SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

Consultation Conclusions on (i) the Proposed Code of Conduct on Bookbuilding and Placing Activities in Equity Capital Market and Debt Capital Market Transactions and (ii) the "Sponsor Coupling" Proposal

October 2021

Contents

Executive summary

1. On 8 February 2021, the Securities and Futures Commission (**SFC**) launched a three-month public consultation on proposed conduct requirements for equity capital market (**ECM**) and debt capital market (**DCM**) transactions in Hong Kong (**Consultation Paper**). The proposed requirements are aimed at clarifying the roles played by intermediaries in ECM and DCM transactions and set out the standards of conduct expected of them in bookbuilding, pricing, allocation and placing activities (**Proposed Requirements**). Intermediaries involved in these activities are referred to as capital market intermediaries (**CMIs**) whereas those CMIs acting as the head of the syndicate (such as overall management of an offering, coordinating the bookbuilding or placing activities conducted by other CMIs and providing advice to the issuer) are designated as overall coordinator (**OC**). There was also a separate "sponsor coupling" proposal to require that, for an initial public offering (**IPO**) of shares, there must at least be one OC, which is either within the same legal entity or the same group of companies, which also acts as a sponsor that is independent of the issuer of that IPO (**Sponsor OC**).

2. The consultation ended on 7 May 2021. The SFC received 41 written submissions, including submissions from various industry associations, intermediaries, professional bodies and individuals. A list of respondents is set out in Appendix A.

3. Respondents were generally supportive of the proposed conduct requirements set out under paragraphs 17 and 21 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (**Code**) and the consequential changes made to the Guideline to sponsors, underwriters and placing agents involved in the listing and placing of GEM stocks (**GEM Placing Guideline**). The key comments and the SFC's responses are summarised below.

Key comments

4. Most respondents agreed with the principles and objectives of the Proposed Requirements. In particular, many respondents shared the view that some prevailing market practices in the capital market have encouraged undesirable intermediary behaviour and prevented functional price discovery and transparent allocation. These respondents agreed that the proposals could address issues arising from competitive pressures which might adversely affect the integrity of both the ECM and DCM transactions, better protect the interests of investors and enhance the reputation and status of Hong Kong as an international financial centre. Nonetheless, some respondents commented that the Proposed Requirements might limit issuers' flexibility and aggravate the conflicts of interest between issuers and CMIs. Some respondents were also of the view that the market should be allowed to function on its own and the status quo should be maintained.

5. The SFC welcomes the respondents' general support. In recent years, the SFC has taken a front-loaded approach to promoting market quality and regulating corporate misconduct. The Proposed Requirements are an integral part of the effort to enhance the transparency and promote the fairness and orderliness of our capital markets. Moreover, specific code requirements for intermediaries involved in bookbuilding and placing activities are also necessary to ensure consistency with global regulatory standards and expectations.

Advice on fee arrangements

6. A number of respondents raised concerns that requiring OCs to advise issuers on fee arrangements would result in a conflict of interest on the part of the OCs. Nonetheless, in the case of an IPO, many supported a requirement to determine upfront the total fees[1] and how it should be split between fixed and discretionary fees (**fee split ratio**). Some respondents suggested requiring OCs to (i) discuss and offer views on fee-related issues or (ii) provide transparent market information and comparable transactions as references for issuers to consider.

7. OCs may not always be in a position to provide issuers with fair and unbiased advice on fee arrangements. We will amend the Code to require OCs to provide guidance to the issuer on market practices for the fee split ratio, which is currently around 75% fixed and 25% discretionary (**75:25 ratio**). We also take the view that issuers should assess whether they should deviate significantly from the 75:25 ratio.

Timing of appointment of OCs and syndicate CMIs and fee determination

8. Some respondents were of the view that the syndicate structure and fee arrangements should be determined upfront, such as at the time the issuer submits the listing application (ie, A1 submission), so as to reduce unhealthy competition amongst syndicate members. Others were of the view that the composition of the syndicate and fee arrangements cannot be determined before the Listing Committee Hearing as market conditions and sentiment can fluctuate greatly, requiring adjustments to the syndicate and fees. As such, the OCs may not be able to submit information about the composition of the syndicate and the allocation of fixed fees paid by the issuer to each syndicate CMI four clear business days before the Listing Committee Hearing as required under the Proposed Requirements. Furthermore, this may create problems with small IPOs where most underwriters are unwilling to commit before in-principle approval has been granted by the Listing Committee.

9. Issuers may need the flexibility to appoint more syndicate CMIs at a later stage, especially for IPOs which are not popular or launched in a poor market environment. We will not require OCs to inform the SFC of the composition of the entire syndicate or the allocation of fixed fees to individual syndicate CMIs. The composition of the syndicate will be disclosed at the time of the publication of prospectus, as is the existing practice.

10. Nonetheless, OCs should be appointed at an early stage so that they have sufficient time to understand the issuer, develop marketing, pricing and allocation strategies, properly coordinate the activities of other CMIs and manage the offering. As such, in the case of an IPO, OCs would have to be appointed no later than two weeks after the A1 submission. In addition, OCs would be required to inform the SFC of all the OCs participating in the IPO, the fixed fee payable to each of them, the total fees and the fee split ratio four clear business days before the Listing Committee Hearing.

Disclosure of identities of underlying investors for orders placed on an omnibus basis

11. While respondents generally agreed that where CMIs place orders in the order book on an omnibus basis, they should provide the relevant OC with information about the

[1] This refers to the total fees (as a percentage of the gross amount of funds raised) for both the public offer and the international tranches to be paid to all syndicate CMIs participating in the offering.

underlying investors, some respondents were concerned that the information disclosed would be used by the OCs to poach their clients.

12. It is essential for the identities of underlying investors to be disclosed to allow OCs to properly manage the order book, for example, to identify and eliminate duplicate orders, inconsistencies and errors. To address the concerns about poaching clients, the SFC will amend the Proposed Requirements to:

    (a) specify that a CMI is only required to provide the client's name and unique identification number (such as the identity card or passport number of an investor client who is a natural person); and

    (b) require CMIs (including OCs) which receive information about the investors to use this information only for placing orders for the specific share or debt offering.

"Sponsor coupling"

13. The majority of respondents agreed in principle with the "sponsor coupling" proposal. Some respondents commented that all OCs must be sponsors while some commented that all sponsors should be OCs. On the other hand, some respondents were of the view that the SFC should not codify this practice as it would give the Sponsor OC too much power and lead to conflicts of interest. In addition, some respondents suggested that "sponsor coupling" should not apply to small IPOs as this could disadvantage boutique sponsors, which often do not have underwriting or distribution capacity, as issuers of small IPOs might not wish to appoint more than one sponsor due to concerns about fees.

14. We consider it appropriate to appoint at least one Sponsor OC which would have obtained a good understanding of the issuer through its due diligence work and be in a good position to give quality advice to the issuer throughout the transaction. The SFC also believes that this proposal would not exacerbate conflicts of interest as "sponsor coupling" is already a prevalent market practice for larger IPOs. Nonetheless, we agree that the market ecology for small IPOs is different and that "sponsor coupling" is not as prevalent. As such, the SFC will apply this requirement only to Main Board IPOs.

Implementation timeline

15. To allow reasonable time to implement the necessary operational and system changes to comply with the requirements, the Code will become effective nine months from the date of gazettal. The SFC will also work with The Stock Exchange of Hong Kong Limited (**SEHK**) to introduce appropriate amendments to the Listing Rules[2] which would dovetail with the requirements of the Code in relation to the conduct of issuers and intermediaries involved in bookbuilding and placing activities.

16. The SFC would like to thank all respondents for their time and effort in reviewing the proposals and for their detailed and thoughtful comments.

17. The Consultation Paper, the responses (other than those respondents requested to be withheld from publication) and this paper are available on the SFC's website.

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[2] The Rules Governing the Listing of Securities on SEHK (Main Board Listing Rules) and the Rules Governing the Listing of Securities on GEM of SEHK (GEM Listing Rules) (collectively referred to as "Listing Rules").

Comments received and the SFC's responses

Section I – Proposed scope of coverage

Question:

1. Do you consider the definitions of "bookbuilding activities" and "placing activities" to be clear and sufficient to cover key capital raising activities? If not, please explain.

Public comments

1. The vast majority of the respondents considered the definitions of "bookbuilding activities" and "placing activities" to be clear and sufficient to cover key capital raising activities. Separately, there were suggestions that (i) firms without a mandate should not be permitted to market to investors so that they would not be able to "swarm" the order book at the last minute; and (ii) firms which only relay their clients' orders to the syndicate without owing any duty to the issuer (ie, execution-only non-syndicate CMIs, including private banks) should either not be subject to paragraph 21 of the Code or be subject to lighter requirements.

2. Many respondents sought clarification of whether placing includes settlement and market sounding.

The SFC's responses

3. We appreciate that respondents generally agreed with the two definitions and wish to clarify that placing does not include settlement or market sounding that is conducted to gauge investors' interest before the issuer has decided to pursue a share or debt offering. We agree that if firms without a mandate could not source or market to investors, this should help avoid confusion about the roles of firms in an offering. If we define "placing activities" to include marketing of shares or debt securities to investors pursuant to bookbuilding activities, firms would need to be formally appointed under a written agreement prior to conducting any marketing and this would prevent firms without mandates from "swarming" the order book at the last minute with orders of unknown quality. We also agree that due to the passive role played by execution-only non-syndicate CMIs in the placing process, many of the Proposed Requirements should not apply to them.

4. We would therefore amend the Proposed Requirements so that:

   (a) "placing activities" would now include marketing; and

   (b) execution-only non-syndicate CMIs, for the purposes of paragraph 21 of the Code, should only comply with the requirements for the assessment of investor clients, transparency of the order book, disclosure of rebates offered to CMIs and any preferential treatments of CMIs and targeted investors and not to pass on rebates to investor clients, ie, paragraphs 21.3.3, 21.3.5 and 21.3.7 of the Proposed Requirements.

Question:

2. Do you agree with the proposed scope of coverage for both ECM and DCM activities?

Public comments

5. Most respondents agreed with the proposed scope of coverage of the Code for ECM activities. A few suggested that the Code should only apply to IPOs.

6. Some respondents sought clarification of whether the Code would apply to (i) an offer of existing shares by way of IPO, commonly described as an offer for sale; (ii) private placements and (iii) other types of transactions such as follow-on share issuances, block transactions and secondary offerings.

7. Other respondents suggested that the Code should also apply to non-IPO transactions.

8. Respondents generally commented that the proposed scope covering listed or unlisted debt securities offered in Hong Kong or otherwise could be unnecessarily wide compared to the proposed scope for ECM activities, which only covers shares listed or to be listed on SEHK.

9. Respondents raised concerns about cross-border debt issues as the Proposed Requirements would capture many international debt offerings where the majority of syndicate members are based outside Hong Kong. The minority Hong Kong-based syndicate members would be disadvantaged because the majority of syndicate members based outside Hong Kong would not need to comply with the Proposed Requirements.

10. Owing to the cost of compliance with the Proposed Requirements and the limited Hong Kong connection with many debt offerings, some respondents worried that issuers might apply regulatory arbitrage and not involve Hong Kong-based syndicate members to lessen their compliance burden.

11. Some respondents suggested aligning the proposed scope of coverage for DCM and ECM activities so that only debt securities listed on SEHK are considered in-scope. Other respondents suggested adopting “bright line tests” so that only debt offerings with a significant Hong Kong connection would fall within the scope of the Proposed Requirements. Still others suggested criteria for the bright line tests such as “Asia-centric” and/or publicly tradable.

12. Separately, some respondents sought clarification on whether equity-linked convertible bonds and exchangeable bonds should be considered equities or debt securities under the Proposed Requirements.

