立法會
Legislative Council

LC Paper No. CB(1)1613/11-12

Ref: CB1/BC/11/10

Report of the
Bills Committee on Securities and Futures (Amendment) Bill 2011

Purpose

This paper reports on the deliberations of the Bills Committee on Securities and Futures (Amendment) Bill 2011 ("the Bills Committee").

Background

Statutory obligation for listed corporations to disclose price-sensitive information

2. At present, the requirement for listed corporations to disclose price-sensitive information ("PSI") is set out in the Listing Rules of the Stock Exchange of Hong Kong Limited ("SEHK"), not in the law.[1] The lack of regulatory teeth in the Listing Rules has been a cause for concern. The Government considers that a statutory PSI disclosure regime is necessary to enhance market transparency and quality, so as to bring the regulatory regime for listed corporations more in line with those of overseas jurisdictions and to sustain Hong Kong's position as a premier capital formation centre.

3. On 29 March 2010, the Administration launched a three-month public consultation on the proposed statutory codification of certain requirements to disclose PSI by listed corporations. The Administration published the consultation conclusions in February 2011. According to the Administration, the respondents[2] generally supported the objective of the legislative proposal of cultivating a continuous disclosure culture among listed corporations. Certain professional bodies in the legal, accounting and financial fields, as well as

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[1] The Listing Rules are made and administered by SEHK. The Rules are non-statutory and compliance with which by issuers is based on the contractual listing agreements between SEHK and the issuers.

[2] The Administration had received 110 written submissions, about half of which were from listed corporations, while the others were mainly from trade bodies of the financial services, accounting and legal sectors as well as investor/consumer groups.

consumer groups indicated general support to the proposed statutory regime. Noting that the lack of regulatory teeth in the Listing Rules has been an issue of public concern, supporters commented that reliance on non-statutory regulation raised doubt about enforcement effectiveness. A statutory regime could encourage compliance, enhance market transparency and provide better protection to investors. However, around 20% of the written submissions (mostly listed corporations, with a few trade bodies) did not support establishing a statutory regime. They opined that a statutory regime would lead to indiscriminatory disclosure of "half-baked" information and increase compliance cost.

Direct institution of Market Misconduct Tribunal proceedings by the Securities and Futures Commission

4. Currently, under the Securities and Futures Ordinance (Cap. 571) ("SFO"), only the Financial Secretary ("FS") may institute proceedings before the Market Misconduct Tribunal ("MMT"). Upon receipt of reports from the Securities and Futures Commission ("SFC"), FS would seek legal advice from the Department of Justice ("DoJ") to assist him in deciding whether proceedings should be instituted. In order to streamline the process for enforcement of the statutory PSI disclosure requirement and to deal with the existing six types of market misconduct stipulated in the SFO[3], the Administration proposed in the public consultation in 2010 (paragraph 3 above) to empower SFC to institute proceedings direct before the MMT, without having to first refer the case to FS for his decision to do so.

5. According to the Administration, the majority of the respondents who did not agree with the proposal were from listed corporations, as they believed the proposal would lead to a loss of checks and balances. Some of them were concerned that SFC should not be both the investigator and prosecutor. Two respondents from the legal and banking sectors sought further elaboration on the reasons for granting SFC direct access. A few respondents raised concerns about the resource implications to the MMT as a result of direct access. On the other hand, a major professional body in the legal sector agreed with the proposal. The professional body pointed out that SFC has direct and expert knowledge of the securities market and law, and it would suffice to rely on SFC's judgment as to whether a case should be referred to the MMT. Involving FS or DoJ to institute proceedings before the MMT would amount to duplication of efforts with SFC. The professional body also pointed out that the MMT itself provides the best checks and balances in the enforcement regime.

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[3] These are insider trading, false trading, price rigging, disclosure of information about prohibited transactions, disclosure of false or misleading information inducing transactions, and stock market manipulation.

Establishment of a separate body on investor education

6. Currently, among the financial regulators in Hong Kong, only SFC has an explicit statutory remit to pursue investor education[4], although other financial regulators and operators, as well as industry bodies, do make information available through various means to promote public understanding of various financial matters. The events of the global financial crisis in 2008 have shown that some investors would need more support and protection when they engage in financial services. SFC, in its report of December 2008 on "Issues raised by the Lehmans Minibonds crisis", recommended that an investor education body be established as a separate corporate funded by SFC to co-ordinate and deliver an expanded investor education programme across the whole financial services sector.

7. The Administration launched a three-month public consultation on the proposed establishment of an investor education body and a Financial Dispute Resolution Centre on 9 February 2010, and published the consultation conclusions in December 2010. According to the Administration, there was a general consensus that provision of financial education was the most effective means to enhance financial literacy of the public, hence helping them make informed financial decisions and detect problems such as market scams and malpractices at an early stage. The vast majority of the respondents supported the proposal of setting up an investor education body to holistically oversee the needs of investor education and delivery of related initiatives.

The Bill

8. The Bill was introduced into the Legislative Council on 29 June 2011. The objectives of the Bill are to amend SFO to enhance the regulatory regime for the financial market and improve investor protection by codifying certain requirements to disclose PSI, empowering SFC to institute proceedings before the MMT and strengthening SFC's investor education role.

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[4] Section 5 of SFO prescribes the functions of the SFC, which include inter alia –

(a) to promote understanding by the public of the securities and futures industry and of the benefits, risks and liabilities associated with investing in financial products;

(b) to encourage the public to appreciate the relative benefits of investing in financial products through persons carrying on activities regulated by the SFC under any of the relevant provisions; and

(c) to promote understanding by the public of the importance of making informed decisions regarding transactions or activities related to financial products and of taking responsibility therefor.

9. The Bill proposes to:

(a) require listed corporations to disclose PSI (i.e. named as "inside information" in the Bill) in a timely manner to the public and impose civil sanctions for breach of the requirement;

(b) enable SFC to institute MMT proceedings direct for market misconduct cases after it has obtained consent from the Secretary for Justice ("SJ"), and to appoint Presenting Officers in MMT in place of SJ;

(c) enable SFC to establish a wholly owned subsidiary to facilitate the performance of its wider investor education functions; and

(d) make certain technical amendments to SFO.

The Bills Committee

10. At the House Committee meeting on 8 July 2011, Members agreed to form a Bills Committee to study the Bill. Under the chairmanship of Hon CHAN Kam-lam, the Bills Committee has held 10 meetings. The membership list of the Bills Committee is at **Appendix I**. Relevant trade associations, professional organizations and the general public have been invited to give views on the Bill. The Bills Committee received oral representations from nine deputations and one individual at the meeting on 24 October 2011 and received written submissions from 16 other organizations. A list of the organizations and individual which/who have submitted views to the Bills Committee is at **Appendix II**.

