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Securities and Futures Commission

Consultation Paper on the Draft Guidelines on Disclosure of Inside Information (March 2010)

Joint Submission of Clifford Chance and Linklaters

Executive Summary:

– This paper sets out the views of Clifford Chance and Linklaters on the Consultation Paper on the Draft Guidelines on Disclosure of Inside Information released by the Securities and Futures Commission ("**SFC**") in March 2010.

– Clifford Chance and Linklaters have also made a joint submission to the Financial Services and the Treasury Bureau ("**Bureau**") in response to its Consultation Paper on the Proposed Statutory Codification of Certain Requirements to Disclose Price Sensitive Information by Listed Corporations released in March 2010. The joint submission is appended to this Paper.

– Clifford Chance and Linklaters do not seek to challenge the Bureau's regulatory objective to codify certain requirements to disclose price sensitive information ("**PSI**") and note, in particular, that the sanctions behind the proposed statutory regime are restricted to civil sanctions. We also do not seek to challenge the primary proposal to adopt the definition of "relevant information" from the insider dealing regime under the Securities and Futures Ordinance ("**SFO**") to define PSI.

– However, we have comments on certain specific aspects of the proposals, including: the SFC's views on what constitutes information "generally known" to the market; the limited disclosure mechanism; the wide definition of "officers"; and the provision that deems the listed corporation to have knowledge of the PSI if its officers "ought reasonably to have" known the information.

– Our responses to the SFC consultation paper are set out below. In some places references have been made to proposals raised in the Bureau's consultation paper and our responses to them have also been included. This is because we believe that such responses may have an impact on the guidance that the SFC provides / may provide in its guidelines on disclosure of inside information.

1 The proposal to adopt the existing definition of "relevant information" from the insider dealing regime under the SFO to define PSI

1.1 We do not disagree with the adoption of the definition of "relevant information" from the insider dealing regime under the SFO to define PSI.

1.2 The Draft Guidelines on Disclosure of Inside Information ("**Draft Guidelines**") published by the SFC set out to summarise the key aspects of what has been viewed by the tribunals in Hong Kong as constituting "relevant information". We believe it would be helpful to include principles from the ***case relating to the listed securities of Tingyi (Cayman Islands) Holding Corp.***, which was omitted from the cases listed in the Draft Guidelines, including that:

- Information will be "specific" if it is capable of being "pointed to, identified and unequivocally expressed", which, in the case of financial information about a listed group means whether the information carried such particularity about aspects of the listed group's financial and economic functioning so as to allow those matters to be identified and coherently described and the information about them to be understood.
- Before information can qualify as being specific information about a company it must be real information. If it is misinformation it cannot be real information. To describe a company as prosperous and stable when it is in the throes of a financial crisis is to provide no information about that company at all. Small inaccuracies in information will not, however, render the information not real information: it is a matter of degree when it comes to financial information.
- In most cases only net profit figures ("bottom line results") are likely to be price-sensitive, and therefore raw financial data would not be price-sensitive unless it was possible to calculate net profit data from them.
- In most cases, an understanding of the market's knowledge of a company's affairs is obtainable only by considering what has been said or published in the media, or in other materials which are readily accessible by the market. An assessment must be made of the completeness of the information released into the market and the degree of penetration of the market.

2 The proposal that a listed corporation should be obliged to disclose to the public as soon as practicable any "inside information" that has come to its knowledge, and that it should be regarded to have knowledge of the inside information if a director or an officer has come into possession of that information in the course of the performance of his duties

2.1 "As soon as practicable"

- We agree with the general principle that a listed corporation should disclose PSI as soon as practicable. However, the Draft Guidelines suggest that "as soon as practicable" means "immediately"[1]. We do not think this is correct. We ask that the SFC provides further guidance on what actions a listed corporation could take to comply with the "as soon as practicable" requirement in circumstances where immediate disclosure is not practicable, for instance:
  - Upon the receipt of a whistle blower's report or discovery of a potential problem, the scale of which is completely unknown, on a matter that is potentially price sensitive, the listed corporation may need some time to verify whether the allegations have any substance or the potential scope of what may need to be investigated to get to the bottom of the issue, before deciding whether to disclose the matter (be it in a "holding announcement" or a "full announcement"), otherwise the market may be inundated with information that lacks integrity and that may even mislead investors.