The SFC’s responses

13. In response to the clarification sought by respondents, we wish to first point out that the terms used by respondents (such as block transactions and secondary offerings) could mean different types of transactions to different market participants. As such, instead of categorically stating that the Code is applicable to certain transactions, we wish to clarify that the Code does not cover offerings which do not involve bookbuilding activities, such as:

(a) bilateral agreements or arrangements between the issuer and the investors (sometimes referred to as "club deals");

(b) transactions where only one or several investors are involved and the terms of the offering are negotiated and agreed directly between the issuer and the investors (sometimes referred to as "private placements"); and

(c) transactions where shares or debt securities are allocated to investors on a pre-determined basis at a pre-determined price.

The Proposed Requirements also does not cover a share offering which has been subscribed by an intermediary as principal deploying its own balance sheet, for onward selling to investors (sometimes referred to as "block transactions") or selling of listed shares by existing shareholders (sometimes referred to as "secondary offering").

14. The scope of coverage for ECM activities will be limited to the following types of offerings, provided that bookbuilding is involved:

(a) the offerings of shares[3] to be listed on SEHK. This includes (i) IPOs, which include share offerings in connection with a secondary listing and offer of existing shares by way of IPO; (ii) offerings of shares of a class new to listing or an offering of new shares of a class already listed under a general or special mandate; and

(b) the placing of listed shares to third-party investors by an existing shareholder if it is accompanied by a top-up subscription by the existing shareholder for new shares in the issuer.

Paragraph 21.1.2 of the Code will be revised to clearly specify the types of offerings covered.

15. Regarding the suggestion to expand coverage to all non-IPO transactions, we maintain that our proposed scope is appropriate but will keep in view the need to cover more transactions in the future.

16. We recognise the significant differences between DCM and ECM activities and that a relatively high percentage of debt offerings in Hong Kong are executed over-the-counter. Therefore, the SFC considers the scope of coverage for DCM activities should not be limited to those listed in Hong Kong.

17. The SFC also considers that the scope would inevitably be too narrow if the suggested criteria in the bright line test were adopted (eg, whether the debt securities are listed in Hong Kong; or the issuers are listed in Hong Kong etc).

18. Furthermore, we are of the view that the suggestion to define the scope to cover debt offerings which are Asia-centric and publicly tradable may not be practical due to the following:

(a) the application of the Proposed Requirements should not be limited to certain types of debt offerings or depend on where the issuers are located;

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[3] This includes depositary receipts, units or interests in SFC-authorised real estate investment trusts listed or to be listed in Hong Kong.

(b) the definition of "Asia-centric" would be subject to interpretation; and

(c) the concern about a limited Hong Kong connection may not be fully addressed by expanding the scope to "Asia-centric" debt offerings, as the majority of syndicate members may still be based outside Hong Kong.

19. Given the fact that (i) a significant portion of debt offerings in Hong Kong are executed over-the-counter and (ii) the scope of coverage should be defined based on regulated activities conducted in Hong Kong so that the Proposed Requirements can address conduct issues, we consider it appropriate to cover regulated activities stated in the proposed paragraph 21.1.2 in respect of an offering of listed or unlisted debt securities offered in Hong Kong or otherwise.

20. In response to the clarification sought, we consider that convertible or exchangeable bond offerings are generally structured in the form of debt securities which may not always be converted into equity securities. Therefore, offerings of convertible or exchangeable bonds where the bookbuilding or placing activities are conducted in Hong Kong would fall under the scope of DCM activities.

Section II – Proposed types of CMIs

Question:

3. Do you consider the role of an OC to be properly defined? If not, please explain.

Public comments

21. The majority of respondents considered the role of an OC to be properly defined. However, one respondent suggested that non-OC syndicate CMIs should also be allowed to perform the same function as an OC, ie, discuss with and advise the issuer on the final offer price.

22. Separately, one respondent suggested that an OC should be defined as a CMI that conduct all the activities in paragraph 21.2.3 of the Proposed Requirements, and not at least one of them.

23. For share offerings, a few respondents suggested that "acting as a stabilising manager" should not be one of the activities specified in paragraph 21.2.3. Other respondents suggested removing the concept of OC for non-IPO transactions given that OCs would find it difficult to comply with the Proposed Requirements due to the compressed timeframe and that significant issues had not been identified with non-IPO transactions.

24. For debt offerings, some respondents also suggested removing the concept of OC and made reference to the regulatory regimes in other jurisdictions where there is no "tiering", ie, no particular syndicate members would have additional or higher levels of responsibility.

The SFC's responses

25. We understand the respondents' concerns about OCs' potential difficulty in complying with the Proposed Requirements in non-IPO transactions and recognise that there are many types of share and debt offerings and they vary in nature and complexity. That said, we have made it clear in paragraph 21.1.4 of the Proposed Requirements that CMIs are

expected to establish and implement policies, procedures and controls, which are commensurate with the nature and complexity of the transaction to ensure compliance with the applicable rules and regulations. Where the transaction only takes a few hours to complete, CMIs may not conduct in-depth discussions with and provide detailed advice to the issuer client. In these cases, the OCs should, at a minimum, document the basis for determining the final offer price and allocation.

26. For share offerings:

    (a) we do not consider it appropriate to define an OC as a firm which conducts all the activities in paragraph 21.2.3 as each activity is key to the offering and should only be carried out by an OC; and

    (b) we agree to amend the Proposed Requirements by excluding "acting as a stabilising manager" from paragraph 21.2.3 as the stabilising manager's role is not central to the functions of an OC.

27. Similarly, OCs play a lead role in the syndicate for debt offerings and thus should shoulder greater responsibilities compared to the other syndicate members. While we appreciate the differences in other jurisdictions' regulatory regimes, we consider that those syndicate members which have greater influence should be subject to additional conduct requirements.

Section III – Proposed standards of conduct expected of OC and CMIs

I. Appointment of CMIs and OCs

Question:

4. Do you agree that the appointments of OCs and other CMIs and the determination of their roles, responsibilities and fee arrangements, should all take place at an early stage? If not, please explain.

Public comments

28. Slightly more than half of the respondents supported appointing syndicate CMIs and determining fees at an early stage. One respondent fully supported this proposal as it clarified syndicate roles and responsibilities and fixed the overall syndicate remuneration. Other respondents expressed some reservations. Some suggested allowing greater flexibility in the early appointment arrangement, especially in light of changing or volatile market conditions. Others stressed the importance of allowing issuers to reward last-minute marketing efforts to ensure the success of an offering.

29. For share offerings, respondents which supported determining syndicate membership and fee allocations at an early stage considered that the syndicate should be established upfront. If the syndicate was not formed early on, too many CMIs would otherwise chase orders and not focus on helping the market find the price equilibrium to ensure the success of the listed company post-IPO. A number of respondents suggested that, for IPO transactions, all OCs should be appointed at A1 submission. Others suggested that all syndicate CMIs should also be appointed at or before A1 submission.

30. However, some respondents took the view that requiring the OC to notify the SFC of the composition of the syndicate and the allocation of fixed fees to each syndicate CMI four

clear business day before the Listing Committee Hearing would not be practical, as many non-OC syndicate CMIs, especially for smaller IPOs, would generally be unwilling to commit before the Listing Committee Hearing due to the uncertainty of obtaining listing approval and market sentiment. Typically for smaller IPOs, non-OC syndicate CMIs would not commit before the result of the Listing Committee Hearing was known. Some suggested allowing flexibility for issuers to change the structure of the syndicate and allocation of fees at a later stage. One respondent even suggested allowing OCs to join the syndicate at a late stage. One respondent commented that the SFC should not need this information before the Listing Committee Hearing as its purpose is more to confirm the suitability of an IPO candidate.

31. For debt offerings, one respondent disagreed with the proposal to appoint OCs and CMIs at an early stage, pointing out that flexibility should be allowed for frequent issuers to appoint CMIs at a later stage and that issuers' commercial decisions around fees would impose constraints at the early stage.

The SFC's responses

32. For IPO transactions, it is of paramount importance that OCs be given sufficient time to understand the issuer, develop marketing, pricing and allocation strategies, properly coordinate the activities of other CMIs and manage the offering. The requirements for the early appointment of OCs (ie, two weeks after A1 submission) and determining their fees at the outset (including fixed fees and fee payment schedules) remain unchanged. We will also require that the list of all the OCs, the fixed fee payable to each OC, the total fees and the fee split ratio be submitted to the SFC four clear business days before the Listing Committee Hearing to allow us to make enquiries. The above changes are reflected in the revised paragraph 21.4.8 of the Code.

33. We note respondents' concerns that issuers might need to appoint more syndicate CMIs at a later stage, especially for IPOs which are not popular or in a poor market environment. To provide flexibility, we will therefore no longer require that the appointment of non-OC syndicate CMIs and the determination of their fees be reported to the SFC. However, all CMIs will still be required to be appointed before conducting any bookbuilding or placing activities. This should allow CMIs to evaluate whether they wish to accept the appointment based on their fixed fee entitlement and determine the resources they should deploy.

34. Flexibility is already provided for the appointment of OCs and CMIs during the debt offering process. Before OCs and CMIs conduct any bookbuilding and placing activities in Hong Kong, they are only required to be formally appointed by issuers under a written agreement which specifies their roles and responsibilities, fixed fee entitlement and fee payment schedule. We consider that this requirement could enhance the certainty of syndicate members' roles and responsibilities as well as their remuneration.

II. Advice to the issuer

Question:

5. Do you agree that an OC should provide advice to the issuer on: (i) syndicate membership and fee arrangements; (ii) marketing strategy; and (iii) pricing and allocation? If not, please explain. What else should the OC advise the issuer about?

18. Do you agree with the scope of fee-related advice to be provided by an OC to an issuer? If not, please explain.

19. Would you envisage substantial practical difficulties in an issuer determining the syndicate membership, the ratio between the fixed and discretionary portions of the fees to be paid to all syndicate CMIs and fixed fees allocation four clear business days before the Listing Committee Hearing? If yes, please cite examples.

Advice by OC

Public comments

35. A few respondents felt that advice should be given by the whole syndicate or that non-OC syndicate CMIs should be able to give limited advice in response to an issuer's request.

36. For share offerings, a few respondents suggested that the issuer should be advised by an independent financial adviser which is not part of the syndicate, such as a sponsor, to avoid potential conflicts of interest.

The SFC's responses

37. We maintain the view that OCs, being overall-in-charge, are in the best position to advise the issuer and should be held accountable for (i) advising on the offer price while being a party to the price determination agreement with the issuer; and (ii) making allocation recommendations.

38. We are of the view that an independent financial advisor, which is not part of the syndicate and hence not participating in the day-to-day bookbuilding process, may not be able to properly gauge investor sentiment and interest in the transaction. As a result, the independent financial advisor may not be in the position to advise the issuer on the pricing and detailed allocation decisions or act as the OC. Nonetheless, we wish to clarify that issuers can continue to appoint financial advisers or other professionals which only provide advice to the issuer and they would not be considered to be a CMI as long as they do not participate in any bookbuilding or placing activities.

Syndicate membership and fee arrangements

Public comments

39. For both share and debt offerings, a large number of respondents, including representatives from both the buy-side and the sell-side, expressed reservations about an OC providing advice to an issuer on syndicate membership and fee arrangements. Many of them had concerns about potential conflicts of interest and that this proposal could work against the interests of issuers. One respondent also pointed out that the roles of OCs and other CMIs are often dictated by market conditions and through commercial negotiations.

40. A few respondents suggested requiring the OC to discuss and offer views on fee-related matters or provide transparent market information and comparable transactions as references for the issuer to consider.

41. Separately, a few respondents suggested that the fee split ratio should be codified at 75:25 given that is the prevalent market norm.