Deliberations of the Bills Committee

11. The Bills Committee supports the policy objectives of the Bill. In respect of the proposed statutory PSI disclosure regime, the main issues deliberated by the Bills Committee include the definition of PSI, the safe harbours, the scope of persons who may be held liable for a breach of the disclosure requirement, and the duties and liabilities of "officers" of listed corporations.

12. In regard to the proposal to enable SFC to institute MMT proceedings direct for market misconduct cases, the Bills Committee has examined the justifications for the proposal and the relevant checks and balances. As for the

proposal to establish an investor education body, the Bills Committee has discussed the appropriateness of establishing the body as a wholly owned subsidiary of SFC. The following paragraphs summarize the Bills Committee's deliberations.

Definition of price-sensitive information and disclosure requirement (clause 3 – proposed sections 307A and 307B)

13. Proposed section 307B under clause 3 provides that a listed corporation must disclose any inside information to the public as soon as reasonably practicable, if (a) the information has, or ought reasonably to have, come to the knowledge of an officer of the listed corporation in the course of performing his functions as an officer of the corporation; and (b) a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.

14. Under proposed section 307A, for the purposes of the proposed new Part XIVA of SFO on "Disclosure of Inside Information", "inside information" (內幕消息), in relation to a listed corporation, means specific information that -

(a) is about –

(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.

15. Some members including Hon Andrew LEUNG, Hon Paul CHAN, Hon WONG Ting-kwong, and Hon Starry LEE have expressed concern whether the proposed definition of "inside information" is appropriate such that while the effectiveness of the statutory PSI disclosure regime can be ensured, the statutory disclosure requirement would not pose undue compliance challenges to listed corporations and their officers. In this regard, the Bills Committee has requested the Administration to provide the following information –

(a) a comparison of the definition of "inside information" under the Bill with those under (i) the relevant legislation in comparable jurisdictions; and (ii) the Listing Rules of SEHK; and

(b) examples of situations under which information relating to the day-to-day operation of a listed corporation would be classified as "inside information" and required to be disclosed under the proposed legislation.

The Bills Committee has also requested the Administration to consider setting quantitative thresholds in the Bill for determining whether a piece of information is "inside information".

16. The Administration has responded that the definition of "inside information" and the applicable tests/thresholds for the liabilities of listed corporations and officers are proposed in the Bill having regard to the existing regulatory regime, the feedback from respondents in the public consultation exercise, and relevant international practices. In providing a comparison between the definition of "inside information" under the Bill and the relevant statutory requirements in the United Kingdom ("UK"), Australia and Singapore[5], the Administration points out that all the three comparable jurisdictions adopt a principle-based instead of a prescriptive approach in defining PSI, and none of these jurisdictions uses 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 the definition of "inside information" under the Bill and those used in the comparable jurisdictions are very similar. Such key elements are –

(a) information concerning the listed corporation and its securities;

(b) not generally available/ known; and

(c) if available/known, would be likely to materially affect the price of the listed securities.

17. The Administration has further advised that the Bill proposes borrowing the concept of "relevant information" currently used in the "insider dealing" regime in SFO[6] to define PSI (i.e. "inside information"). 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 inside information and hence the need for disclosure. During the public consultation on the legislative proposals for the statutory PSI disclosure regime conducted in March to June 2010, respondents generally supported the adoption of the

[5] Annex A to LC Paper No. CB(1) 261/11-12(02)
[6] Section 245 of SFO

concept of "relevant information" under the insider dealing regime in the Bill. This approach is also the same as that adopted by the European Union (including UK), which has developed the insider dealing regime and the PSI disclosure regime on the basis of the same concept of "inside information".

18. As regards the concern of Hon Audrey EU and Hon Paul CHAN on how the proposed definition of "inside information" in the Bill compares with the definition of PSI in the Listing Rules of SEHK, the Administration has advised that the scope of the proposed definition of "inside information" in the Bill is narrower than the current definition of PSI adopted under Listing Rule 13.09 (**Appendix III**). The major difference is that the latter also covers information on any major new developments in the group's sphere of activity (i.e. Listing Rule 13.09(1)) and any information necessary to avoid the establishment of a false market (i.e. Listing Rule 13.09(1)(b)). SFC and SEHK will work to revise Listing Rules 13.09 after the passage of the Bill. The tentative thinking is to incorporate those elements which are in the existing Listing Rule 13.09 but would fall outside the scope of the statutory regime into other provisions of the Listing Rules which would not give rise to legal consequences.

19. On Hon Andrew LEUNG's concern about the circumstances under which information relating to the day-to-day operation of a listed corporation would be regarded as inside information, the Administration has referred to a relevant statement in the report of the Insider Dealing Tribunal ("IDT") on Hanny Holdings Limited[7] and advised that the bulk of the information that "officers" of a listed corporation (see paragraph 22 below) have in the daily operations of a listed corporation would generally not be inside information, and these "officers" are not expected to come into knowledge of significant or dramatic events on a day-to-day basis. Nevertheless, these "officers" should recognize that ordinary day-to-day activities may transform into irregular or unforeseen events due to changes in the elements comprising these activities or the occurrence of matters impacting upon these activities. What begins as a normal day-to-day activity may become a non-routine or irregular event that changes the course of a company's business. If an "officer" of a listed corporation reasonably expects that the event, once stripped off its confidentiality, would be likely to materially affect the share price, the disclosure duty should arise.

20. As for some Bills Committee members' suggestion of setting quantitative thresholds in the Bill for determining whether a piece of information is inside information, the Administration has responded that since the business nature,

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[7] The statement was 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*".

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 inside information for continuous disclosure purposes.[8] To facilitate compliance, SFC will publish a new set of guidelines, namely "Guidelines on Disclosure of Inside Information" ("the Guidelines")[9], setting out the key aspects of what has been viewed by the IDT and MMT as constituting "relevant information". Specifically, paragraph 35 of the revised draft Guidelines (**Appendix IV**) gives a non-exhaustive list of common examples of events or circumstances where a corporation should consider whether a disclosure obligation arises. In addition, SFC will provide consultation service to assist corporations understand how to apply the disclosure provisions initially for 24 months from the enactment of the Bill.

