparency and monitoring of short selling activities in light of their potential implications for the orderliness and stability of markets.

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

9. For those Designated Securities that are CISs, which include open-ended CISs, the SFC proposed that the reporting threshold trigger will be set at the \$30 million threshold only. It would be impractical to set the reporting threshold for CISs by reference to market capitalisation since the value of market capitalisation of open-ended CISs can change frequently as a result of the daily creation and redemption process.

¹ In general, only securities with sufficient liquidity will be accepted as Designated Securities. The current list of Designated Securities include constituent stocks of equity indices, exchange traded funds, underlying stocks of options and futures contracts as well as other stocks with a relatively large market capitalization and turnover volume.

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

10. There are some Designated Securities which are traded in a currency other than Hong Kong dollars (i.e. US dollars or Renminbi) or in multiple currencies. To determine the value of a net short position in relation to those Designated Securities of which the trade price is expressed in a currency other than Hong Kong dollars, the SFC proposed that the closing price should first be converted into Hong Kong dollars at the rate of exchange for that currency which is the buying rate for telegraphic transfers on the reporting day, as determined by the Hong Kong Monetary Authority.²

Reporting in contingency situations

11. In the event that daily reporting of short position is required in contingency situations, the SFC proposed that daily reporting would only apply to those Designated Securities as determined by the SFC (“Daily Reporting Securities”). A public notice identifying the Daily Reporting Securities will be provided by the SFC before daily reporting takes effect. Depending on the prevailing market situation, the SFC may decide to stop daily reporting on one or more of the Daily Reporting Securities and the SFC will issue a public cessation notice accordingly.

Reporting through SFC designated electronic system

12. Currently, short positions are reported through an online communication system designated by the SFC, namely the Short Position Reporting Service. The SFC proposed to provide for more than one electronic system that may be designated for reporting.

THE AMENDMENT RULES

13. The main provisions of the Amendment Rules are as follows -
- (a) Rule 3(2) repeals the definition of business day in rule 2 of the SPR Rules so that the term has the meaning given by section 1 of Part 1 of Schedule 1 to the SFO.

² This arrangement is also the current practice in relation to the existing specified shares that are denominated in Renminbi.

- (b) For the purpose of expanding the scope of securities in respect of which positions must be reported—
 - (i) rule 3(1) amends the definition of specified shares in rule 2 of the SPR Rules by providing that it includes interests in a CIS;
 - (ii) rule 4(1), (2), (3) and (4) amends rule 3 of the SPR Rules by providing for separate thresholds for positions in shares and interests in CISs; and
 - (iii) rule 9 amends Schedule 1 to the SPR Rules by providing that specified shares are those that the Stock Exchange Company determines (under its rules) to be “designated securities”.
- (c) Rule 4(6) amends rule 3(2) of the SPR Rules by adding rule 3(2)(d) which provides for the calculation of positions in specified shares where the closing price of the specified shares is not expressed in Hong Kong dollars.
- (d) The SPR Rules require notifications to be submitted to the SFC by means of an online communication system designated by the SFC. Rule 7 amends rule 5 of the SPR Rules by providing that the SFC may designate one or more electronic systems. Rules 5(4) and 6 make consequential amendments to the requirements in the SPR Rules relating to submitting notifications to the SFC.
- (e) The SPR Rules empower the SFC, in a contingency situation, to require daily reporting of reportable short positions by publishing a daily reporting requirement notice. Rule 8 amends rule 7(2) and (3) of the SPR Rules by adding a requirement that the daily reporting requirement notice must identify the specified shares to which the notice relates. Rule 5(2) makes a consequential amendment to rule 4(3) of the SPR Rules.

PUBLIC CONSULTATION

14. The SFC conducted a public consultation on expanding the

scope of short position reporting and on the draft Amendment Rules in November 2015. A majority of the financial institutions and professional associations that responded to the consultation supported the proposal while there were individual commentators who raised objection and proposed to do away with the SPR Rules altogether or to raise the reporting threshold. After considering all the comments from the market, the SFC concludes that expanding the scope of short position reporting to all Designated Securities is appropriate for the Hong Kong market. The Panel on Financial Affairs of the Legislative Council (“LegCo”) was also briefed on the matter on 15 February 2016. Members raised no objection to the proposal.

FINANCIAL AND STAFFING IMPLICATIONS

15. There are no financial or staffing implications for the Government or the SFC.

LEGISLATIVE TIMETABLE

16.	The legislative timetable is as follows -	
	Publication in the Gazette	26 February 2016
	Tabling at LegCo	2 March 2016

COMMENCEMENT

17. The Amendment Rules will come into operation on 15 March 2017.

PUBLICITY

18. A press release will be issued by the SFC.

ENQUIRIES

19. Any enquiries on this brief may be addressed to Mr. Rico Leung, Senior Director, or Ms. Tan Poh Hiang, Senior Manager, of the Supervision of Markets Division of the SFC at 2231 1357 and 2231 1815 respectively.

The Securities and Futures Commission

24 February 2016

Securities and Futures (Short Position Reporting) (Amendment) Rules 2016

(Made by the Securities and Futures Commission under section 397(1) and
(2) of the Securities and Futures Ordinance (Cap. 571) after consultation
with the Financial Secretary)

1. Commencement

These Rules come into operation on 15 March 2017.

2. Securities and Futures (Short Position Reporting) Rules amended

The Securities and Futures (Short Position Reporting) Rules (Cap. 571 sub. leg. AJ) are amended as set out in rules 3 to 9.

3. Rule 2 amended (interpretation)

(1) Rule 2, definition of *specified shares*, after “corporation”—

Add

“, or interests in a collective investment scheme (whether or not the interests are shares in a corporation),”.