The SFC's responses

42. Noting these concerns, we will not require OCs to provide advice to the issuer on syndicate membership or fee arrangements.

43. For IPOs, when an OC is no longer required to advise the issuer on the basis for the allocation of fixed and discretionary fees to syndicate CMIs, we agree that the issuer should at least be informed of the 75:25 ratio. In this connection, we will require an OC to provide guidance to the issuer on the market's fee split practice. Furthermore, we will require the fee split ratio to be reported to the SFC four clear business days before the Listing Committee Hearing. This would give the SFC an opportunity to make enquiries where the ratio significantly deviates from 75:25. Moreover, if any material changes are subsequently made to the ratio reported to the SFC, the OC should notify the SFC as soon as practicable. Together, these measures should alleviate some of the concerns about fluid incentive structures and help prevent last-minute scrambles for orders and fees. These changes have been reflected in the revised paragraph 21.4.2(b)(i) of the Code. For ease of reference, we have summarised requirements that govern the appointment of syndicate CMIs and the determination of their fee entitlements as well as the respective timeframes in Appendix D. Separately, given that fees should be agreed through commercial negotiations, it is not appropriate to codify the fee split ratio in the Code.

44. For debt offerings, we will only require CMIs (including OCs) to be formally appointed under a written agreement, which should clearly specify the CMI's roles and responsibilities, the fee arrangements and the fee payment schedule.

Marketing strategy and pricing and allocation

Public comments

45. The majority of respondents agreed that an OC should provide advice to the issuer on marketing strategy and pricing and allocation.

46. Nonetheless, for both share and debt offerings, two respondents were concerned that the proposals would create disincentives for CMIs to work hard to secure adequate demand to support a higher price. For example, the CMI may seek to price the offering below its fair market value to favour its investor clients and allow them to subscribe to the securities at a lower cost. However, this may go against the interests of the issuer as less funds will be raised.

47. For share offerings, a few respondents commented that OCs should not advise issuers on allocation or else OCs could provide large allocations of hot IPOs to "preferred" clients.

The SFC's responses

48. The risk of under-pricing could be a problem if issuers were in a weak bargaining position, but this is understood not to be the case in Hong Kong. Moreover, it may not be in the interest of OCs to set a lower offer price as this may generate less fees. Most importantly, we maintain the view that for both share and debt offerings it is essential for OCs to advise the issuers on pricing and allocation in order to balance the interests of different parties and promote transparent and effective price discovery. Regardless, the issuer still has the final say on price and allocation; the OC would only need to explain the potential concerns and advise the issuer appropriately. It is also worth pointing out that, under the Proposed Requirements:

(a) a CMI (including an OC) should establish, implement and maintain policies and procedures to identify, manage and disclose actual and potential conflicts of interest which may, for example, arise when that CMI serves the interests of both its issuer and investor clients; and

(b) an OC should also follow a marketing and investor-targeting strategy agreed with the issuer client, and explain to the issuer client when the allocation recommendations materially deviate from its allocation policy that has been communicated to the issuer.

III. Rebates and preferential treatment

Question:

6. Do you agree that a private bank should not pass on to investor clients any rebates provided by the issuer? If not, please explain.

Public comments

49. A few respondents suggested that rebates in whatever form, including rebates to private banks and investor clients, should be banned entirely to maintain a level playing field.

50. For debt offerings, the majority of respondents agreed that private banks should not pass on rebates to their investor clients to prevent end investors paying different prices for the same debt securities.

51. A number of respondents raised concerns about whether syndicate CMIs could in practice police the conduct of private banks, commenting that "it is the obligation of the recipient of a rebate to comply with its own fiduciary obligations as well as the Proposed Requirements and other application regulations".

52. For IPOs, one respondent sought clarification of whether rebates from the CMIs to the end investors in the form of a reduction of the 1% brokerage fee is allowed. Two respondents took the view that disallowing reductions of brokerage fees would have an adverse impact on small and medium brokers.

The SFC's responses

53. The aim of disallowing rebates is to prevent investor clients paying different prices for the same debt securities. While we acknowledge that some respondents wanted to go further to ban rebates entirely in whatever form, we consider that rebates offered by issuers to intermediaries as incentives for their selling efforts should remain, provided that they are not passed on to investor clients and properly disclosed as stipulated in paragraph 21.3.7 of the Code.

54. Syndicate CMIs will not be responsible for policing conduct requirements for private banks' rebate arrangements. Private banks (as execution-only non-syndicate CMIs) will be required to comply with the requirement not to pass on rebates to investor clients stipulated in paragraph 21.3.7 of the Code.

55. For IPOs, the SFC would like to clarify that under the Listing Rules[4] rebates to investor clients through a reduction of brokerage commission are not allowed.

IV. Assessment of investor clients

Question:

7. Do you agree that an OC should provide relevant information to CMIs to enable them to identify investor clients which are Restricted Investors in share offerings or have associations with the issuer in debt offerings? If not, please explain.

Public comments

56. The majority of respondents agreed that this information should be provided by OCs to CMIs. However, two respondents argued that it should be the issuer's obligation to identify investor clients to whom the allocation of shares will be subject to restrictions or require prior consent from SEHK (**Restricted Investors**) in share offerings or have associations with the issuer, CMIs or companies in the same group of companies[5] as the CMI (**group companies**) in debt offerings.

57. A few respondents raised concerns about OCs' responsibility (including liability for the accuracy and completeness of the information) as well as the potentially onerous burden. Some respondents commented that it may be difficult to (i) implement if there is more than one OC and (ii) ensure that all CMIs have the same information. One also expressed concern that the OC might not be able to assess the accuracy and completeness of the information.

58. For share offerings, some respondents suggested that a better way would be to amend the Listing Rules to require the issuer to provide the information directly to all syndicate CMIs or require sponsors to provide the list of connected persons.

59. For debt offerings, a number of respondents sought clarification of the definition of "associations" with the issuer client, the CMI or a company in the same group of companies as the CMI.

60. One respondent raised a concern that the requirements for the CMI to assess its investor clients based on their profiles, such as investment preferences and past investment histories, contradicted the existing exemptions available for Professional Investors under paragraphs 15.4 and 15.5 of the Code.

The SFC's responses

61. For share offerings, we agree that it would be more direct and efficient for the issuer to disseminate the relevant information to all the syndicate CMIs. Therefore, instead of requiring an OC to provide relevant information to syndicate CMIs, we will require an OC

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4 LR2.03(2) of the Main Board Listing Rules and LR2.06(2) of the GEM Listing Rules: "the issue and marketing of securities is conducted in a fair and orderly manner" and LR2.03(4) of Main Board Listing Rules and LR2.06(4) of the GEM Listing Rules: "all holders of listed securities are treated fairly and equally".

5 For the purposes of the Proposed Code, "group of companies" has the same meaning as in section 1 of Part 1 of Schedule 1 of the Securities and Futures Ordinance.

to specifically advise the issuer of the information which should be provided to syndicate CMIs to identify the issuer's directors and existing shareholders as well as the directors' and shareholders' close associates and nominees for the subscription or purchase of shares offered in the IPO. At the same time, CMIs will still be required to identify whether their investor clients are Restricted Investors and inform the OC. We will work with SEHK to reflect in the Listing Rules or appropriate guidance letters the role of the issuer in connection with the above matters.

62. Similarly, for debt offerings, we will require an OC to advise the issuer client to provide sufficient information to all syndicate CMIs to enable them to reasonably identify whether investor clients have any associations with the issuer client. In addition, an OC is expected to take all reasonable steps to identify whether investor clients have any associations with the issuer client, CMIs or their group companies, such that the OC could manage conflicts of interest by taking into consideration whether orders placed by these investor clients may negatively affect the price discovery process.

63. In respect of debt offerings, we expect that investor clients which are directors, employees or major shareholders of the issuer client, the CMIs or their group companies would be considered to have "associations" with the stated parties. We will clearly specify who would be considered as having associations with the stated parties in the revised paragraph 21.3.3 (c) of the Code.

64. Regarding the comment that the Proposed Requirements contradict the existing exemptions available for Professional Investors, we wish to clarify that, irrespective of whether the investor client is a Professional Investor, CMIs are required to assess the investor client's profile under the Proposed Requirements for the purpose of ascertaining whether the investor client is one of the types of investors specified in the marketing and investor targeting strategy. The two examples (ie, "investment preferences" and "past investment histories") cited under paragraph 21.3.3(a) of the Proposed Requirements were provided for illustrative purposes and have been deleted to avoid confusion. CMIs may use appropriate factors to assess their investor clients' profiles.

V. Order book

Question:

8. Do you agree that information about the underlying investors should be provided to an OC by CMIs placing orders on an omnibus basis when they place orders in the order book? If not, please explain.

Public comments

65. The majority of respondents agreed with the proposal but many were concerned that client information is a commercial secret and disclosing it to competitors may result in client poaching.

66. One respondent suggested that disclosure should only be required for orders over a certain threshold (eg, 3% of the offer) and with client consent. On the other hand, one respondent suggested full transparency ie, all names should be disclosed in the order book with no-poach agreements in place.

67. Many respondents sought clarification of the meaning of "placing orders on an omnibus basis" and "underlying investors" and asked for examples of information which a CMI would need to provide to the relevant OC.

The SFC's responses

68. For share offerings, we acknowledge that placee lists have always been separately submitted to the SEHK by individual CMIs and these CMIs are very worried about potential poaching. However, OCs should have full transparency to properly manage the order book and, among other things, identify and eliminate duplicate orders, inconsistencies and errors. We would therefore amend the Proposed Requirements to require:

    (a) a CMI to only provide the name and unique identification number of the underlying investor clients to the OC and the issuer when placing an order on an omnibus basis; and

    (b) a CMI (including the OC) which receives information about the underlying investor clients to only use this information for placing orders for the specific share or debt offering.

    The above changes are reflected in revised paragraphs 21.3.5(b) and (c) of the Code.

69. We also wish to clarify that:

    (a) placing orders on an omnibus basis refers to where a CMI (such as a private bank) acts as an agent and has aggregated the orders of two or more investor clients for placing in the order book in the CMI's name; and

    (b) subject to the Listing Rules, fund managers which place orders only for funds and discretionary accounts under their management will not be required to disclose the names of these funds or discretionary accounts to the OC or issuer when placing those orders.

Question:

9. Do you think there would be difficulties in a large IPO or debt offering for OCs to remove duplicate orders and identify irregular or unusual orders in the order book? If so, please provide examples.

Public comments

70. Most respondents saw no or few difficulties for OCs to remove duplicate orders and identify irregular or unusual orders in the order book. However, a few respondents considered that it would be hard to determine what orders were irregular or unusual. Two respondents pointed out that OCs might not have the first-hand client order information needed to identify irregular or unusual orders.

71. One respondent suggested that we should clarify that the primary obligation to place genuine orders lies with the investors. Two respondents commented that the OC should have power to request investor profiles from the CMIs.

72. A few respondents suggested that duplicate orders could be removed by SEHK, for example, by making use of the FINI platform.

The SFC's responses

73. We welcome the overwhelming support and will proceed with these requirements. Managing the order book properly is a key role played by the OC during the bookbuilding and allocation process and it cannot be delegated to FINI which deals with placee information only after bookbuilding and allocation. An OC is only required to take all reasonable steps to remove duplicate orders and identify irregular or unusual orders or errors in the order book. It will be adequate for the OC to demonstrate that it has developed and implemented effective systems and controls. Separately, it should not be necessary to empower the OC to obtain client information from the CMIs. We expect the OC to make due enquiries with the CMIs upon identifying any irregular or unusual orders and take client information supplied by the CMIs into consideration when making allocation recommendations.

74. As for examples of irregular or unusual orders, we generally expect an OC to make enquiries where the name of an investor client suggests that it is related to the issuer client.