21. While Bills Committee members appreciate the difficulty of prescribing quantitative thresholds to define PSI in legislation, members consider that to assist listed corporations and their officers in understanding the disclosure requirement and to facilitate their compliance, more concrete guidance on what constitutes inside information should be provided in the Guidelines. The Administration has responded that the IDT and the MMT have given on occasions views on the concept of "material change". To facilitate compliance, SFC will set out in the Guidelines relevant precedent cases in the IDT and the MMT for listed corporations' reference in deciding whether a particular piece of information is price sensitive.

Scope of persons covered by the proposed statutory PSI disclosure regime

22. The term "officer" is defined in Part 1 of Schedule 1 to SFO as follows –

> "(a) in relation to a corporation, means a director, manager or secretary of, or any other person involved in the management of, the corporation; or
>
> (b) in relation to an unincorporated body, means any member of the governing body of the unincorporated body;"

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[8] It was stated in the footnote in the Administration's paper (LC Paper No. CB(1)261/11-12(02))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.

[9] The Administration provided the Bills Committee with a draft of the Guidelines vide LC Paper No. CB(1)135/11-12 in October 2011, and a revised draft of the Guidelines vide LC Paper No. CB(1)1325/11-12(01) in March 2012.

As the statutory PSI disclosure regime concerns obligations of a listed corporation, paragraph (a) of the definition is relevant in the context of the Bill.

23. In view of the definition of "officer" in SFO, some members including Hon Andrew LEUNG, Hon Audrey EU, Hon Jeffrey LAM, Hon WONG Ting-kwong and Hon Paul CHAN have expressed concern whether the scope of persons (i.e. "officers" of list corporations) covered by the proposed statutory PSI disclosure regime may be too wide. The members have pointed out that some persons involved in the management of listed corporations do not have access to the PSI of the corporations and/or are not in a position to decide whether a piece of information related to the corporations is inside information and hence should be disclosed. Some deputations[10] have expressed similar concern and suggested replacing the concept of "officer" by another concept covering a narrower scope of persons.

24. The Administration has advised that the term "officer" has been used in SFO and its predecessor ordinances for many years. Within the definition of "officer", the term "secretary" reads "secretary of the corporation", and refers to "company secretary", which has the same meaning as ascribed to it under the Companies Ordinance (Cap. 32). To address the concern that the definition of "officer" might be too broad and catch middle management and low ranking staff and to enhance certainty of the term, SFC has included the following interpretive guidance in paragraph 53 of the revised draft Guidelines:

> "As a general principle, one must look to the object of the legislation and the context to determine the meaning of the term "manager". In the context of Part XIVA, in considering whether a person is a "manager", the person's actual responsibilities are more important than the person's formal title. A "manager" normally refers to a person who, under the immediate authority of the board, is charged with management responsibility affecting the whole of the corporation or a substantial part of the corporation. A person is normally regarded to be "involved in the management of the corporation" if the person discharges the role of a "manager"."

In providing the above interpretive guidance, SFC has considered relevant interpretations under common law and comparable concepts adopted in major international jurisdictions.

25. The Administration has affirmed that the policy intention is to cover senior members of a corporation who are charged with management

[10] The Law Society of Hong Kong, the Hong Kong Association of Banks, the Chamber of Hong Kong Listed Companies, and Economic Synergy.

responsibility affecting the whole or a substantial part of the corporation. If these persons become aware of certain information, they are in a position to determine whether such information amounts to inside information. Under the Bill, these persons are responsible for taking all reasonable measures from time to time to ensure proper safeguards exist to prevent a breach of the disclosure obligation. The approach adopted for the Bill in this regard is similar to that of Australia.

Duty and liability of officers of listed corporations (clause 3 – proposed section 307G)

26. With regard to the liability of the officers of listed corporations under the proposed statutory PSI disclosure regime, some members including Hon Andrew LEUNG, Hon Ronny TONG and Hon Audrey EU have expressed concern about the formulation of proposed section 307B(2) which include the phrase of "ought reasonably to have come to the knowledge of an officer". In this regard, the Bills Committee has sought explanation for such formulation of the provision and asked whether and what defence would be available to an "officer" if the "officer" actually does not have knowledge of the information, or the "officer" has made in good faith a judgment that a piece of information should not be disclosed but the decision is wrong based on an objective test.

27. The Administration has advised that the concept "ought reasonably to have come to knowledge" under section 307B(2) is an element that triggers the disclosure obligation for a listed corporation and does not by itself result in a liability on "officers". The intention of including the concept is to avoid listed corporations evading from the disclosure obligation by arguing that inside information has been channelled to the officers but has not been read, or deliberately keeping inside information away from being accessed by the officers of the listed corporation. Based on proposed section 307G, an "officer" would be held liable only if the breach of a disclosure requirement is a result of the officer's intentional, reckless or negligent conduct, or his failure to take all reasonable measures from time to time to ensure that proper safeguards existed to prevent a breach of a disclosure requirement. The enforcement authorities have to provide evidence to prove that the "officer" concerned has breached the disclosure requirement based on proposed section 307G.

28. SFC has also advised that based on proposed section 307B(2)(b), defence is available to an "officer" that he has acted as a reasonable person in deciding that the information is not inside information and therefore did not disclose the information. It is also a defence if from the view-point of a reasonable person who has traded the securities concerned, a piece of information would not materially affect the price of the securities concerned.

29. In response to the Bills Committee's request, the Administration has provided a comparison[11] between the proposals in the Bill and the relevant legislation in comparable jurisdictions regarding the triggering of the PSI disclosure requirement, and the circumstances under which a person would be liable.

30. The Bills Committee has noted that the Law Society of Hong Kong and the Hong Kong Institute of Certified Public Accountants (HKICPA) have suggested adding a safe harbour to cover the situation where a corporation has set up internal control procedures and concluded that certain information is not inside information out of good faith. Specifically, HKICPA has suggested adding an additional safe harbour in the Bill to cover the situation where a corporation has appropriate internal control procedures in place, has taken reasonable steps to ensure a specific issue has been properly considered and the directors, having carefully considered the circumstances (e.g. taking professional advice, where appropriate), have exercised judgement, with reasonable prudence and in good faith, concluding that certain information is not inside information and does not warrant a disclosure at that time. The Bills Committee has requested the Administration to consider the suggestion of HKICPA.

31. The Administration has responded that to limit the circumstances wherein a listed corporation would have a disclosure obligation, the Bill has specified "a reasonable person" test. A listed corporation would not have breached the disclosure requirement unless it can be proved that –

(a) the information has, or ought reasonably to have, come to the knowledge of an officer of the corporation in the course of performing functions as an officer of the corporation; and

(b) a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.

