APPENDIX E

EXAMPLES OF COMMENTS RAISED BY SFC ON DRAFT PROSPECTUSES AND MARKETING LEAFLETS OF CERTAIN SERIES OF MINIBONDS AND CONSTELLATION NOTES

Prospectus

(a) Minibonds

Series 1

1. SFC expressed concerns on (i) whether investors would need information on the underlying security guarantor to enable them to form a view as to its creditworthiness, and (ii) given the "structured and derivative" nature of the product, whether investors would need to know and monitor the price of the underlying security. The website where information in relation to the underlying security guarantor could be accessed was subsequently disclosed in the prospectus. Investors were also informed in the prospectus that up-to-date price information in respect of the underlying security was available on display on Bloomberg by inputting its unique international securities identification number ("ISIN").

2. Following SFC's query, the issuer set out in the prospectus the priority of claims following early termination of the notes and enforcement of the collateral.

3. Following SFC's request, the issuer enhanced the disclosure on the swap guarantee and highlighted for investors' attention that the swap guarantee comprised a guarantee only in respect of the swap counterparty's payments under the swap agreement and not the notes or the underlying securities.

4. Following SFC's query, the issuer disclosed in the prospectus that any enforcement of the collateral would be taken by the trustee directly (not the individual noteholders).

5. Upon SFC's query on the proposed offer of notes, the issuer represented that for the purpose of disclosure, it should be assumed that the public in general would be approached but it would become clearer once the marketing of the notes commenced.

6. Following SFC's query, the issuer set out in the prospectus the standard investor's confirmations and undertakings and also highlighted certain information on application procedures.

Series 10 (first Minibond series where collateral may comprise CDOs)

7. Different from previous series of Minibonds, this series of notes would not be secured on notes guaranteed by LBHI. Instead, it would be secured on AAA rated securities purchased with the proceeds from the issue of the notes.

   At SFC's request, the issuer agreed:-

   - to put on display the terms and conditions of the underlying security; and
   - to provide more detailed disclosure on the package of information relating to the underlying security that would be available on display .

It was stated in the issue prospectus that "*….[i]nformation relating to the Underlying Securities including ratings, the terms and conditions, information memorandum (if one is prepared) and regarding where investors could obtain information relating to the performance of the Issuer on an on-going basis together with any further information which is available to the Arranger…..*", would be available on display.

8. Following SFC's request, the issuer highlighted in the prospectus that when prospective investors apply for the notes, information about the underlying security would not be available and referred them to the relevant risk factors in the prospectus. The issuer also highlighted as risks that the underlying security would be AAA rated, not subject to negative outlook on the issue date of the notes only, and the credit ratings may change after the issue date.

9. Following SFC's request, details regarding the early redemption of the notes following a default event concerning the underlying security were disclosed in the prospectus.

Series 27

10. Since the reference obligations of certain reference entities were subordinated notes, the SFC queried if the issuer should disclose in the prospectus the particular nature and risks in relation to subordinated notes as reference obligations. This was subsequently set out in the prospectus.

11. Following SFC's query, the issuer revised its definitions of credit ratings in the prospectus as they are only applicable to the reference entities' overall capacity to repay debts and the credit rating agencies have issued a different set of definitions for credit ratings in respect of specific financial obligations.

12. As the notes were credit-linked to the reference entities and not their reference obligations (which would serve as benchmark obligations when calculating the credit event redemption amount following the occurrence of a credit event), the SFC queried if the issuer should, and the issuer subsequently did, highlight this in the prospectus.

Series 34

13. Following the sub-prime crisis in mid-2007, the SFC queried if the issuer should disclose in the prospectus whether the CDO collateral would be linked to mortgage-backed or asset-backed securities. A statement to the effect that the CDO would not be an asset-backed securities CDO and that they would not be linked to asset-backed or mortgage-backed securities was subsequently added to the prospectus.

14. Following SFC's query, a risk factor on the liquidity of the CDO collateral was added to the prospectus.

Series 35

15. Since one of the reference obligations of a reference entity was a subordinated note, the SFC queried if the issuer should, and the issuer subsequently did, disclose in the prospectus the particular nature and risks in relation to a subordinated note as a reference obligation.

(b) Constellation Notes

Series 1

16. Following SFC's query, the issuer clarified upfront that following the occurrence of a credit event, investors would not be entitled to receive any further payments of interest (including any interest accrued since the last interest payment date).

17. Following SFC's query, a section headed "Application procedure and offering structure" including (a) standard investors' confirmations and (b) certain distributors' undertakings e.g. that they would not accept an application from an investor who has not had the opportunity to read and understand the prospectuses and that the notes would not be sold on the basis of any information that is inconsistent with the prospectuses, was subsequently included.

18. Following SFC's concern, the issuer decided to put on display notices given in respect of the notes pursuant to the terms and conditions.

19. The SFC raised concerns regarding the effect / purpose of including in the prospectus ratings of the senior long-term unsecured debts of the proposed reference entities when the reference obligations of the majority of these entities are subordinated. The SFC queried where a reference obligation is subordinated, whether it would be more appropriate to use the credit rating applicable to such subordinated obligation instead. The issuer subsequently included in the prospectus a statement to the effect that the value of a subordinated debt obligation of a defaulted reference entity is typically substantially less than the value of a senior and unsubordinated debt obligation of such defaulted reference entity.