Question:

10. Do you agree that OCs and CMIs should not accept knowingly inflated orders? If not, please explain.

Public comments

75. Most respondents agreed that OCs and CMIs should not accept knowingly inflated orders. However, a few respondents believed that as long as the orders are firm or investors are willing to bear the risk, the orders should be accepted.

76. A few respondents asked for the definition of "knowingly inflated orders" or commented that they are hard to identify. One respondent suggested that we should clarify that the primary obligation to place genuine orders lies with investors.

The SFC's responses

77. We wish to stress that OCs and CMIs are not required to second-guess the intentions of their investor clients. However, when investor clients instruct the CMI to, among other things, place an order whose amount is larger than what the clients indicated that they anticipate to be allocated, the CMI should clarify with clients the size of the order they wish to place to the order book and confirm that they are willing to take up the full allocation. Before placing the order, CMIs are also required under paragraph 21.3.5 (a) of the Code to make enquiries with the investor clients if the order is not commensurate with the investor client's financial profile.

78. While the Code does not govern investors' behaviour, the SFC will not hesitate to take appropriate action against investors engaged in any market misconduct.

Question:

11. Do you agree that OCs should ensure the transparency of the order book? If not, please explain.

Public comments

79. Many respondents agreed that OCs should ensure the transparency of the order book. One respondent pointed out that transparent order books are vital to the healthy functioning of the market.

80. A few respondents considered that transparency should be the responsibility of the issuer but not the OC and one respondent stated that transparency should be the responsibility of both the issuer and the syndicate. One respondent sought clarification of the degree of transparency required, while another suggested that information such as addresses or telephone numbers should not be revealed in light of privacy concerns and commercial sensitivities.

81. A few respondents argued that book updates should not be compulsory. Another encouraged compulsory book updates throughout the bookbuilding process.

The SFC's responses

82. The transparency of the order book is of paramount importance and therefore this requirement should remain unchanged. We believe that limiting the transparency of the orders to the OCs and the issuers strikes an appropriate balance. As regards the degree of transparency required, we would generally consider it sufficient to provide investor clients' names and unique identification numbers.

83. In relation to book updates, we maintain our view that the OC should disseminate material information related to the offering in a timely manner to all syndicate CMIs.

Question:

12. Do you agree that "X-orders" should be prohibited? If not, please explain.

Public comments

84. The majority of respondents supported prohibiting the use of "X-orders" in the order book for debt offerings. They envisaged that the OCs would be able to efficiently identify and remove duplicate orders when the identities of all investors are clearly disclosed in the order book.

85. Nevertheless, some respondents suggested that exemptions should be granted for debt offerings to entities with a legitimate reason to make limited use of "X-orders" such as sovereigns, central banks and state-owned companies. They further elaborated that in some jurisdictions, it might be illegal to reveal the identities of certain sovereigns, central banks, and state-owned companies in the order book due to privacy laws.

86. Furthermore, some respondents raised concerns that the commercial interests of CMIs might be jeopardised if "X-orders" were not allowed. They worried that OCs will poach CMIs' investor clients if their identities are disclosed. They also commented that some CMIs will place orders through private banks to circumvent the need to disclose the identities of their investor clients.

The SFC's responses

87. Given that the majority of respondents supported the prohibition of "X-orders" in the order book, the requirement as stipulated in paragraph 21.3.5(b) and paragraph 21.4.4(a)(i) of the Proposed Requirements will remain unchanged.

88. We do not agree to grant exemptions for the use of "X-orders" because disclosing the identities of investor clients in an order book is fundamental to ensure transparency during the bookbuilding process.

89. We note respondents' concerns about the commercial interest of CMIs and will amend the Proposed Requirements as explained in paragraph 68 above. We have also clarified in paragraph 69 above that placing orders through private banks would be considered to be placing orders on an omnibus basis and thus these client orders would be required to be disclosed as stipulated in paragraph 21.3.5 of the Code.

VI. Pricing and allocation

Question:

13. Do you agree that OCs and CMIs should be required to establish and implement allocation policies? If not, please explain.

Public comments

90. There was broad support for the proposal for CMIs to establish and implement allocation policies. Some respondents considered that allocation policies would be beneficial to address the conflicts of interest that exists in an offering.

91. Whilst supporting the proposal, a few respondents took the view that the policy should be principle-based and that there should be flexibility in exceptional circumstances.

92. A few respondents also suggested additional consideration factors to be included in the allocation policy including targeted investors' integrity, past behaviour, indicated interests, sophistication, reputation and contribution to the price discovery process.

93. One respondent commented that it is hard to determine what a fair allocation would be or what factors should be taken into account, especially the spread of investors, before a book is built.

The SFC's responses

94. CMIs are only required to address or take into account certain factors, principles and requirements in developing their allocation policies which are expected to be general and broadly suitable for most share and debt offerings. CMIs may modify them as needed on a case-by-case basis. One factor to be taken into account is the circumstances of the investor clients and this can include any relevant aspects. As such, this requirement will remain unchanged.

VII. Conflicts of interest and proprietary orders of CMIs and their Group Companies

Question:

14. Do you agree that client orders must have priority over proprietary orders at all times? If not, please explain.

15. Do you agree that proprietary orders can only be price takers? If not, please explain.

Public comments

95. We received a number of responses supporting our proposal that client orders must have priority over proprietary orders at all times, and proprietary orders can only be price takers.

96. Some respondents sought clarification of the definition of "proprietary order" and suggested that it should be properly defined. They explained that in general there are three types of intra-group orders which raise concerns: (i) orders from syndicate members' asset management arms; (ii) orders from syndicate members' treasury functions; and (iii) orders from syndicate members' trading desks.

97. Most of these respondents suggested that orders from syndicate members' asset management arms and treasury functions should not be classified as "proprietary orders". These orders represent genuine demand and should be treated pari passu with other client orders (ie, not lower priority and not as a price taker) as long as they are placed on an arm's length basis and the firms have Chinese Wall controls in place to prevent the free flow of confidential or price sensitive information. Respondents agreed that orders from syndicate members' trading desks should be treated as proprietary orders subject to lower allocation priority according to international DCM practices.

98. Some respondents disagreed that client orders should have priority over proprietary orders and proprietary orders should only be price takers in debt offerings. They pointed out that proprietary orders placed on an arm's length basis represent genuine demand and should be treated pari passu with client orders. Proprietary orders often bring momentum to, and help sustain, the order book. In some cases, they serve as anchor support without which the entire debt offering may fail.

The SFC's responses

99. We agree with the majority of respondents that orders from syndicate members' trading desks should be treated as proprietary orders. We also agree that orders from syndicate members' asset management arms should be treated as client orders, provided that the orders are placed on an arm's length basis and effective Chinese Wall controls are in place. A note has been included in paragraph 21.3.10(b)(iii) of the Proposed Requirements clarifying that "proprietary orders of a group company exclude orders placed by the group company on behalf of its investor clients or funds and portfolios under its management, but include orders placed on behalf of funds and portfolios in which a CMI or its group company has a substantial interest".

100. However, we do not share the view that orders from syndicate members' treasury functions should be treated as client orders. The treasury function is responsible for

managing the firm's capital and making investment decisions. A potential conflict of interest may arise when the firm is committing its capital in a debt offering and the syndicate desk of the firm is exercising control over bookbuilding activities and making pricing and allocation recommendations to the issuer client. Therefore, orders placed by the treasury function of a CMI will be treated as that CMI's proprietary orders.

101. The overarching objective of this requirement is for CMIs to address conflicts of interest in debt offerings. We believe requiring client orders to have priority over proprietary orders and proprietary orders to only be price takers in debt offerings is consistent with the fundamental principle of the existing Code and the IOSCO DCM Report[6] which pointed out the need to appropriately manage potential or actual conflicts of interest and associated conduct risks when the intermediary, when providing services to its clients, has a proprietary interest in the transaction. Therefore, we maintain the view that client orders must have priority over proprietary orders and proprietary orders can only be price takers in debt offerings.

Question:

16. Do you agree that a CMI's proprietary orders and those of its Group Companies should also include orders placed on behalf of funds and portfolios in which a CMI or its Group Companies have a substantial interest? If not, please explain.

Public comments

102. A few respondents sought clarification of the meaning of "substantial interest".

The SFC's responses

103. If the CMI or its group company has more than 50% interest in the fund or portfolio, it will be regarded as "substantial" and the orders from that fund or portfolio should be treated as proprietary orders.

VIII. Keeping of records

Question:

17. Orders received and entries placed in the order book are subject to constant amendments and updates throughout the bookbuilding process. Do you think it is feasible for the OC and CMIs to maintain records which evidence every change? If not, please explain.

[6] Report on conflicts of interest and associated conduct risks during the debt capital raising process issued by the International Organization of Securities Commissions (**IOSCO**) in September 2020 (**IOSCO DCM Report**).

Public comments

104. More than half of the respondents considered that this is feasible. Those in favour were of the view that with technology, keeping the order book updated is feasible and it is important to ensure the accuracy and transparency in the bookbuilding process. One respondent stated that keeping a complete, reliable audit trail for regulatory review is part of an intermediary's responsibilities.

105. However, some respondents believed that this would be burdensome and suggested that only key discussions or final allocations should be recorded. One respondent suggested that a day-end review and update would be sufficient.

106. A few respondents pointed out that using electronic platforms, Bloomberg chats or emails for the bookbuilding process should already record the needed information.

107. One respondent suggested we provide a quantifiable range and only require changes exceeding this range to be recorded.

The SFC's responses

108. It should be feasible for OCs and CMIs to maintain records of all changes made to the order book, especially given the proliferation of electronic means which intermediaries can adopt when conducting bookbuilding activities. Setting a quantifiable range would be arbitrary and hence undesirable. OCs and CMIs should keep proper audit trails, from order generation and modification to allocation, for their own protection as well as to protect their investor clients.

IX. Fee arrangement

Question:

20. Would you envisage substantial difficulties in issuers determining the allocation of discretionary fees and the fee payment schedule no later than listing? If yes, please cite examples.

Public comments

109. Most respondents did not foresee significant difficulties. A few commented that this is the market practice for most IPO transactions.

110. A few respondents suggested that the timing for determining the allocation of discretionary fees should be after the stabilisation period in order for issuers to incentivise the syndicate's after-market performance.

111. Two respondents commented that fee should be paid at settlement. One respondent suggested that a breach of the payment schedule should be reported to the SFC.

The SFC's responses

112. The SFC shares the view that the determination of these items before listing can encourage greater discipline in the market and provide more certainty to market participants, which are conducive to a healthier market.

113. However, we regard the timing for fee payment and the enforcement of the fee payment schedule to be commercial matters which the SFC is not in a position to intervene.

114. Furthermore, as we will not require OCs to advise issuers on fee arrangements, we will also not require OCs to confirm to us that the issuer has determined the allocation of discretionary fees to each syndicate CMI and the fee payment schedule no later than listing. Nonetheless, the SFC will explore with the SEHK on the possibility of requiring issuers to confirm directly that they have determined the allocation of discretionary fees to each syndicate CMI and the fee payment schedule no later than listing.

115. On a separate note, we would like to reiterate that post-IPO price performance should not be a consideration for the allocation of discretionary fees.

Question:

21. Do you agree that (i) the syndicate membership (including the names of OCs) should be disclosed at an early stage; (ii) the total fees to be paid to all syndicate CMIs participating in the offering for the international placing tranche should be disclosed in the prospectus; and (iii) the total monetary benefits paid to each syndicate CMI should be disclosed after listing? If not, please explain.