32. The Administration has further advised that a safe harbour based on "good faith" and the other grounds proposed by HKICPA is inappropriate for the proposed regime for the disclosure of inside information. Such safe harbour is not found in the PSI regimes of other jurisdictions. The introduction of such a safe harbour, which is in a number of important respects a subjective test, would render the proposed PSI regime ineffective because disclosure could be withheld as long as a listed corporation believes "in good faith" that the information is not inside information. In effect, the proposed PSI regime risks becoming a voluntary scheme where it would be up to the listed corporation and

[11] Annex to LC Paper No. CB(1)433/11-12(02)

its officers to decide whether a piece of information is inside information and needs to be disclosed. This would defeat the purpose of the proposed legislation.

33. Taking note of the Administration's advice regarding the liabilities of "officers" and the guidance available in the draft Guidelines, Hon Andrew LEUNG has expressed concern that as the definition of "inside information" in the Bill is principle-based and the draft Guidelines provide a non-exhaustive list of examples on the types of information which are required to be disclosed, it is still difficult for the officers of listed corporations to fulfill their duty stipulated under proposed section 307G. The Bills Committee has also noted that under Hong Kong law, there is no distinction between the duties and responsibilities of executive and non-executive directors (NEDs). Some members including Hon Andrew LEUNG, Hon Jeffrey LAM, Hon WONG Ting-kwong, Hon Abraham SHEK and Hon CHIM Pui-chung have expressed concern that NEDs of listed corporations are usually not directly involved in the daily operation of the corporations, and very often they actually do not have knowledge of the inside information of the corporations. As such, it would not be fair to NEDs if they are equally held responsible for breach of the disclosure requirement as the executive directors of listed corporations. Hon CHIM Pui-chung has opined that there should be clear demarcation between the liabilities of executive directors and NEDs under the proposed PSI disclosure regime. Hon WONG Ting-kwong and Hon Andrew LEUNG have opined that in taking enforcement actions against a listed corporation on a breach of a disclosure requirement, consideration should be given to the different roles of executive directors and NEDs and their varied degree of involvement in the corporation's operation.

34. In view of members' concerns, the Administration has advised that SFC will set out clearly in the Guidelines that assuming a listed corporation has implemented reasonable measures to prevent a breach, an officer (including NEDs) who acts in good faith and in accordance with all his fiduciary duties without actual knowledge of the information or involvement in the corporation's breach is unlikely to be personally liable on ground of intentional, reckless or negligent conduct. On the requirement for officers to take all reasonable measures from time to time to ensure that proper safeguards exist to prevent breach of the disclosure requirement, to facilitate compliance, SFC has provided in the revised draft Guidelines a list of examples of such measures, including those set out at **Appendix V,** and additional guidance on officers' liability and obligations of NEDs as set out at **Appendix VI**.

35. The Administration has further advised that when considering whether an officer has taken all "reasonable measures" and whether an officer has been negligent, SFC will take into account the roles of the officers concerned in the

listed corporation. Insofar as NEDs are concerned, in the event of a breach of the disclosure requirement by a listed corporation, an NED is unlikely to be held liable if proper internal control procedures for monitoring and reporting potential inside information to the board have been established and reviewed periodically, and the NED concerned has no knowledge of the inside information in question because other officers or employees of the listed corporations do not comply with the established internal control procedures.

Timing and manner of disclosure of inside information (clause 3 – proposed sections 307B and 307C)

36. Proposed section 307B(1) under clause 3 provides that a listed corporation must, as soon as reasonably practicable after any inside information has come to its knowledge, disclose the information to the public. According to the Administration, this provision would enable listed corporations to verify the facts, conduct assessment of the matter and its likely impact and seek professional advice as appropriate and reasonable. Hon James TO has expressed concern that a listed corporation may defer disclosure on grounds of the need to verify the details of the inside information and/or assess the public relations implications of the disclosure.

37. SFC has advised that under the Bill, a listed corporation should disclose inside information as soon as reasonably practicable, and the information should be accurate and complete in all material respects. This notwithstanding, the listed corporation should make the disclosure once the basic facts have been ascertained. While the listed corporation may seek legal advice to ascertain its disclosure obligation, it should not await verification of detailed data or assessment of public relations implications before making the disclosure.

38. Proposed section 307C(1) under clause 3 provides that a disclosure of inside information must be made in a manner that can provide for equal, timely and effective access by the public to the inside information disclosed. Proposed section 307C(2) provides that without limiting the manner of disclosure permitted under subsection (1), a listed corporation complies with that subsection if it has disseminated the inside information through an electronic publication system operated by a recognized exchange company for disseminating information to the public.

39. Hon Andrew LEUNG has expressed concern that a listed corporation may not be able to make a timely disclosure of inside information in the event that the electronic publication system of SEHK has broken down. The Administration has responded that the Hong Kong Exchanges and Clearing Limited has put in place contingency measures, including the provision of an electronic bulletin board, to facilitate the dissemination of PSI in case of

disruption of the HKExnews Website service[12]. In determining the compliance of a listed corporation, the enforcement authorities will take into account the availability of electronic publication systems at the material time for disclosure of inside information by listed corporations.

Status and effects of the Guidelines in relation to disclosure proceedings

40. Under section 399 of SFO, SFC will issue the Guidelines to provide interpretive guidance on the key concepts adopted for the proposed statutory PSI disclosure regime and other guidance to facilitate listed corporations and their officers to comply with the disclosure requirement under the proposed new Part XIVA of SFO. The Bills Committee has sought explanation on the status and effects of the Guidelines in relation to the disclosure proceedings and the procedures for making amendments to the Guidelines.

41. The Administration has advised that the purpose of the Guidelines is to assist listed corporations and their officers to understand and meet the statutory disclosure obligations under the proposed new Part XIVA of SFO. In discharging its functions under the disclosure regime, SFC will have regard to the provisions of the Guidelines. According to section 399(6) of SFO, the Guidelines made thereunder shall be admissible in evidence and may be taken into account as a relevant matter in deciding any question arising in the proceedings under the SFO, although a failure to comply with it shall not by itself render a person liable to any judicial or other proceedings. Although it is not obliged to under SFO, it is SFC's stated policy and procedure to conduct public consultation on any codes or guidelines it proposes to make under section 399 of SFO. In tandem with the Administration's public consultation on the PSI proposals, SFC launched a three-month public consultation on the draft Guidelines in March 2010. Taking into account the public comments received, SFC has revised the draft Guidelines accordingly. The Guidelines will be finalized and issued upon the enactment of the Bill. In future, any amendments of the Guidelines would only be made after public consultation and with the approval of the SFC's Board.

