

**Response to Ms Alice Y L Chan, Department of Professional Legal  
Education, Faculty of Law,  
University of Hong Kong**

**Schedule 1 – Amendments updating the prospectus regime**

**I. Offers not subject to the prospectus regime (Section 2(1) and the  
17<sup>th</sup> Schedule)**

Sections 3 and 4 of the proposed 17<sup>th</sup> Schedule

The monetary threshold prescribed for the maximum size of an offer has been proposed on the basis of comments received during the public consultation on the proposed amendments to the Companies Ordinance (CO) to facilitate offers of shares and debentures in March 2003. In response to market's concerns about the legal, accounting and other costs associated with making an offer, we have proposed to pitch the threshold at HK\$5 million.<sup>1</sup>

2. We will consider proposing drafting amendments to the Bill to the effect that the monetary thresholds referred to in sections 3 and 4 of the proposed 17<sup>th</sup> Schedule would include their equivalent in other currencies.

Section 7 of the proposed 17<sup>th</sup> Schedule

3. We consider that the wording in the UK Financial Services and Markets Act 2000 (FSMA) referred to by Ms Alice Chan does not entirely meet our objective. The phrase “the securities are shares and are offered free of charge to all or any of the holders of shares in the issuer” under FSMA would not extend to an offer of shares pursuant to a scrip dividend scheme which is covered by section 7 of the proposed 17<sup>th</sup> Schedule. This is because such an offer is arguably not free of charge to shareholders – they forego a cash dividend in return for shares.

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<sup>1</sup> The threshold suggested by the market ranges from HK\$5 to 10 million. The market also notes that in Australia, the similar threshold is AUD 2 million (approximately HK\$10 million) (see section 708 of Australia's Corporations Act).

## Section 8 of the proposed 17<sup>th</sup> Schedule

4. The proposed “qualifying persons” exemption is intended to benefit offeror companies which reward persons who could safely be assumed to have a high level of knowledge about the offeror and its group of companies. Consultants contracting with the issuer should be grouped under the exemption directed at employees because it is not uncommon for services to be provided by a consultant instead of an employee, and it would be arbitrary to provide an exemption in respect of one and not the other. For example, in the insurance industry, it is common that an insurance company does not maintain a so-called “employer-employee” relation with its insurance agents. These agents instead work as “consultants” to the insurance company.

5. As regards the identity of the “consultant”, the normal rules about legal persons will apply. If the contract for services is with a company or a firm, the legal person would be the company or the firm - not all the directors and officers of the company/partners or associates of the firm; if with an individual, the legal person would be the individual - not all his/her partners or associates.

## Section 11a(ii) of the proposed 17<sup>th</sup> Schedule

6. We are giving detailed consideration to comments raised by Ms Chan on offers in respect of an exchange of debentures and would revert to Bills Committee.

## **II. SFC’s powers of exemption and amendment (Sections 38A and 360)**

7. Under the proposed new section 38A(2), the Securities and Futures Commission (SFC) may, by order published in the Gazette, and subject to such conditions (if any) as SFC thinks fit and specified in the notice, exempt any class of companies, or prospectuses issued by companies, from any or all of the requirements of the relevant provisions (as specified in the proposed section 38A(4)). Under the proposed section 38A(5), SFC may, by order published in the Gazette, amend subsection (4) which specifies the “relevant provisions”. Under the new section 360(6),

SFC may, by order published in the Gazette, amend the Third, Seventeenth, Eighteenth, Nineteenth, Twentieth, Twenty-first and Twenty-second Schedules. In all the above cases, an order published in the Gazette will be subsidiary legislation subject to negative vetting by the Legislative Council. In addition, under the new section 360(7), where SFC proposes to make an order under section 360(6), it must publish a draft of the proposed order for public consultation. Therefore, any proposals by SFC to increase the coverage of exemptions that can be granted or to amend the prospectus-related Schedules are subject to public consultation and examination by the legislature.

8. One of the regulatory objectives of SFC is to provide protection for members of the public investing in or holding financial products (section 4(c) of the Securities and Futures Ordinance (Cap. 571) (SFO)), and one of its functions is to secure an appropriate degree of such protection (section 5 of SFO). Before proposing any amendment to the list of CO requirements that may be exempted by an order published in the Gazette, SFC will have to take into consideration its statutory regulatory objectives and functions.

### **III. Construction of offerings to the public (Section 48A)**

9. Section 48A(1) states that any reference in the Ordinance to offering to the public is construed as including an offering to any section of the public (and therefore subject to certain rules). Subsection (2) says that “domestic” offers are not offers to the public (and therefore are not subject to the prospectus-related provisions.) The proposed 17<sup>th</sup> Schedule introduces 12 new categories of offers that are not subject to the prospectus-related provisions.

10. The purpose of the proposed section 48A(3) is to make it clear that the 17<sup>th</sup> Schedule does not displace the general rule in section 48A(1), that offers made to any section of the public are subject to certain provisions. But that will only be the case if an offer does not fall within an exemption, such as the 17<sup>th</sup> Schedule, or sections 48A(2) or 343(2). The 17<sup>th</sup> Schedule does not limit section 48A(1) in those cases where the 17<sup>th</sup> Schedule does not apply.

#### **IV. Overall standard of disclosure in prospectus (Paragraph 3 of the 3<sup>rd</sup> Schedule)**

11. The existing prospectus content requirements in the 3<sup>rd</sup> Schedule do not differentiate between equity and debt issues. All issues, regardless of whether they are equity or debt issues, have to comply with the relevant disclosure requirements set out in the 3<sup>rd</sup> Schedule. What may be seen as relevant information for an investor in equity (e.g. profitability of a company) may not be viewed as such by a debt investor who may be more concerned about the sufficiency of reserves of the company in determining its repayment ability. The proposed amendment to paragraph 3 is to allow the regulator to tailor disclosure requirements to a particular offer, having regard to the nature of the company and securities being offered, etc.

12. This proposal is part of our efforts to facilitate offers of shares and debentures. Investors would also benefit from this initiative as they will not be overloaded with information irrelevant to the making of informed investment decisions.

#### **V. Definition of “prospectus” (Section 2(1))**

13. The word “company” is capable of meaning an overseas company in the context of the definition of “prospectus”. Ms Chan’s suggestion of replacing the word “company” in the proposed definition of “prospectus” with the phrase “body corporate or corporation” may have the effect of applying the relevant CO prospectus provisions to corporations which are currently outside the prospectus regime under CO (e.g. bodies incorporated by statute or charter).

Financial Services and the Treasury Bureau  
Securities and Futures Commission

October 2003