Disclosure of syndicate membership

Public comments

116. For share offerings, the majority of the respondents agreed that syndicate membership should be disclosed at an early stage. A few respondents commented that this disclosure should be made at A1 submission as this would help enhance market transparency at an early stage and lock in all the syndicate CMIs. However, a few respondents suggested maintaining the status quo of making the disclosures only at the time of the publication of prospectus. These respondents were of the view that changes in market conditions and sentiment may necessitate the addition of CMIs and OCs, particularly for small IPOs.

117. A few respondents suggested that all syndicate CMIs should be disclosed while others suggested limiting it to OCs only.

The SFC's responses

118. We appreciate why the buy-side would welcome early disclosure of syndicate membership. However, as explained in paragraph 33 above, it may not be feasible to prescribe a timeframe for the appointment of syndicate CMIs for all IPO transactions. As we now define "placing activities" to include "marketing", firms without mandates approaching potential investors would be in breach of the Code. Hence, the buy-side should reasonably assume that it would only be approached by CMIs which have been appointed by the issuer for the offering.

119. We also agree in principle that public disclosure of the OCs should be made at an early stage of the offering so that the market can be better informed. We will work with the SEHK on reflecting such requirements for the issuer under the Listing Rules or appropriate guidance letters to the extent allowed under the applicable laws and regulations.

Underwriting fees

Public comments

120. Respondents generally supported disclosing in the prospectus the total fees to be paid to all syndicate CMIs participating in the international placing tranche. One respondent suggested that this information should be disclosed in an announcement, rather than the prospectus, as total fees may not be fixed and available at the time the prospectus is published.

121. However, most respondents opposed requiring the disclosure of the total monetary benefits paid to each syndicate CMI after listing. A number of respondents were of the view that fees are determined by commercial agreements negotiated with the issuers and publishing the breakdown between CMIs could negatively affect the interests of CMIs in future deals.

The SFC's responses

122. We note the respondents' concerns on the disclosure of total monetary benefits paid to each syndicate CMI.

123. Nonetheless, given that the OCs will be required to submit information on the total fees (ie, payable to all syndicate CMIs covering the international placing tranche as well as the Hong Kong public offer tranche) and fee split ratio to the SFC four clear business days before the Listing Committee Hearing, the issuer must have already decided on the total fees payable.

124. As such, we take the view that the prospectus should disclose total fees payable to all syndicate CMIs covering both tranches to facilitate investors in making an informed decision. If an overseas firm is also appointed by the issuer to conduct underwriting, bookbuilding or placing of shares in an IPO, the prospectus should disclose the fees payable to the overseas firm covering both tranches as well.

Section IV – Proposed requirements for the "Sponsor Coupling" proposal

Question:

22. Do you agree with the "sponsor coupling" proposal? If not, please explain.

Public comments

125. The majority of respondents supported the "sponsor coupling" proposal. They believed that it will help ensure offerings are transparent, which is in the best interest of investors, and alleviate concerns that sponsors which are not appointed as OCs at an early stage may compromise their due diligence to get the mandate. One respondent commented that sponsors should work closely with the listing applicants and provide guidance on the share offering. Another considered that an issuer is best served with a Sponsor OC. A few respondents noted that in practice it is very rare for sponsors (or their group companies) not to also engage in bookbuilding.

126. Amongst those which disagreed, some argued that the proposal might give too much bargaining power to the Sponsor OCs without appropriate checks and balances as the Sponsor OC cannot be easily replaced. They argued that this proposal institutionalises

the conflicts between the interests of the issuer and the selling group's interest in satisfying their investor clients.

127. A few respondents were concerned that small boutique sponsors without underwriting or distribution capacity might be driven out of the market as issuers generally do not wish to appoint multiple sponsors, especially in the case of GEM IPOs. Many small but highly professional sponsors may no longer be able to act as sponsors.

128. Two respondents disagreed with the proposal because the appointment of sponsors and OCs should be subject to separate considerations based on the quality and standard of work. The skill required to act as sponsor is completely different from that required for underwriting or distribution.

The SFC's responses

129. We welcome the strong support for this proposal. However, we do not agree that it might give too much bargaining power to Sponsor OCs. As explained in paragraph 140(e) of the Consultation Paper, fees are currently not aligned with sponsor costs and responsibilities, putting sponsors under undue pressure to compromise their due diligence to secure their appointment as an OC. Hence, it appears that the sponsors presently have too little bargaining power. The "sponsor coupling" requirement is aimed at redressing that and ensuring quality sponsor work.

130. Furthermore, given that sponsor coupling is already prevalent for IPO transactions on the Main Board[7], there is no basis to believe that mandating it should exacerbate conflicts of interest.

131. The impact on small boutique sponsors should be limited. As stated in footnote 32 of the Consultation Paper, in the year ended 30 September 2020, 72% of the 127 sponsors were engaged as a syndicate member indicating that they already have the necessary capabilities.

132. On the other hand, we acknowledge that "sponsor coupling" is not as prevalent in GEM IPOs[8], where small boutique sponsors with limited underwriting or distribution capability tend to be more active. Unlike the Main Board, where joint sponsors are more common[9], few GEM IPOs have joint sponsors. Furthermore, sponsors potentially compromising their standard of due diligence should also be less of a concern in GEM IPOs where sponsors are generally paid fees commensurate with their work.

133. For the reasons stated in paragraphs 130 and 132, we would apply the "sponsor coupling" requirement only to IPOs on the Main Board. The above changes are reflected in revised paragraph 21.4.1 of the Code.

Question:

23. Do you think one Sponsor OC is adequate or should more OCs be required to act as

[7] The sponsor or its group company was appointed as head of syndicate for 105 out of 130 (81%) new listings on the Main Board in 2018 and 120 out of 136 (88%) new listings in 2020.

[8] The sponsor or its group company was appointed as head of syndicate for 43 out of 75 (57%) new listings on GEM in 2018 and 5 out of 8 (63%) in 2020.

[9] 43 out of 130 (33%) new listings on the Main Board had joint sponsors in 2018 and 50 out of 136 (37%) had joint sponsors in 2020.

sponsors? For example, should the majority of OCs be required to act as sponsors (ie, if the issuer appoints three OCs, two must also act as sponsor)? Please explain.

Public comments

134. Responses were mixed as respondents' expectations varied. While many suggested having one Sponsor OC, a few respondents suggested that the optimal policy would be for all sponsors to be appointed as OCs (unless they are small boutique sponsors without underwriting or distribution capacity) to ensure that they would be treated equally by the issuer and free of any pressure to compromise their due diligence.

135. On the other hand, a few respondents suggested that all OCs must be sponsors.

The SFC's responses

136. In view of the very diverse market feedback, we regard that the Proposed Requirements of having at least one Sponsor OC appointed for each IPO (on the Main Board only) strikes an appropriate balance.

Section V – Implementation timeline

Question:

24. Do you have any comments on the proposed implementation timeline?

Public comments

137. Some respondents considered six months to be sufficient, whereas many more suggested extending the transition period to nine months or longer so that CMIs have more time to revise their systems, policies and procedures.

The SFC's responses

138. Having considered the above comments, the Code will take effect nine months after gazettal so as to give reasonable time for CMIs to implement the necessary operational and system changes to comply with the new requirements.

Conclusions and the way forward

139. The final version of the Code and GEM Placing Guideline are set out in Appendix B and Appendix C respectively. The SFC will proceed with the gazettal of the Code and the GEM Placing Guideline.

140. The SFC would like to thank all respondents for their time and effort in reviewing the proposals and for their detailed and thoughtful comments.

141. A number of respondents requested that the SFC clarify the Code requirements and provide guidance on the means of implementation. We will closely monitor the implementation of the new requirements and issue additional guidance as necessary.

Appendix A – List of respondents

(in alphabetical order)

1. Anglo Chinese Securities, Limited
2. Asset Management Group of Asia Securities Industry & Financial Markets Association
3. Blackrock, Inc.
4. BookBuild.Online Limited
5. British Chamber of Commerce in Hong Kong
6. Central China International Capital Limited
7. Charltons on behalf of Altus Capital Limited, Anglo Chinese Corporate Finance Limited, Asian Capital Limited and Frontpage Capital Limited
8. China International Capital Corporation Hong Kong Securities Limited
9. China Tonghai Securities Limited and China Tonghai Capital Limited
10. Everbright Sun Hung Kai Company Limited
11. FIL Investment Management (Hong Kong) Limited
12. Hong Kong Institute of Certified Public Accountants
13. Hong Kong Investment Funds Association
14. Hong Kong Professionals and Senior Executives Association
15. Hong Kong Securities and Futures Professionals Association
16. Hong Kong Securities Association
17. International Capital Market Association
18. Risk Management and Compliance Committee of the Chinese Securities Association of Hong Kong
19. The Equity Capital Markets Committee and the Asset Management Group of the Asia Securities Industry & Financial Markets Association
20. The Institute of Securities Dealers
21. The Law Society of Hong Kong
22. Submissions of nine respondents are published on a “no-name” basis upon request
23. Submissions of 11 respondents are withheld from publication upon request

Appendix B – Final form of the Paragraphs 17.1A and 21 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission

Paragraph 17.1A of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission

Paragraph 17 – Sponsors

17.1A Appointment

Before accepting an appointment by a listing applicant as a sponsor in relation to a listing application on the Main Board of the Stock Exchange, a sponsor should either:

(a) be independent[1] of the listing applicant and ensure that it or one of the companies within its group of companies[2] is appointed at the same time as an overall coordinator ("OC") (as defined under paragraph 21.2.3 of the Code) in connection with that listing application; or

(b) obtain written confirmation from the listing applicant that at least one sponsor, which is independent of the listing applicant, or one of the companies within the group of companies of that sponsor, has been appointed as an OC in connection with that listing application.

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1 The circumstances under which a sponsor is considered not to be independent of the listing applicant are set out under the Listing Rules.

2 For the purposes of this paragraph, "group of companies" has the same meaning as in section 1 of Part 1 of Schedule 1 to the SFO.

Paragraph 21 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission

Bookbuilding and placing activities in equity capital market and debt capital market transactions

21.1 Introduction

21.1.1 Paragraph 21 applies to a licensed or registered person that engages in providing services to issuers, investors or both in respect of an offering of shares or debt securities and involves the following activities conducted in Hong Kong:

(a) collating investors' orders (including indications of interest) in an offering in order to facilitate:

(i) the price determination and the allocation of shares or debt securities to investors; or

(ii) the process of assessing demand and making allocations

("bookbuilding activities");

(b) marketing or distributing shares or debt securities to investors pursuant to those bookbuilding activities ("placing activities"); or

(c) advising, guiding and assisting the issuer client[1] in those bookbuilding and placing activities.

A licensed or registered person engaged in any of the above-mentioned capital market activities is referred to as a "capital market intermediary" ("CMI").

21.1.2 Paragraph 21 covers only the following types of offerings that involve bookbuilding activities:

(a) an offering of shares[2] listed[3] or to be listed[4] on The Stock Exchange of Hong Kong Limited ("SEHK") ("share offering"); or

(b) an offering of debt securities listed or unlisted, and offered in Hong Kong or otherwise ("debt offering").

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1 In the case of an initial public offering of shares (including a public offer conducted in connection with a secondary listing in Hong Kong) ("IPO"), "issuer client" includes "listing applicant".

2 References to "shares" in paragraph 21 also include depositary receipts and units or interests in SFC-authorised real estate investment trusts ("REITs") listed or to be listed in Hong Kong.

3 This only covers the placing of listed shares to third-party investors by an existing shareholder if it is accompanied by a top-up subscription by the existing shareholder for new shares in the issuer.

4 This covers (i) IPOs, which include share offerings in connection with a secondary listing and offer of existing shares by way of IPO; (ii) offerings of a class new to listing; and (iii) offerings of new shares of a class already listed under a general or special mandate.