Use of evidence received for purposes of disclosure proceedings (clause 3 – proposed section 307L)

42. Proposed section 307L under clause 3 restricts the use in other proceedings of evidence given in disclosure proceedings. Subsection (1)(b) provides that subject to subsection (2), evidence given by any person at or for

[12] Hong Kong Exchanges & Clearing Limited publishes regulatory disclosures submitted by listed issuers on the HKExnews website (www.hkexnews.hk) for mainboard companies and the Growth Enterprise Market ("GEM") websites (www.hkgem.com) for GEM board companies respectively. They are often collectively referred to as "HKExnews Website".

the purposes of any disclosure proceedings is not admissible in evidence against the person for any other purposes in any other proceedings (civil or criminal) in a court of law brought by or against the person.

43. Hon Ronny TONG has enquired about the purpose of applying the restriction under proposed section 307L(1)(b) to proceedings "brought by" the person. The Administration has advised that proposed section 307L(1) mirrors existing section 255(1), and provided an example to illustrate the application of proposed section 307L(1)(b). In this example, Person A gave evidence at or for the purpose of a disclosure proceeding, and subsequently, lodges a civil claim, unrelated to the giving of evidence at or for the purpose of the disclosure proceeding, against Person B. If Person B makes a counterclaim against Person A in the same civil action, under proposed section 307L(1)(b), Person B cannot use the evidence given by Person A at or for purpose of the disclosure proceeding as evidence in the counterclaim against Person A.

Level of regulatory fine (clause 3 – proposed section 307N)

44. Proposed section 307N under clause 3 empowers the MMT to make orders in respect of a person it has identified as being in breach of a disclosure requirement. Hon Andrew LEUNG has enquired about the basis for setting the maximum regulatory fine at $8 million under subsection (1)(d). The Administration has advised that in setting the maximum regulatory fine at $8 million, it has taken into consideration that the statutory disclosure regime is in principle a civil regime with the imposition of civil sanctions only, and the maximum regulatory fine should not be set at a level too close to the maximum fine of $10 million for criminal offences related to market misconduct cases. Based on proposed section 307N(1)(d), the regulatory fine will only be applicable to the listed corporation concerned, and/or the directors and chief executive of the corporation. The MMT has to take into account the factors stipulated in proposed section 307N(3) in determining the level of the regulatory fine.

Civil liability for breach of a disclosure requirement (clause 3 – proposed section 307Z)

45. Proposed section 307Z under clause 3 imposes a statutory civil liability on a person who is in breach of a disclosure requirement, and mirrors existing section 281 of SFO[13]. Hon Ronny TONG has enquired about the reason for

[13] Section 281 of SFO enables a person to seek compensation, based on the "fair, just and reasonable" principle, from a person who was found by the Market Misconduct Tribunal (MMT) for having committed a market misconduct offence, without having to prove to the court once again that the defendant has committed the offence.

providing a "fair, just and reasonable" test under proposed section 307Z(2), and whether there has been any proceedings instituted under section 281 of SFO.

46. The Administration has advised that proposed section 307Z enables a person to seek compensation, based on the "fair, just and reasonable" principle, from a person who has been found by the MMT to be in breach of a disclosure requirement, without having to prove to the court once again that the defendant is guilty of the breach. The "fair, just and reasonable" test is the test adopted by the court in determining whether a defendant is liable to compensate the plaintiff for losses suffered due to the defendant's negligence. The inclusion of the "fair, just and reasonable" test in proposed section 307Z aims to serve as a useful guidance to the court to allay concerns that proposed section 307Z may be overly wide, thereby leading to a floodgate of claims lodged against persons who are in breach of the disclosure requirement. The Administration has conducted a case search and found that there have been no proceedings instituted under section 281 of SFO so far.

Direct access to Market Misconduct Tribunal proceedings by Securities and Futures Commission (clauses 17 to 28)

47. Some members including Hon Andrew LEUNG, Hon Jeffrey LAM, Hon Abraham SHEK, Hon CHIM Pui-chung and Hon Paul CHAN have expressed views on the proposal to empower SFC to institute proceedings before the MMT direct without the prior consent of FS, and to provide for SFC instead of SJ to be responsible for appointing the Presenting Officers in MMT proceedings. While Hon Paul CHAN is in support of the direct access proposalsome members are concerned that the proposed new arrangement would lead to excessive expansion of SFC's powers and over zealous enforcement actions against listed and licensed corporations and their officers. These members consider that suitable checks and balances should be available in the system to ensure that the legitimate interests of all parties concerned would be protected. In this connection, the Bills Committee notes that while the Hong Kong Bar Association has expressed support for the proposal, some deputations[14] have expressed reservations about or disagreement with the proposal.

48. In response to the concerns of members, the Administration and SFC have made the following points –

(a) When SFO was enacted in 2003, the key objective of establishing the MMT was to create a speedy civil fast track for market misconduct cases. Building on the strengths of the then civil tribunal system under the Securities (Insider Dealing) Ordinance

[14] HKICPA, the Law Society of Hong Kong, the Hong Kong Association of Banks and Economic Synergy

(Cap. 395) (repealed in 2003) in combating insider dealing, the then Securities and Futures Bill proposed to extend the civil tribunal system and establish an MMT to cover insider dealing as well as other instances of market misconduct. It was against this background that the composition and procedures of the MMT, including the institution of proceedings by FS, provided in the Securities and Futures Bill and the enacted SFO largely emulated those of the IDT.

(b) The proposed direct institution of MMT proceedings by SFC is in line with the aforesaid objective of providing a speedy civil fast track for market misconduct cases, and would allow for a streamlined process to enforce the new disclosure requirement.

(c) The current arrangement involves more than three parties (i.e. SFC, the Prosecution Division and Civil Division of DoJ, the Financial Services and the Treasury Bureau and the Financial Secretary's Office) in examining the same case though for different purposes and from different perspectives. As all the parties will need to examine the information and materials in detail in order to formulate their own recommendations, and it is not uncommon to involve several rounds of clarifications and questions, the whole process takes time to complete. In view of the experience in MMT proceedings gained in the past years and SFC's experience in managing other civil proceedings, the Administration and SFC consider that there is room to streamline the current procedure.