20. As one of the proposed reference entities was not listed on any stock exchange, the SFC expressed concerns as to how investors could access ongoing regulatory disclosure / financial information of such entity – a risk factor warning investors on the limited independent regulatory information of such entity was subsequently included in the prospectus.

21. As the SFC was concerned that there would be a limited or no secondary market during the first 6 months after the issue date (as the market agent only intends to start making a market in the notes 6 months after the issue date), the issuer included a related risk factor in the prospectus, that it might be difficult for investors to obtain bid or offer prices during the first 6 months.

Series 14-17 (first series of Constellation notes where collateral may comprise CDOs)

22. Following SFC's request, the issuer clarified that interest would cease to accrue from the last interest payment date before the occurrence of an early redemption event or an event of default.

23. As it is stated in the prospectus that collateral may consist of CDOs, the SFC queried if the issuer should include, and the issuer subsequently did include, a warning to the effect that if the CDO collateral is early redeemed due to a default, it is likely that the proceeds of realisation will be substantially less than the principal amount of the collateral being realised and that prospective investors may lose all or substantially all of their investments in the notes.

24. Following SFC's request, the issuer included a warning to the effect that if the issuer becomes unable to make payment of the full amount due in respect of the principal or interest on the notes for certain tax reasons and the swap counterparty does not elect to pay additional amounts to the issuer to enable full payments to be made under the notes, all further payments shall be made after deduction of all applicable taxes and that investors would have no right to require the issuer to redeem the notes in such circumstances.

25. The SFC asked the issuer to re-consider the sentence "*The Issuer makes no representation whatsoever that the contents of any such marketing materials issued and/or distributed by persons other than the Issuer are accurate, true, not misleading or not deceptive and no responsibility whatsoever is accepted in relation to any such marketing materials by or on behalf of any person who is responsible for this Issue Prospectus and Programme Prospectus*" as it may potentially conflict with the new section 40(6) of the CO which extends an issuer's liability to information in marketing materials. This sentence was subsequently deleted.

26. For series 17 which is HKD-denominated, the SFC queried if the floating rate component of the interest rate applicable should be changed from USD-LIBOR to HKD-HIBOR. The issuer amended the prospectus accordingly.

27. Following SFC's request, the issuer included an additional warning to the effect that if a succession event such as merger, demerger or spin off occurs with respect to any reference entity and any successor is not an existing reference entity, such successor could have a different, and worse, credit rating than the original predecessor reference entity.

Series 43-46

28. Following SFC's query, the issuer corrected the information in the prospectus to the effect that following the occurrence of a credit event, investors would receive the "credit event redemption amount", and not an "early redemption amount". This is because the methods for calculating the early redemption amount (following the occurrence of an early redemption event other than a credit event) and credit event redemption amount are different.

29. Following SFC's query, the issuer included as one of the display documents the unaudited quarterly financial results of the swap counterparty.

Series 55-58

30. SFC raised concerns regarding how the initial proposed slogan "*Let your investment ascend from our favourable interest rates*" related to the notes. The issuer submitted another headline (together with the rationale) for Series 55-58 – "*Outstanding returns. Proud achievement*" and "取得驕人投資回報，當然值得自豪". As the maximum potential return was subject to non-occurrence of credit events and other early redemption events, SFC questioned the use of the term "取得". The authorised version of the prospectus contained the headlines "驕人潛在回報，當然值得自豪" (in Chinese) and "*Outstanding potential returns. Proud achievement*" (in English).

31. SFC requested the issuer to enlarge font size of and space out the text in "Summary of Main Terms" and "The Reference Entities" sections to improve legibility.

32. The initial draft prospectus included a statement that the investor will need to confirm and acknowledge to the distributor that he/she has "*received or have been afforded sufficient opportunity to obtain a copy of our programme prospectus, the addendum, this issue prospectus* <u>*and any updating addendum or supplement to the prospectus published before the offer of the notes closes*</u>" – the underlined part of the sentence did not appear in earlier series of Constellation notes. The SFC queried how investors could give this confirmation if the updating addendum was published after the investor placed his/her order but before the offer closes. The issuer amended the prospectus by elaborating on the effect of the confirmation as follows:

  a. the investor confirmation was amended to say that "*… if any updating addendum or supplement to these prospectuses have been published when you place your order, you will be asked to confirm you have received or have been afforded sufficient opportunity to obtain a copy of that updating addendum or supplement too*";
  b. a new confirmation was added – "*when you place your order for the notes, you have agreed with your distributor (if your distributor is acting as principal) or the initial subscriber (if your distributor is acting as agent) that you cannot revoke your order for the notes, even if we publish and register any updating addendum or supplement … during the offer period (unless we specify otherwise in the updating addendum or supplement)*";
  c. the statement to the effect of paragraph (b) above was drawn to the attention of investors in the "IMPORTANT" box on page 2 (i.e., first page after the cover page) of the prospectus.