21.1.3 Paragraph 21 sets out the standards of conduct expected of a CMI in a share or debt offering. CMIs are also reminded to fulfil their obligations under applicable laws, rules and regulations, including properly addressing actual and potential conflicts of interest, ensuring the fair treatment of both their issuer client and investor clients, and upholding the integrity of the market at all times. In the case of a share offering, these include the Listing Rules[5] and other regulatory requirements or guidance issued by SEHK from time to time ("SEHK Requirements"). In the case of a debt offering where the debt securities are listed on SEHK, CMIs are also reminded to ensure compliance with the applicable rules and regulations issued by SEHK.

21.1.4 There are many types of share and debt offerings, which vary in nature and complexity, and a CMI may play different roles in different offerings. It is the responsibility of the senior management of a CMI to establish and implement adequate and effective policies, procedures and controls to ensure compliance with the rules and regulations which are applicable to the roles they play in an offering.

21.2 Types of CMIs

21.2.1 A CMI which is engaged by the issuer of a share or debt offering is referred to as a syndicate CMI.

21.2.2 A CMI which is not engaged by the issuer[6] of a share or debt offering is referred to as a non-syndicate CMI.

21.2.3 In the case of a share offering, an "Overall Coordinator" ("OC") of the offering is a syndicate CMI which, solely or jointly, conducts any of the following activities:

(a) overall management of the offering, coordinating the bookbuilding or placing activities conducted by other CMIs, exercising control over bookbuilding activities and making allocation recommendations to the issuer client;

(b) advising the issuer client of the offer price and being a party to the price determination agreement with the issuer client; or

(c) exercising the discretion to reallocate shares between the placing tranche and public subscription tranche, reduce the number of offer shares, or exercise an upsize option or over-allotment option.

21.2.4 In the case of a debt offering, an OC of the offering is a syndicate CMI which, solely or jointly, conducts the overall management of the offering, coordinates the bookbuilding or placing activities conducted by other CMIs, exercises control over bookbuilding activities and makes pricing or allocation recommendations to the issuer client.

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5 The Rules Governing the Listing of Securities on SEHK and Rules Governing the Listing of Securities on GEM of SEHK.

6 Given that a non-syndicate CMI is not engaged by the issuer, the issuer is not its client and hence not an "issuer client". The above notwithstanding, references to "issuer client" in this paragraph include references to "issuer" in the case of a non-syndicate CMI.

21.2.5 For the avoidance of doubt, irrespective of whether or not a CMI has been formally appointed by, or has entered into a written agreement with, the issuer client, a CMI which conducts any of the activities in paragraphs 21.2.3 or 21.2.4 will be an OC and is required to comply with this paragraph.

21.3 CMI - Obligations and expected standards of conduct[7]

A CMI should uphold market integrity and ensure compliance with all applicable legal and regulatory requirements.

21.3.1 Assessment of issuer client and offering

A CMI should conduct an adequate assessment of an issuer client before engaging in a share or debt offering for that issuer client. This includes:

(a) taking reasonable steps to obtain an accurate understanding of the history and background, business and performance, financial condition and prospects, operations and structure of the issuer client, except for a repeated issuer of debt offerings where a CMI acted as the CMI for previous offerings made by the same issuer. In this case, the CMI should ascertain whether there have been any material changes in the circumstances of the issuer client of relevance to its role as CMI; and

(b) establishing a formal governance process to review and assess the share or debt offering, including any actual or potential conflicts of interest between the CMI and the issuer client as well as the associated risks.

21.3.2 Appointment of CMI

Subject to paragraph 21.4.1 of the Code, before a CMI conducts any bookbuilding or placing activities, it should ensure that it has been formally appointed under a written agreement to conduct such activities by an issuer client in the case of a syndicate CMI or another CMI in the case of a non-syndicate CMI. The written agreement should clearly specify the roles and responsibilities of a CMI, the fee arrangements (including fixed fees as a percentage of the total fees to be paid to all syndicate CMIs participating in the offering[8]) and the fee payment schedule.

21.3.3 Assessment of investor clients

(a) A CMI should take reasonable steps to assess whether its investor clients, based on their profiles, fall within the types of investors targeted in a marketing and investor targeting strategy ("targeted investors") as referred to under paragraph 21.4.3.

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7 For the purpose of this paragraph, a non-syndicate CMI which is not appointed by a syndicate CMI (hence does not receive remuneration directly or indirectly from the issuer client) and is only responsible for relaying investor clients' orders to CMI for placing into the order book is only required to comply with paragraphs 21.3.3, 21.3.5 and 21.3.7.

8 This includes fees for providing advice to the issuer, marketing, bookbuilding, making pricing and allocation recommendations and placing these securities with investor clients. This is also commonly referred to as "underwriting fees" by the industry.

(b) In the case of a share offering, a CMI should take all reasonable steps to identify investor clients to whom the allocation of shares will be subject to restrictions or require prior consent from SEHK under the SEHK Requirements ("Restricted Investors") and inform the OC (whether directly or indirectly) before placing an order on behalf of such clients.

(c) In the case of a debt offering, a CMI should take all reasonable steps to identify whether its investor clients may have any associations[9] with the issuer client, the CMI or a company in the same group of companies[10] as the CMI ("group company") and provide sufficient information to an OC to enable it to assess whether orders placed by these investor clients may negatively impact the price discovery process.

21.3.4 Marketing

(a) A CMI should only market the shares or debt securities to its investor clients which are targeted investors. In the case of a share offering, where the shares are only marketed to selected investor clients, the CMI should be satisfied that the shares have been marketed to a sufficient number of clients and the likelihood of undue concentration of holdings is reasonably low.

(b) A CMI should allow all of its investor clients which are targeted investors and have indicated an interest in an offering to participate in that offering.

21.3.5 Order book

(a) A CMI should take reasonable steps to ensure that all orders (including indications of interest) placed in an order book represent bona fide demand of its investor clients, itself and its group companies. A CMI should also make enquiries with its investor clients about orders which appear unusual, for example, an order which is not commensurate with the investor client's financial profile, before placing the order.

(b) A CMI should ensure transparency in the bookbuilding process. It should disclose (whether directly or indirectly) the identities of all investor clients in an order book, except for orders placed on an omnibus basis. For orders placed on an omnibus basis, a CMI should provide, whether directly or indirectly, information about the underlying investor clients (ie, the investor client's name and unique identification number) to the OC and the issuer when placing the orders.

(c) A CMI (including the OC) which receives information about the investor clients for orders placed on an omnibus basis as mentioned under sub-paragraph (b)

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9 Investor clients who are the directors, employees or major shareholders of the issuer client, the CMIs or their group companies would be considered as having an association with the issuer client, the CMIs or their group companies.

10 For the purposes of this paragraph, "group of companies" has the same meaning as in section 1 of Part 1 of Schedule 1 to the SFO.

should only use this information for placing orders in that specific share or debt offering transaction.

21.3.6 Allocation

A CMI should establish and implement an allocation policy to ensure a fair allocation of shares or debt securities to its investor clients. This policy should:

(a) address or take into account the principles and requirements under paragraph 21.3.10 and the following factors:

(i) the marketing and investor targeting strategy;

(ii) the order size and circumstances of the investor client;

(iii) the price limits for the investor client's orders;

(iv) any minimum allocation amounts indicated by investor clients;

(v) any applicable legal and regulatory requirements; and

(b) prevent any practices which may result in the unfair treatment of investor clients or knowingly distort the demand for other share or debt offerings.

21.3.7 Rebates and preferential treatment offered

(a) A CMI should not offer any rebates to an investor client or pass on any rebates provided by the issuer client to an investor client. In addition:

(i) in the case of an IPO, a CMI should not enable any of its investor clients to pay, for each of the shares allocated, less than the total consideration as disclosed in the listing documents; and

(ii) in the case of a debt offering, a CMI should not enter into any arrangements which may result in investor clients paying different prices for the debt securities allocated.

(b) A CMI should disclose (whether directly or indirectly) to the issuer client, OC, all of its targeted investors and the non-syndicate CMIs it appoints:

(i) any rebates offered (such as those offered by the issuer client of a debt offering) to CMIs. The disclosure should specify, for example:

- the targeted recipients of the rebates;

- the terms and conditions under which the targeted recipients may receive the rebates; and

- the timing for the payment of the rebates; and

(ii) any other preferential treatment of any CMIs or targeted investors (such as guaranteed allocations).

In the case of a share offering, a CMI should make the above disclosure upon becoming aware of any such rebates or preferential treatment. In the case of a debt offering, the disclosure should be made no later than the time of the dissemination of the deal "launch message" to targeted investors.

21.3.8 Disclosure of information to OC, non-syndicate CMIs and targeted investors

A CMI should disclose complete and accurate information in a timely manner on the status of the order book and other relevant information it received to:

(a) the OC (whether directly or indirectly) and non-syndicate CMIs it appoints for them to carry out their duties; and

(b) its targeted investors for them to make an informed decision[11].

21.3.9 Record keeping

A CMI should maintain books and records which are sufficient to demonstrate its compliance with all applicable requirements in this paragraph. In particular, a CMI should document:

(a) assessments of the issuer client, share or debt offering and investor clients;

(b) audit trails from the receipt of orders (i.e. including indications of interest), the placing of orders in the order book (whether directly or indirectly) through to the final order allocation (including changes in the orders received, details of the rejected orders and the reasons thereof, order confirmations with each investor client or CMI prior to the final allocation decisions and records of the allocation decisions made with a special focus on large or unusual allocations);

(c) all key communications with, and information provided to, the OC, other CMIs or investor clients, including information about the status of the order book (such as the launch term sheet and book messages);

(d) where a CMI's order is placed on an omnibus basis, the intended basis of allocation for all orders with justifications as well as any material deviations from its allocation policy as referred to in paragraph 21.3.6;

(e) all key communications with the issuer client, such as disclosures made to the issuer client in relation to actual or potential conflicts of interest;

(f) rebates offered by the issuer client and the payment details;

[11] Where a CMI is a non-syndicate CMI (such as a sub-placing agent), it should disclose information received from syndicate CMIs or non-syndicate CMIs (such as a distributor).

(g) any other preferential treatment offered to itself, non-syndicate CMIs it appoints or its investor clients; and

(h) information forming the basis of all submissions made to SEHK and the SFC.

Except for records mentioned in sub-paragraph (b), which should be kept for a period of not less than two years, a CMI should maintain the above records for a period of not less than seven years.

21.3.10 Conflicts of interest

(a) A CMI should establish, implement and maintain policies and procedures to:

(i) identify, manage and disclose actual and potential conflicts of interest which may, for example, arise when a CMI:

- serves both the interests of its issuer client and investor clients;

- serves the interests of its investor clients when having a proprietary interest (including a proprietary interest of its group companies) in an offering; or

- has full discretion over allocations to investor clients or a proprietary order; and

(ii) govern the process for generating proprietary orders as well as making allocations to such orders.

(b) A CMI should:

(i) always give priority to satisfying investor clients' orders over its own proprietary orders[12] and those of its group companies;

(ii) only be the price taker in relation to its proprietary orders and those of its group companies and ensure that these orders would not negatively impact the price discovery process; and

(iii) segregate and clearly identify its own proprietary orders and those of its group companies (whether directly or indirectly) in the order book and book messages.

Note: For the purposes of this paragraph, proprietary orders of a group company exclude orders placed by the group company on behalf of its investor clients or funds and portfolios under its management, but include orders placed on behalf of funds and portfolios in which a CMI or its group company has a substantial interest.

[12] For share offering, proprietary orders are subject to the SEHK Requirements.

(c) In relation to a debt offering, a CMI should take reasonable steps to disclose (whether directly or indirectly) to the issuer client how any risk management transactions it intends to carry out for itself, the issuer client or its investor clients will not affect the pricing of the debt securities.

21.3.11 Resources, systems and controls

A CMI should maintain sufficient resources and effective systems and controls to ensure that it can discharge its obligations and responsibilities.