(d) Without derogating from the powers of SJ in criminal prosecution, SFC already has power to invoke section 388(1) of SFO to prosecute offences under its own name before a magistrate. Besides, SFC is able to make direct applications to the Court of First Instance for injunction and other orders under section 213 of SFO and handle disciplinary proceedings and review of SFC's decisions before the Securities and Futures Appeals Tribunal ("SFAT") respectively under Parts IX and XI of SFO. As with MMT proceedings, these proceedings are all civil in nature and are heard by judges[15] (with lay members in SFAT cases). Currently, MMT proceedings are the only proceedings of a civil nature under SFO which are instituted by FS but not SFC.

[15] "Judge" is defined for the purpose of MMT and SFAT under sections 245(1) and 215 of the SFO as (a) a judge or deputy judge of the CFI; (b) a former Justice of Appeal of the Court of Appeal; or (c) a former judge or a former deputy judge of the CFI.

(e) Under the proposed procedure, after obtaining the approval of the SFC Board to institute MMT proceedings, SFC will seek consent from SJ under proposed section 252A (clause 21) for market misconduct cases. SJ will not give his consent if (a) market misconduct offences under Part XIV of SFO are contemplated, or (b) other indictable offence(s) are contemplated or instituted in respect of the same conduct and the institution of MMT proceedings would be likely to cause serious prejudice to the investigation or prosecution of such offence(s). On obtaining SJ's consent, SFC can then implement its Board's decision to institute a case before the MMT. The proposal will significantly streamline the process and strengthen individuals' rights to a timely and fair proceeding without compromising the integrity of the system.

(f) Under the proposed procedure, although SFC is no longer required to seek FS' approval before instituting MMT proceedings, there are numerous checks and balances built into the system, including (i) the need for SFC to obtain the consent of SJ before it may institute MMT proceedings to ensure the primacy of criminal prosecution; (ii) the need to obtain the approval of the SFC Board to institute MMT proceedings; and (iii) the independence of the MMT.

(g) The proposal to enable SFC to institute civil proceedings with the MMT direct for market misconduct cases is consistent with the function and power of statutory securities regulators in other jurisdictions including UK, Australia, Canada and the United States.[16]

49. Hon Andrew LEUNG and Hon Jeffrey LAM have expressed the view that compared to the existing arrangement, there are fewer checks and balances in the proposed procedure for SFC to institute proceedings before MMT direct. Hon Paul CHAN has expressed support for the proposal, as he considers that Hong Kong being an international financial centre needs to be able and to be seen as being able to deal with market misconduct cases in an efficient manner. He also considers that there are adequate checks and balances under the proposed procedure.

50. The Administration and SFC have further elaborated on the various checks and balances under the proposed direct access arrangements[17] -

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[16] SFC has provided a comparison table vide Annex to LC paper No. CB(1)900/11-12(03) setting out the arrangements for market misconduct proceedings in comparable jurisdictions.

[17] Details of the checks and balances are set out in Annex D to the Administration's paper LC Paper No. CB(1)942/11-12(02).

(a) Consent by SJ – under the new section 252A, SFC must obtain the consent of SJ before it may institute MMT proceedings to ensure the primacy of criminal prosecution.

(b) Approval by SFC Board – SFC would need to submit a paper to the SFC Board for approval to institute MMT proceedings subject to the consent of SJ under the new section 252A. The decision to institute MMT proceedings will be a non-delegable one and made by the Board. There is a significant level of independent views on the Board. SFO stipulates that the number of Non-Executive Directors ("NEDs") shall exceed the number of Executive Directors ("EDs"), and currently, the Board comprises a non-executive Chairman, seven NEDs and five EDs (including the Chief Executive Officer). Non-executive representation on the Board is drawn from acclaimed members in the financial services-related sector, including experienced accountants, senior barristers and solicitors, academics and a member of the Legislative Council.

(c) The MMT proceedings – the statutory framework governing MMT proceedings provides another level of checks and balances. MMT is an independent tribunal chaired by judges appointed by the Chief Executive ("CE") on the recommendation of the Chief Justice, and members are appointed by CE (or FS under delegated authority), all of whom are independent from SFC. Parties before it are entitled to legal representation. MMT has full powers to inquire into the case, including powers to require a person to give evidence and produce any record/document relating to the subject matter of the proceedings, and to obtain further evidence through SFC (sections 253 and 254). MMT will determine whether there has been any market misconduct after considering all the evidence and submissions from the parties. Any person who is dissatisfied with the MMT's finding or determination may appeal to the Court of Appeal.

Time limit for institution of MMT proceedings

51. Noting that the Bill does not specify a time limit for institution of disclosure proceedings in the MMT, Hon Andrew LEUNG and Hon Paul CHAN have expressed concern that the absence of such a time limit may be unfair to listed corporations and their officers, and listed corporations may have to incur substantial expenses in maintaining and retrieving relevant records in the event that disclosure proceedings in respect of an event occurred long time ago are instituted against them. The Bills Committee has requested the

Administration to consider setting a time limit for the institution of disclosure proceedings in the MMT.

52. The Administration has advised that the proposed provisions for the institution of disclosure proceedings mirror the current arrangements in relation to proceedings before the MMT, for which no time limit is set. Unlike an adversarial civil litigation for which a time limit usually applies, an MMT inquiry is inquisitorial in nature and it is a common arrangement in local legislation[18] that no limitation period is set for such inquiries. Moreover, market misconduct and disclosure breaches could be serious civil contraventions and from an investor protection perspective, it would not be desirable to specify a time period to limit the institution of actions against such serious cases. When instituting any proceedings before the MMT, the principles of fairness, justice and reasonableness must be observed. Any undue delay can be taken as a ground for a person to object to the institution of the proceedings, either before the MMT or before a court of law.

Establishment of a separate body on investor education (clauses 31 to 33)

53. Clause 31 of the Bill seeks to widen SFC's functions in relation to investor education, and enable the Commission to establish a wholly owned subsidiary to facilitate the performance of its investor education functions. Clause 32 seeks to enable SFC to delegate any of its investor education functions to the wholly owned subsidiary, and clause 33 amends Part 2 of Schedule 2 to the Ordinance to provide that the Commission's power to establish a wholly owned subsidiary to facilitate the performance of its investor education functions is non-delegable.

54. Hon Audrey EU has sought explanation for establishing the proposed body on investor education as a wholly owned subsidiary of SFC, and enquired about the staff establishment and estimated expenditure of the proposed body.