The issuer's legal advisers explained that this concept of "irrevocable orders" was akin to the position in listed equity initial public offerings.

33. Following SFC's concern, it is stated in the prospectus that despite the unlisted nature of one of the reference entities (with limited public information available), its parent company is listed and would be required to provide certain public disclosures in respect of itself and its subsidiaries.

Marketing Leaflets

(a) Minibonds

Series 16 (the first Minibond series where marketing materials were submitted to the SFC for authorisation)

34. The original draft marketing slogan included the term “guarantee” in Chinese (“保證“). The SFC questioned the appropriateness of the use of such term when the product is not capital guaranteed and also asked the issuer to consider revising the marketing leaflet in order to present a more balanced view. The term “實力的保證” was replaced with “實力的代表” in the authorised version of the marketing leaflet.

35. SFC requested the issuer to re-consider the use of the phrase “first come first serve basis” as this may mislead investors into thinking that the product was popular. The phrase was replaced by “…on offer for a limited period only”.

36. SFC urged the issuer to refer to the “Disclaimer / Important Notice” section in leaflets by other issuers and consider whether any additions need to be made as appropriate. The equivalent section in the marketing leaflet for Minibond series 16 was revised with the use of headings. E.g. The following headings were put in bold in the marketing leaflet:- “*The Notes are not capital protected investments*”, “*Secured nature of the Notes*”, “*Prospective investors must read the Prospectus*”, and “*General*”.

Series 27

37. The issuer and the arranger confirmed in its application letter for authorisation that the marketing leaflet is, in their view, clear and unambiguous, accurate and not misleading.

38. Following SFC’s request, the issuer highlighted the non-principal protected feature of the notes more prominently and improved legibility of the “Important Notice/Disclaimer” section.

Series 34

39. The arranger confirmed in its application letter for authorisation that the marketing leaflet is, in their view, clear and unambiguous, accurate and not misleading.

40. Following SFC’s request, the issuer highlighted the non-principal protected feature of the notes more prominently.

41. With only one of 4 tranches of the series linked to the USD/RMB exchange rate, SFC queried whether it is justified to have the marketing slogan for the series linked to that particular feature. Note: this particular feature and the relevant tranche of the series were subsequently removed from the offer.

Series 35

42. The arranger confirmed in its application letter for authorisation that the marketing leaflet is, in their view, clear and unambiguous, accurate and not misleading.

(b) **Constellation Notes**

Series 10-11 (first Constellation series where marketing materials were submitted to the SFC for authorisation)

43. The SFC queried the use of the phrase "*first come, first served*" to avoid misleading investors that the notes are popular – this was subsequently changed to "*Notes are offered for a limited time*".

44. The SFC queried whether the issuer should clarify in the headlines that the interest rate payable is on a per annum basis. This change was subsequently made by the issuer.

45. In the section headed "summary of main terms", the SFC queried if the issuer should refer, and the issuer did subsequently refer, prospective investors to the prospectuses for details relating to credit events.

46. The SFC requested, and the issuer agreed, to add SFC authorisation and disclaimer wording in "Risk Factor / Important Notice" section.

47. The SFC queried the appropriateness of the sentence "*information contained in this leaflet which is based on the Programme Prospectus (as supplemented by the Addendum), the Issue Prospectus and sources from third parties is believed to be reliable, but no representation is made and no responsibility is accepted for its truthfulness, accuracy or completeness"* as it conflicts with the responsibility statement. This sentence was subsequently deleted.

48. The SFC raised concerns about the phrase "a 100% fixed purchase price guaranteed". The issuer subsequently changed it to "a fixed issue price at 100% of principal amount".

49. Following SFC's queries, warnings to the effect that (i) the information is a summary only; and (ii) the market agent intends, but is not obliged, to commence making a market in the notes 6 months after the issue date of the notes and accordingly, it may be difficult for investors to obtain a bid or offer price for the notes during the first 6 months, were included in the marketing leaflet.

50. The SFC requested the issuer to improve legibility of the section headed "Risk Factors / Important Notices".

Series 43-46

51. SFC raised concerns as to the consistency between the English and Chinese versions and whether the description fits some of the reference entities.

52. SFC raised queries on the accuracy and consistency of various terms used in the marketing leaflet as compared to the prospectus.

53. Rather than showing the credit ratings of the reference entities, SFC queried if the issuer should include credit ratings of reference obligations, especially since the reference obligations are often subordinated obligations. Credit ratings for the subordinated reference obligations were subsequently set out.

54. SFC requested the issuer to increase font size and legibility of certain phrases, including the "non-principal protection" warning.

Series 55-58

55. SFC reminded the issuer to amend the marketing leaflet by tracking our corresponding comments on the issue prospectus.

56. SFC asked, and the issuer made, the section headed “Risk Factors / Important Notices” more prominent.

57. SFC highlighted inconsistencies between the English and Chinese versions – it was noted that there was information missing from the English version. The missing information was subsequently inserted into the English version.

58. SFC requested the issuer to consider including additional “non-principal protection” warning. The issuer agreed to SFC’s request.