Chinese walls

(a) Where a CMI is a company or is part of a group of companies undertaking multiple activities in relation to an offering, for example, it or its group company is involved in the preparation and issuance of research reports, sponsor work, bookbuilding activities, placing activities and other related business activities, the CMI should take adequate measures to prevent the flow of information which may be confidential or price sensitive between staff performing different activities and to prevent and manage any conflicts of interest which may arise. In particular, the CMI should establish and maintain:

(i) an effective system of functional barriers (Chinese walls) which should include having physical separation between, and different staff employed for, the various business activities; and

(ii) appropriate policies and procedures which cover:

- the procedures (including approval procedures) for bringing staff over the wall;
- the standards of conduct expected of staff brought over the wall; and
- the records to be kept on wall-crossing activities.

Review and approval of orders and allocations

(b) The placing of orders for, or the allocation of shares or debt securities to, any of the following types of accounts by a CMI should be subject to appropriate risk assessments (taking into consideration, for instance, a CMI's financial capability and exposure to associated risks) and management review and approval:

(i) proprietary orders for the CMI and any of its group companies;

(ii) orders from its investor clients which may appear unusual, for example, orders which might appear to be related to the issuer client; and

(iii) in the case of a share offering, allocations which are subject to restrictions or require the prior consent of SEHK under the SEHK Requirements.

Appointment of non-syndicate CMIs

(c) Where a CMI appoints a non-syndicate CMI to assist it in distributing shares or debt securities, it should exercise due skill, care and diligence in the selection and appointment.

Surveillance and monitoring

(d) A CMI should conduct independent surveillance and monitoring on a regular basis to detect irregularities, conflicts of interest, leakage of price sensitive or confidential information about the issuer client and the offering, and potential non-compliance with applicable regulatory requirements or its own policies and procedures. For example, a CMI should:

(i) review the book messages it prepares and disseminates to ensure that there are no misleading messages;

(ii) perform surveillance of electronic communications; and

(iii) select debt or share offerings for post-deal reviews to ensure that the pricing or allocation is adequately justified.

This should be supplemented by an effective incident management and reporting mechanism to ensure that any issues identified are reported to independent control functions for follow-up action and escalated to senior management as appropriate.

21.3.12 Communication with the SFC and SEHK

A CMI should deal with the SFC and SEHK in an open and cooperative manner and promptly provide all relevant information and explanations in accordance with applicable legal or regulatory requirements or upon request.

21.4 OC - Obligations and expected standards of conduct

In addition to the requirements specified in paragraph 21.3, an OC should comply with the following requirements.

21.4.1 Terms of appointment

(a) Before an OC conducts any activities specified in paragraph 21.2.3 for a share offering or participates in any bookbuilding or placing activities for a debt offering, it should ensure that:

(i) it has been formally appointed by the issuer under a written agreement to conduct such activities; and

(ii) the written agreement should clearly specify its roles and responsibilities, fee arrangements (including fixed fees as a percentage of the total fees to be paid to all syndicate CMIs participating in the offering) and the fee payment schedule.

(b) In the case of an IPO on the Main Board of SEHK, an OC should, before accepting an appointment, either:

(i) ensure that it (or one of its group companies) is also appointed as a sponsor[13], which is independent[14] of the issuer client, and that both appointments are made at the same time and at least two months before the submission of the listing application to SEHK by or on behalf of the issuer client; or

(ii) obtain a written confirmation from the issuer client that for that IPO at least one sponsor, which is independent of the issuer client, or a group company of that sponsor, has been appointed as an OC, in which case its appointment as an OC should be made no later than two weeks after the submission of the listing application to SEHK by or on behalf of the issuer client.

(c) In the case of an IPO on GEM of SEHK, an OC should ensure that it is appointed as an OC no later than two weeks after the submission of the listing application to SEHK by or on behalf of the issuer client.

21.4.2 Advice to issuer client

(a) An OC should act with due skill, care and diligence when providing advice, recommendations and guidance to the issuer client. In particular, an OC should:

(i) ensure that its advice and recommendations are balanced and based on thorough analysis and are compliant with all applicable legal and regulatory requirements;

(ii) engage the issuer client at various stages during the offering process to understand the issuer client's preferences and objectives with respect to pricing and the desired shareholder or investor base so that the OC is in a position to advise, develop or revise a marketing and investor targeting strategy with a view to achieving these objectives given prevailing market conditions and sentiment;

(iii) explain the basis of its advice and recommendations to the issuer client, including any advantages and disadvantages. For example, it should communicate its allocation policy to the issuer client to ensure that the issuer client understands the factors underlying the allocation recommendations;

(iv) advise the issuer client in a timely manner, throughout the period of engagement, of key factors for consideration and how these could

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[13] Reference to "sponsor" in this paragraph 21 shall include the listing agent in the context of a REIT seeking the SFC's authorisation.

[14] The circumstances under which a sponsor is considered not to be independent of the issuer client are set out under the Listing Rules.

influence the pricing outcome, allocation and future shareholder or investor base; and

(v) advise the issuer client on the information that should be provided to syndicate CMIs to enable them to meet their obligations and responsibilities under the Code of Conduct. This includes information about the issuer client to facilitate a reasonable assessment of the issuer client required under paragraph 21.3.1.

(b) An OC which participates in a share offering should

(i) provide guidance to the issuer client on the market's practice on the ratio of fixed and discretionary fees[15] to be paid to syndicate CMIs participating in an IPO; and

(ii) advise and guide the issuer client and its directors as to their responsibilities under the SEHK Requirements which apply to placing activities and take reasonable steps to ensure that they understand and meet these responsibilities.

(c) Where the issuer client decides not to adopt an OC's advice or recommendations in relation to pricing or allocation of shares or debt securities or, in the case of a share offering, its decisions may lead to a lack of open market, an inadequate spread of investors or may negatively affect the orderly and fair trading of such shares in the secondary market, the OC should explain the potential concerns and advise the issuer clients against making these decisions.

21.4.3 Marketing, rebates and preferential treatment offered

(a) An OC should, in consultation with the issuer client, devise a marketing and investor targeting strategy for order generation, taking into account the objectives and preferences of the issuer client. This may include specifying the types of investors targeted[16] and the portion of an offering to be allocated to each type of investors to establish the desired shareholder or investor base. In the case of an IPO, the strategy should include which types of investors who may be appropriate to be cornerstone investors and aim to achieve an open market and an adequate spread of investors and promote the orderly and fair trading of the shares in the secondary market in accordance with the SEHK Requirements.

(b) An OC should keep in view prevailing market conditions and sentiment and advise the issuer client to adjust the strategy as appropriate.

(c) An OC should advise the issuer of the disclosure of any rebates and preferential treatment.

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[15] Discretionary fees refer to the portion of the total fees to be paid to all syndicate CMIs at the absolute discretion of the issuer client.

[16] These include institutional clients, sovereign wealth funds, pension funds, hedge funds, family offices, high net worth individuals and retail investors.

21.4.4 Bookbuilding

An OC should take all reasonable steps to ensure that the price discovery process is credible and transparent, the order book has been properly managed and the allocation recommendations made to the issuer client as well as the final allocation have a proper basis. An OC should use its best endeavours, when advising the issuer client or when making pricing and allocation decisions as delegated by the issuer client, to strike a balance between the interests of the issuer client and investor clients and to act in the best interests of the integrity of the market.

(a) Order generation and consolidation of an order book

An OC should take reasonable steps to properly manage an order book and ensure the transparency of the order book.

(i) In particular, an OC should:

- ensure that the identities of all investor clients are disclosed in the order book, except for orders placed on an omnibus basis;

- properly consolidate orders in the order book by taking reasonable steps to identify and eliminate duplicated orders, inconsistencies or errors;

- segregate and clearly identify in the order book and book messages any proprietary orders of CMIs and their group companies; and

- make enquiries with CMIs which have placed orders on behalf of their investor clients, themselves or their group companies which appear unusual or irregular, for example, orders which appear to be related to the issuer client.

(b) Pricing

An OC should:

(i) advise the issuer client on the pricing with reference to, for instance, the results of the bookbuilding activities, the characteristics of the issuer client, prevailing market conditions and sentiment and the requirements of the relevant authorities;

(ii) advise the issuer client against providing any arrangements whereby:

- in the case of an IPO, the investor clients would pay, for each of the shares allocated, less than the total consideration as specified in the listing documents; and

- in the case of a debt offering, the investor clients would pay different prices for the debt securities allocated.

(iii) ensure that the proprietary orders of CMIs or their group companies and, for debt offering, the orders placed by investor clients which have associations with the issuer client, CMIs or their group companies, will not negatively impact the price discovery process.

(c) Allocation

(i) An OC should develop and maintain an allocation policy which sets out the criteria for making allocation recommendations to the issuer client. The allocation policy should address or take into account the following factors:

- the issuer client's objectives, preferences and recommendations;
- the prevailing market conditions and sentiment;
- the types and characteristics as well as the circumstances of targeted investors;
- the spread of investors (for example, the sizes and number of large holdings); and
- the overall subscription rate for the offer.

(ii) An OC should make allocation recommendations in accordance with an allocation policy as referred to in subparagraph (i) above. In addition:

- recommendations regarding the allocation of shares or debt securities to the investor clients of the OC should take into account the policy specified in paragraph 21.3.6; and
- in the case of an IPO, allocation recommendations should also ensure that allocations to Restricted Investors comply with the SEHK Requirements and be made with a view to achieving an open market, an adequate spread of shareholders and the orderly and fair trading of the shares in the secondary market.

Should the allocation recommendations materially deviate from the allocation policy or the policy specified in paragraph 21.3.6, the OC should explain to the issuer client the reasons for the deviation.

21.4.5 Assessment of investors

(a) In the case of an IPO, an OC should:

(i) advise the issuer client to provide to all syndicate CMIs a list of its directors, existing shareholders, their close associates and nominees engaged by any of the above for the subscription or purchase of shares offered in the IPO; and

(ii) take all reasonable steps to identify investors which are on the list mentioned under sub-paragraph (i) and ensure that they will only be allocated shares in accordance with applicable SEHK Requirements.

(b) In the case of a debt offering, an OC should

(i) advise the issuer client to provide sufficient information to all syndicate CMIs to enable them to reasonably identify whether investor clients have any associations with the issuer client; and

(ii) take all reasonable steps to identify whether investor clients have any associations with the issuer client, CMIs or their group companies.

21.4.6 Disclosures to syndicate CMIs and targeted investors

An OC should:

(a) inform other syndicate CMIs of the issuer client's marketing and investor targeting strategy; and

(b) disseminate material information related to the offering (for example, information which may affect the prices, orders received per investor type, proprietary orders of CMIs and their group companies, and known preferential treatments and rebates) as included in, for example, the launch term sheet and book messages, in a timely manner to all syndicate CMIs and ensure that such information is complete, accurate and has a proper basis.

21.4.7 Record keeping

An OC should document:

(a) all changes in the order book throughout the bookbuilding process;

(b) all key discussions with the issuer client on, for instance, the ratio of fixed and discretionary fees to be paid to all syndicate CMIs participating in the IPO, marketing and investor targeting strategy, pricing, allocation policy and disclosures of any actual or potential conflicts of interest;

(c) key advice or recommendations provided to the issuer client (including the allocation rationale, advantages and disadvantages, and any material deviations from the allocation policy);

(d) the final decisions of the issuer client which deviate materially from the advice or recommendations provided by the OC, including the OC's explanation to the issuer client on any potential concerns associated with these decisions and the advice provided; and

(e) the rationale for any decisions delegated to it by the issuer client (such as pricing and allocation of shares).

An OC should maintain records of the above for a period of not less than seven years.