55. The Administration and SFC have advised that in addition to taking over the current investor education responsibilities from SFC on securities and futures products, the investor education body will also undertake investor education work in relation to other financial products such as credit cards and insurance products. The establishment of the body as a wholly owned subsidiary of the SFC will enhance its accountability and transparency in the performance and expenditure on investor education. A non-executive director of SFC will be appointed as the chairman of the board of the investor education body, which will include representatives from other relevant regulatory bodies,

[18] Examples quoted by the Administration are the inquisitorial processes relating to a Commission of Inquiry set up under the Commission of Inquiry Ordinance (Cap. 86) and inquiries held under the Legislative Council (Power and Privileges) Ordinance (Cap. 382).

the financial sector and the Education Bureau. The board would decide the scope and strategy of the work of the investor education body. Its set-up cost will be about $7.5 million. It would have about 20 staff and its annual expenditure will be about $50 million in its initial year of operation, which will be largely used on investor education work, as the investor education body would be located in SFC's premises and SFC would provide some support services to it. The seven existing staff of SFC engaged in investor education work would be transferred to the new body.

Publication of modification or waiver granted under section 134(1) (clause 37)

56. Clause 37 of the Bill amends section 134(6) and (7) such that SFC is required to publish a modification or waiver it has granted under section 134(1) on the Internet, instead of publication in the Gazette as presently required. The Bills Committee has sought clarification on whether a modification or waiver granted by SFC under section 134(1) is subsidiary legislation, and if so, whether it is appropriate to publish the modification or waiver on the Internet, instead of in the Gazette.

57. The Administration has confirmed that a grant by SFC of a modification or waiver under section 134(1) is not subsidiary legislation. As provided in section 134(1) and (2), such a waiver is granted on an individual basis and is communicated to the applicant by notice in writing. The proposed amendments to section 134(6) and (7) are to require publication of the modification or waiver by SFC on the Internet, rather than in the Gazette. In contrast, class waivers, which are subsidiary legislation, are dealt with in section 134(8) which is not engaged by the proposed amendments.

58. On the suggestion of Bills Committee members, the Administration agrees that the term "on-line medium" should be replaced by "internet", and will move Committee Stage amendments (CSAs) to clause 37 and add new clause 40A in this regard. The Administration has also proposed CSAs for corresponding revisions to section 309(5) under the new clause 40A, and related provisions in the Companies Ordinance under Part 5 (new clauses 44A to 44C).

Commencement

59. Clause 1 of the Bill provides that Part 2 (the PSI disclosure regime) comes into operation on a day to be appointed by the Secretary for Financial Services and the Treasury by notice published in the Gazette, and the rest comes into operation on the day on which the Ordinance is published in the Gazette. The Administration's plan is for Part 2 to commence operation on 1 January 2013. The Administration intends to table the commencement notice at LegCo for negative vetting in May 2012 after passage of the Bill.

Committee Stage amendments

60. Apart from the proposed CSAs mentioned in paragraph 58 above, pursuant to the suggestions of members of the Bills Committee, the Administration has proposed CSAs to the following clauses –

(a) clauses 3 and 24 – to revise proposed sections 307Q(2)(a) and (b) and existing section 262(2)(a) and (b) for copies of the reports of the MMT on its proceedings to be given to SFC and other parties at the same time, instead of providing advance copies of the reports to SFC;

(b) clause 11 – to clarify that the notes in the Bill has no legislative effect; and

(c) clause 36 – to revise the Chinese wording of the amendment under section 109 for clarity in presentation.

61. In response to the observations of the legal adviser to the Bills Committee, the Administration will move CSAs to improve the drafting of the following clauses –

(a) clause 3 – to delete subsection (3) of proposed section 307F, as the circumstance in subsection (3) has already been specified in subsection (1);

(b) clause 19(3) – to revise the Chinese text of proposed section 251(8) to align with the English text of the provision;

(c) clause 3 – to revise the Chinese texts of proposed sections 307I (heading and subsection (2)) and 307J (heading and subsection (1)) to achieve internal consistency;

(d) clause 13(9) – to revise the Chinese text to achieve internal consistency; and

(e) clauses 13(10) and 23(2) – to rectify errors in the Chinese text.

62. The Administration has also proposed the following CSAs to fine-tune the Chinese text of the provisions in the Bill –

(a) clause 3 – in relation to proposed sections 307C(2), 307D(1) and (2), 307I(1) and 307N(1)(d);

(b) clauses 13(2) , 28(1) and (7);

(c) clause 13(11);

(d) clause 20(1);

(e) clause 21; and

(f) clause 44(2).

63. Separately, the Administration has proposed CSAs to Part 4 and clause 29, and add new clauses 33A and 33B to amend Schedule 1 to the Prevention of Bribery Ordinance (POBO) to designate the investor education body to be established in accordance with Part 4 of the Bill as a "public body" under POBO in order to subject the body under the checks and balances of the Independent Commission Against Corruption.

64. The Administration has also proposed a CSA for a technical amendment to section 407 under the new clause 42A(2) to state the effect of the newly added Part 4 of Schedule 10. The new clause 42A(1) rectifies an error in the existing Chinese text of section 407(1) and (2).

65. The Bills Committee agrees to the CSAs proposed by the Administration. The Bills Committee has not proposed any CSA in its name.

Recommendation

66. The Bills Committee supports the resumption of the Second Reading debate on the Bill.

Consultation with the House Committee

67. The House Committee was consulted on 23 March 2012 and supported the recommendation of the Bills Committee in paragraph 66.

Council Business Division 1
Legislative Council Secretariat
20 April 2012

Appendix I

Bills Committee on Securities and Futures (Amendment) Bill 2011

Membership list

Chairman	Hon CHAN Kam-lam, SBS, JP
Members	Hon Albert HO Chun-yan Hon James TO Kun-sun Hon Abraham SHEK Lai-him, SBS, JP Hon Audrey EU Yuet-mee, SC, JP Hon Jeffrey LAM Kin-fung, GBS, JP Hon Andrew LEUNG Kwan-yuen, GBS, JP Hon WONG Ting-kwong, BBS, JP Hon Ronny TONG Ka-wah, SC Hon CHIM Pui-chung Hon Starry LEE Wai-king, JP Hon Paul CHAN Mo-po, MH, JP (Total: 12 Members)
Clerk	Ms Anita SIT
Legal Adviser	Miss Winnie LO

Appendix II

Bills Committee on Securities and Futures (Amendment) Bill 2011

List of organizations and individual which/who have submitted views to the Bills Committee

1. 中信泰富小股東關注組

*2. Association of Chartered Certified Accountants Hong Kong

*3. The Chamber of Hong Kong Listed Companies

*4. China Everbright Holdings Co. Ltd.