(2) Rule 2—

Repeal the definition of *business day*.

4. Rule 3 amended (reportable short position)

(1) Rule 3—

Repeal subrule (1)

Substitute

“(1) In these Rules, a person has a reportable short position—

(a) in any specified shares, except specified shares which are interests in a collective investment scheme, if the person has a net short position value in the specified shares that is equal to or more than the threshold specified in subrule (2)(b); or

(b) in any specified shares which are interests in a collective investment scheme, if the person has a net short position value in the specified shares that is equal to or more than the threshold specified in subrule (2)(ba).”.

(2) Rule 3(2)(b)—

Repeal

“subrule (1)”

Substitute

“subrule (1)(a)”.

(3) After rule 3(2)(b)—

Add

“(ba) in subrule (1)(b), the threshold in relation to a reporting day is \$30 million;”.

(4) Rule 3(2)(c), after “is”—

Add

“, subject to paragraph (d)”.

(5) Rule 3(2)(c)—

Repeal the full stop

Substitute a semicolon.

(6) After rule 3(2)(c)—

Add

“(d) if, in relation to any specified shares, the closing price referred to in paragraph (c)(i) or (ii) is expressed in a currency other than Hong Kong dollars, the closing price is taken to be its equivalent in Hong Kong dollars on the reporting day, calculated using the rate of exchange for the currency that is the buying rate for telegraphic transfers at the commencement of business on the reporting day, as determined by the Monetary Authority.”.

5. Rule 4 amended (reportable short positions to be notified to Commission)

(1) Rule 4(2), after “this rule”—

Add

“and rule 4A”.

(2) Rule 4(3), after “shares”—

Add

“to which the notice relates”.

(3) Rule 4(4), after “this rule”—

Add

“and rule 4A”.

(4) Rule 4(8)—

Repeal

“subrule (9)”

Substitute

“rule 4A”.

(5) Rule 4—

Repeal subrule (9).

6. Rule 4A added

After rule 4—

Add

“4A. Submitting notification to Commission

Notification to the Commission required under rule 4(2) or (4)—

(a) must contain—

(i) particulars identifying the person who has a reportable short position in specified shares;

(ii) particulars of the net short position value and number of specified shares comprised in the reportable short position; and

(iii) the name and stock code of the specified shares comprised in the reportable short position; and

(b) is to be regarded as duly submitted only if it is submitted—

(i) by means of an electronic system designated by the Commission under rule 5(1); and

(ii) in accordance with the directions and instructions relating to the system referred to in rule 5(2).”.

7. Rule 5 substituted

Rule 5—

Repeal the rule

Substitute

“5. Commission may designate electronic system

- (1) The Commission may, for the purposes of these Rules, designate one or more electronic systems.
- (2) Where the Commission designates an electronic system under subrule (1), it must as soon as reasonably practicable publish, in the manner it considers appropriate, directions and instructions relating to the use of, and the submission of notifications under rule 4(2) or (4) by means of, that system.”.

8. Rule 7 amended (daily reporting requirement notice)

- (1) After rule 7(2)(a)—

Add

“(ab) must identify the specified shares to which the notice relates;”.

- (2) Rule 7(3), after “positions”—

Add

“in one or more of the specified shares to which the notice relates”.

- (3) Rule 7(3), after “effect”—

Add

“in relation to the specified shares identified in the cessation notice”.

9. Schedule 1 substituted

Schedule 1—

Repeal the Schedule

Substitute

“Schedule 1

[r. 2]

Specified Shares

Shares, or interests in a collective investment scheme, which are determined by the Stock Exchange Company to be a “designated security” in accordance with the rules of the Stock Exchange Company.”.



Ashley Alder

Chief Executive Officer,
Securities and Futures Commission

22 February 2016

Explanatory Note

The object of the Securities and Futures (Short Position Reporting) Rules (Cap. 571 sub. leg. AJ) (*SPR Rules*) is to impose a duty on a person who has a net short position in specified shares that amounts to or exceeds certain thresholds to report the short position to the Securities and Futures Commission (*Commission*) on or before a reporting deadline.

2. Rule 3(2) repeals the definition of *business day* in rule 2 of the SPR Rules so that the term has the meaning given by section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571).
3. For the purpose of expanding the scope of securities in respect of which positions must be reported—
 - (a) rule 3(1) amends the definition of *specified shares* in rule 2 of the SPR Rules by providing that it includes interests in a collective investment scheme;
 - (b) rule 4(1), (2), (3) and (4) amends rule 3 of the SPR Rules by providing for separate thresholds for positions in shares and interests in collective investments schemes; and
 - (c) rule 9 amends Schedule 1 to the SPR Rules by providing that specified shares are those that the Stock Exchange Company determines (under its rules) to be “designated securities”.
4. Rule 4(6) amends rule 3(2) of the SPR Rules by adding rule 3(2)(d) which provides for the calculation of positions in specified shares where the closing price of the specified shares is not expressed in Hong Kong dollars.
5. The SPR Rules require notifications to be submitted to the Commission by means of an online communication system designated by the Commission. Rule 7 amends rule 5 of the SPR

Rules by providing that the Commission may designate one or more electronic systems. Rules 5(4) and 6 make consequential amendments to the requirements in the SPR Rules relating to submitting notifications to the Commission.

6. The SPR Rules empower the Commission, in a contingency situation, to require daily reporting of reportable short positions by publishing a daily reporting requirement notice. Rule 8 amends rule 7(2) and (3) of the SPR Rules by adding a requirement that the daily reporting requirement notice must identify the specified shares to which the notice relates. Rule 5(2) makes a consequential amendment to rule 4(3) of the SPR Rules.