21.4.8 Communication with the SFC

(a) An OC should report and provide the following information to the SFC in a timely manner:

(i) any instances of material non-compliance with the SEHK Requirements related to, for example, the placing activities conducted by itself or the issuer client;

(ii) any material changes to the information it previously provided to the SFC and SEHK;

(iii) the reasons for ceasing to act as an OC in a share offering transaction;

(iv) other information as the SFC may require from time to time.

(b) In the case of an IPO, an OC[17] should provide the following information to the SFC by no later than four clear business days prior to the Listing Committee Hearing[18]:

(i) the name of each OC participating in the offering;

(ii) the allocation of the fixed portion of the fees paid by the issuer to each OC; and

(iii) the total fees (as a percentage of the gross amount of funds raised) of both the public offer and the international tranche to be paid to all syndicate CMIs participating in the offering and the ratio between the fixed and discretionary portions of the total fees to be paid to all syndicate CMIs participating in the offering (in percentage terms).

If there are any material changes to any of the above, the OC should notify the SFC as soon as practicable.

Note: If more than one intermediary is appointed as an OC for an IPO, arrangements should be made for one of them to provide the information specified in this sub-paragraph to the SFC. Notwithstanding this, each OC is jointly and severally liable for ensuring that such information is accurate and complete and has been provided to the SFC within the timeframe stipulated above.

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[17] In the case of an IPO on the Main Board of the SEHK, this requirement is only applicable to an OC which is also appointed as a sponsor for that IPO as referred to in paragraph 21.4.1(b).

[18] Reference to "Listing Committee Hearing" shall refer to the expected date of the issue of the approval-in-principle letter by the SFC in the context of a REIT seeking the SFC's authorisation.

Appendix C – Final form of the Guideline to capital market intermediaries involved in placing activities for GEM stocks

SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

Guidelines to capital market intermediaries involved in placing activities for GEM stocks

August 2022

Introduction

1. These Guidelines are published by the Securities and Futures Commission (SFC) under section 399 of the Securities and Futures Ordinance (SFO) for the purposes of supplementing the existing conduct requirements relating to equity capital market placing activities.

2. These Guidelines were first issued[1] together with the Joint Statement regarding the price volatility of GEM stocks issued by the SFC and The Stock Exchange of Hong Kong Limited (Exchange) (Joint Statement) on 20 January 2017 and were revised following the introduction of paragraph 21 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of Conduct). These Guidelines should be read in conjunction with the Joint Statement and paragraph 21 of the Code of Conduct. If there are any conflicts between these Guidelines and paragraph 21 of the Code of Conduct, the more stringent requirements shall prevail. Unless otherwise stated, the terms used in these Guidelines are as defined in paragraph 21 of the Code of Conduct.

3. These Guidelines apply to capital market intermediaries (CMIs) engaged in placing activities conducted in Hong Kong in respect of GEM initial public offerings (IPOs).

4. Any failure by a CMI to comply with any applicable provisions of these Guidelines:

   (a) shall not by itself render a CMI liable to any judicial or other proceedings, but these Guidelines shall be admissible in evidence in any proceedings under the SFO before any court, and if any provisions set out in these Guidelines appear to the court to be relevant to any questions arising in the proceedings, they shall be taken into account in determining the questions; and

   (b) may cause the SFC to consider whether such failure adversely reflects on the CMI's fitness and properness and the need for regulatory action.

Guidance for overall coordinators (OCs)

5. OCs play an important role in the placing of GEM IPO shares. They should ensure the fair treatment of both the issuer client and investor clients and uphold the integrity of the market. Accordingly, they are expected to use their best efforts to assist their issuer clients in complying with the Rules Governing the Listing of Securities on GEM (GEM Listing Rules) (as supplemented by the Joint Statement) relevant to placing activities.

6. An OC is expected to use all reasonable efforts to advise the issuer client of the following in relation to placing activities:

   (a) The relevant regulatory requirements, including relevant GEM Listing Rules (as supplemented by the Joint Statement) and potential consequences[2] for non-compliance;

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[1] These Guidelines were formerly known as the Guideline to sponsors, underwriters and placing agents involved in the listing and placing of GEM stocks.

[2] Please see paragraphs 21 and 22 of the Joint Statement.

(b) The targeted investor type and placee mix (for example, the issuer client may indicate its preference for a percentage of shares to be allocated to long-term investors rather than short-term investors or to institutional investors rather than retail investors);

(c) The overall strategy and allocation basis with a view to achieving an open market and an adequate spread of shareholders, and to ensure that the percentage of shares in public hands meets the relevant requirements under the GEM Listing Rules (as supplemented by the Joint Statement). This will generally include selecting an appropriate number of syndicate CMIs, taking into account their investor client base, competence, resources, track record and allocation strategy; and

(d) The retention of proper documentation by the issuer client as required under the Joint Statement[3].

7. An OC is also expected to retain proper documentation to demonstrate that it has used all reasonable efforts to discharge all of its obligations.

Guidance for CMIs when placing shares to their investor clients

8. The following guidance is provided to assist CMIs (including syndicate CMIs and non-syndicate CMIs) to comply with relevant regulatory principles and requirements as well as to fulfil their responsibilities to the issuer client[4] (where applicable) when placing shares to their investor clients.
In particular:

(a) Placings should be conducted with sufficient senior management oversight by the CMI's senior management.

(b) CMIs should put in place appropriate policies and procedures to avoid any undue concentration of shareholdings and to maximise the likelihood of an open market and a fair and orderly trading of shares in the secondary market, which should include a marketing programme directed to a wide range of investor clients. For example:

(i) CMIs should notify[5] their investor clients[6] as part of their marketing programmes that they have been appointed as a CMI for a GEM IPO[7] and provide a brief description of the issuer client and a cautionary statement[8];

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3 Please see paragraph 18 of the Joint Statement.

4 Given that a non-syndicate CMI is not engaged by the issuer, the issuer is not its client and hence not an "issuer client". Notwithstanding this, references to "issuer client" in these Guidelines include references to "issuer" in the case of a non-syndicate CMI.

5 This notification should provide factual, fair and balanced information about the GEM IPO. It does not need to recommend that GEM IPO to investor clients.

6 A CMI is generally expected to notify all of its active investor clients of each GEM IPO to the extent that these clients fall within the targeted investor types specified in the marketing and investor targeting strategy (targeted investors). However, where a CMI opts to notify only selected investor clients when also meeting its suitability obligations (for details, please refer to footnote 7), based, for example, on investor clients' risk appetites and past investment preferences, this would be acceptable provided that senior management of the CMI is satisfied that a sufficient number of investor clients are offered the opportunity and the likelihood of undue concentration of shareholdings is reasonably low.

(ii) CMIs should allocate a reasonable number of account executives to each GEM IPO and allow all of its investor clients which are targeted investors and have indicated an interest in a GEM IPO to participate in it;

(iii) CMIs should endeavour to respond to enquiries from prospective investor clients[9] who are interested in participating in a GEM IPO and to open accounts for these investor clients in good time for them to participate in the GEM IPO; and

(iv) CMIs should not afford any preferential treatment[10] to investor clients unless this has already been properly disclosed in the listing document. Practices which may result in the unfair treatment of investor clients and potentially manipulate the demand for other share offerings are prohibited. This includes the following types of preferential treatment:

- offering rebates by CMIs to investor clients or passing on any rebates provided by the issuer to investor clients; and
- making any arrangements which would result in investor clients paying, for each of the shares allocated, less than the total consideration as disclosed in the listing document.

(c) "Know-your-client" procedures must be conducted properly. CMIs are required to take reasonable steps to establish the identity of an investor client and to confirm whether a person intending to subscribe is the beneficial owner of an investor client's account (i.e. not a nominee of some other person) and is independent of the issuer client, its controlling shareholders and directors. For the avoidance of doubt, CMIs should exercise caution when relying on an investor client's declaration of its independence and should make further enquiries (for example, by way of an internet search). CMIs are generally expected to pay special attention to the following "red flags":

(i) investor clients subscribing for the GEM IPO shares are procured or introduced by the issuer client, its controlling shareholders or directors;

(ii) investor clients subscribing for the GEM IPO shares have known business, financial or other relationships (e.g. as employees, suppliers or customers) with the issuer client or any of its controlling shareholders or directors;

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7 CMIs are also required to observe the suitability obligations under paragraph 5.2 of the Code of Conduct (as supplemented by the Circular to Intermediaries - Frequently Asked Questions on Triggering of Suitability Obligations dated 23 December 2016 and Circular to Intermediaries - Frequently Asked Questions on Compliance with Suitability Obligations dated 23 December 2016) when placing shares with their investor clients.

8 Please refer to the cautionary statement included in the Joint Statement as a reminder to the public about the higher investment risks and susceptibility to high market volatility of GEM stocks.

9 To the extent that these investor clients are targeted investors.

10 Preferential terms or treatment may include guaranteed allocation, unusually large allocation, put options or offers to repurchase placing shares after listing.

(iii) investor clients subscribing for the GEM IPO shares have familial relationships or share the same address with other placees; and

(iv) the accounts of investor clients subscribing for the GEM IPO shares are operated by the same person.

(d) The sources of funding for the subscription of GEM IPO shares should be established using a risk-based approach before any acceptance of an investor client's subscription. CMIs are expected to ensure that the subscriptions are commensurate with an investor client's financial position.

(e) Save for nominee companies[11], subscriptions should be rejected where there are any suspicions that an investor client may be a nominee of some other person whose identity the CMI is unable to ascertain or the acceptance of subscriptions would result in an inadequate spread of shareholders.

(f) Proper records must be kept so that CMIs can demonstrate their compliance with these Guidelines throughout the entire placing process. Sufficient details should be available, covering, for example: (i) all notifications to investor clients; (ii) all orders received; (iii) the rationale for the allocation of shares as well as the reasons for the rejection of orders; and (iv) the list of placees submitted to the Exchange.

[11] Rule 10.12(1A) of the GEM Listing Rules allows allocation to nominee companies with the written consent of the Exchange.

Appendix D – Requirements governing the appointment of syndicate CMIs, determination of their fee entitlements and related matters

Appointment of syndicate CMI (including OC) including determination of their fee entitlements

Under paragraph 21.3.2 of the Code, the syndicate CMI (including OC) should be appointed by the issuer under a written agreement before it conducts any bookbuilding or placing activities (which now includes marketing activity).

The written agreement should clearly specify, among other things, the fixed fees to be paid to that syndicate CMI.

Before the issuer could decide on the fixed fees to be paid to any syndicate CMI, the issuer would need to decide (i) its total fees; and (ii) the fee split ratio.

[Note: The issuer would only be guided by the OC on the market's practice on the fee split ratio under the revised Code.]

Appointment of OCs

Under paragraph 21.4.1(a) and (b) of the Code, the issuer should at least appoint one OC (that is also acting, or has a group company that acts, as an independent sponsor to the IPO) at least two months before A1 submission[1].

Under paragraph 21.4.1(a) of the Code, the issuer should appoint all OCs no later than two weeks after A1 submission.

There is no specific timeframe for appointing OCs in the case of a non-IPO transaction.

Appointment of non-OC syndicate CMIs

There are no specific timeframes for appointing non-OC syndicate CMIs in any transaction.

Reporting to the SFC

Under paragraph 21.4.8(b) of the Code, the OC should:

(a) provide the following information to the SFC[2] four clear business days prior to the Listing Committee Hearing:
   (i) the name of each OC participating in the IPO;
   (ii) the fixed fees to be paid to each OC; and
   (iii) the total fees and fee split ratio; and

(b) notify the SFC as soon as practicable if there are material changes to any of the above information that has been provided previously.

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1 This only applies to Main Board IPOs.

2 For Main Board IPOs, this is only applicable to an OC which is also appointed as a sponsor for that IPO.