*5. The Chinese General Chamber of Commerce

*6. Consumer Council

*7. The DTC Association

8. Debt and Financial Capability Project Service, Caritas Family Crisis Line and Education Centre

9. Economic Synergy

*10. The Hong Kong Association of Banks

11. Hong Kong Bar Association

*12. The Hong Kong Confederation of Insurance Brokers

*13. The Hong Kong Federation of Insurers

*14. Hong Kong Institute of Certified Public Accountants

15. The Hong Kong Institute of Directors

16. Hong Kong Investment Funds Association

17. Hong Kong Securities Professionals Association

*18. The Hong Kong Society of Financial Analysts

19. The Institute of Accountants in Management

*20. Institute of Financial Planners of Hong Kong

21. Mr Johnny CHAN

22. The Law Society of Hong Kong

*23. The Real Estate Developers Association of Hong Kong

*24. SBI E2-Capital (HK) Limited

*25. SFC's Public Shareholders Group

*26. Standing Committee on Company Law Reform

* *submitted written views only*

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.

Appendix IV

Extract of SFC's revised draft Guidelines
(LC Paper No. CB(1)1325/11-12(01))

Examples of possible inside information concerning the corporation

35. 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.

36. 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.

37. 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. For example, what may constitute material information to one party to a contract may be immaterial to another party. Similarly, cancellation of a credit line by a bank which is material to an entity facing liquidity problems may be immaterial to another entity which is highly liquid.

Appendix V

Extract of SFC's revised draft Guidelines
(LC Paper No. CB(1)1325/11-12(01))

60. Under sections 307G(1) and 307G(2)(b), officers must take all reasonable measures from time to time to ensure that proper safeguards exist to prevent a breach of a disclosure requirement. In this respect, officers, including non-executive directors, are responsible to ensure that appropriate systems and procedures are put in place and reviewed periodically to enable the corporation to comply with the disclosure requirements. Officers with an executive role would also have a duty to oversee the proper implementation and functioning of the mechanisms and ensure that any material deficiencies are detected and resolved in a timely manner. In developing the systems and procedures, boards should take into account the particular needs and circumstances of the corporation. The following provides examples of measures which should be considered when establishing systems and procedures. These are not hard and fast rules and should not be taken as a definitive or exhaustive list. It would depend on the specific circumstances to determine whether there was a breach of section 307G(1) or section 307G(2)(b) and the absence of some of the examples below would not be conclusive.

(a) Establish controls for monitoring business and corporate developments and events so that any potential inside information is promptly identified and escalated.

(b) Establish periodic financial reporting procedures so that key financial and operating data is identified and escalated in a structured and timely manner.

(c) Maintain and regularly review a sensitivity list identifying factors or developments which are likely to give rise to the emergence of inside information.

(d) Authorize one or more officer(s) or an internal committee to be notified of any potential inside information and to escalate any such information to the attention of the board.

(e) Maintain an audit trail of meetings and discussions concerning the assessment of inside information.

(f) Restrict access to inside information to a limited number of employees on a need-to-know basis. Ensure employees who are in possession of inside information are fully conversant with their obligations to preserve confidentiality.

(g) Ensure appropriate confidentiality agreements are in place when the corporation enters into significant negotiations.

(h) Disseminate inside information via the electronic publication system operated by the Stock Exchange before the information is released via other channels, such as the press, wire services or posting on the corporation’s website.

(i) Designate a small number of officers or executives with the appropriate skills and training to speak on behalf of the corporation when communicating with external parties such as the media, analysts or investors.

(j) Develop procedures to review presentation materials in advance before they are released at analysts' or media briefings.

(k) Record briefings and discussions with analysts or the media afterwards to check whether any inside information has been inadvertently disclosed.

(l) Develop procedures for responding to market rumours, leaks and inadvertent disclosures.

(m) Provide regular training to relevant employees to help them understand the corporation's policies and procedures as well as their relevant disclosure duties and obligations.

(n) Document the disclosure policies and procedures of the corporation in writing and keep the documentation up to date.

(o) Publish the disclosure policies and procedures of the corporation so that the media and other stakeholders understand the corporation's statutory disclosure obligations.

Appendix VI

Extract of SFC's revised draft Guidelines
(LC Paper No. CB(1)1325/11-12(01))

Officers' liability

57. An officer would only have liability under section 307G(2)(a) **if** (i) the listed corporation is in breach of a disclosure requirement; **and** (ii) the officer's intentional, reckless or negligent conduct resulted in the breach.

58. In the situation where an officer has actual knowledge of information which should have been disclosed the meaning of "intentional", "reckless" and "negligent" can be summarised as follows –

(a) The requirement for conduct to be intentional means that there must be evidence that the officer intended the corporation not to disclose information that was required to be disclosed under a disclosure requirement.

(b) The requirement for conduct to be reckless means that the officer was aware that there was a risk that by not disclosing the information the corporation may breach a disclosure requirement and it was in the circumstances known to him unreasonable to take the risk.

(c) The requirement for conduct to be negligent means the officer failed to exercise such care, skill or foresight as a reasonable officer in his situation would exercise to ensure or cause the corporation to comply with a disclosure requirement.

Assuming a corporation has implemented reasonable measures to prevent a breach, an officer who acts in good faith and in accordance with all his fiduciary duties without actual knowledge of the information or involvement in the corporation's breach is unlikely to be personally liable under any of the elements discussed above.

Obligations of non-executive directors

59. Given the unitary nature of a board and the indivisible legal duties of all directors, both executive directors and non-executive directors should exercise due care, skill and diligence to fulfil their roles and obligations. However, as acknowledged in the Code of Corporate Governance Practices issued by the Stock Exchange[1], non-executive directors normally are not involved in the daily operations of a corporation and would usually rely on a corporation's internal controls and reporting procedures to ensure that, where appropriate, material information is identified and escalated to the board as a whole. It is for this reason that the board's responsibility for establishing and monitoring key internal control procedures is of particular significance for non-executive directors as this is an area where they are more likely to be directly involved. It is therefore more likely that sections 307G(1) and 307G(2)(b) will be of direct relevance to them.

[1] See Listing Rule Appendix 14 - A.5.2. The functions of non-executive directors should include but should not be limited to the following: (a) participating in board meetings of the corporation to bring an independent judgement to bear on issues of strategy, policy, performance, accountability, resources, key appointments and standards of conduct; (b) taking the lead where potential conflicts of interests arise; (c) serving on the audit, remuneration and other governance committees, if invited; and (d) scrutinising the corporation's performance in achieving agreed corporate goals and objectives, and monitoring the reporting of performance.