[1] para. 32 of the Draft Guidelines

- There may be some time lag between the time when an officer comes into possession of a piece of inside information and the time when the decision makers in the listed corporation are made aware of the information. This is especially the case for larger size listed corporations. Please also see our submission below in relation to the definition of "officer".

- We ask that the regulators take a practical and reasonable approach in determining whether disclosure has been made "as soon as practicable".

2.2 "Officer"

- We agree with the principle that a listed corporation should be regarded to have knowledge of the inside information if certain of its officers have come into possession of that information in the course of the performance of their duties.

- However, many listed corporations in Hong Kong are very sizeable and may have thousands of managers. The proposed definition of "officer" is so wide that many staff who do not have the authority to influence the decision on PSI disclosure, or from whom there are a few levels of reporting before the information will reach the decision makers, are considered as "officers". To deem a listed corporation to have the knowledge that any of its officers (which can include junior managers) has would make the legislation very difficult and costly to comply with, and again may lead to "over-disclosure" if officers choose to "play it safe" and make disclosure indiscriminately.

- We note that the Chinese translation of "officer" in the proposed legislation refers to "senior officer" but the English definition does not contain the same qualification. We propose that for the purpose of the new Part IIIA of the SFO, the definition of "officer" be refined so that it will only include:

  - directors; and

  - senior officers who are expected to come into possession of PSI because of the nature of their role within the listed corporation. We suggest that such senior officers should be company secretaries, senior public relations managers, and senior legal counsel / senior compliance officers.

2.3 Corporations listed on Hong Kong and PRC exchanges

- Whilst the Draft Guidelines provide guidance on disclosure in cases where inside information is released to another market when the market in Hong Kong is closed (including the possibility of requesting a suspension in trading its securities pending the issue of the announcement in Hong Kong[2]), there is no similar guideline addressing the situation where the release of inside information in Hong Kong is on hold pending a synchronised release in another market.

- We understand that a corporation that is dual-listed on a PRC stock exchange and the Stock Exchange of Hong Kong ("**SEHK**") cannot post

[2] para. 65 and 66 of the Draft Guidelines

announcements directly on the websites of the PRC exchange, and as a result the timing of posting announcements in the PRC is beyond the corporation's control. We further understand that the periods for posting announcements on PRC exchange websites are more restrictive than those for posting announcements through HKEx-EPS. In order for a PRC / Hong Kong dual-listed corporation to ensure equal dissemination of information to its shareholders, there may be a delay in the disclosure in Hong Kong. We therefore ask that:

- the regulators take into account the need to wait for the PRC exchange(s) to post the announcement when determining whether a disclosure in Hong Kong has been made "as soon as practicable" ; and
- the SFC provides guidance on disclosure in a case where disclosure in Hong Kong needs to be delayed pending disclosure in the PRC (including the possibility of a trading suspension in the meantime).

2.4 "ought reasonably to have"

- The proposed legislation[3] provides that a listed corporation is deemed to have knowledge of the inside information if an officer of the corporation ought reasonably to have come into possession of the information in the course of performing functions as an officer of the corporation.
- Since a breach of the proposed disclosure obligation might not involve a clear deliberate act or behaviour, we are of the view that if:
  - as proposed, there is already a requirement to take all reasonable measures to ensure that proper safeguards exist to prevent the breach of a disclosure requirement[4];
  - the officers have indeed taken all reasonable measures to ensure compliance; and
  - the officers do not have actual knowledge of the inside information,

  then the listed corporation should not be liable for a failure to disclose. The requirement under the proposed s.101G(1) should provide enough protection to the public. To include an additional deeming provision on the basis of constructive knowledge would suggest that there is something else the officers should do on top of taking all reasonable measures to ensure compliance. Any such additional obligations may (i) create undue administrative burden on the listed corporations and their officers; and (ii) result in listed corporations making disclosure indiscriminately in order to "play it safe".

[3] s.101B(2) of the SFO

[4] s.101G(1) of the SFO

3 The proposal that the disclosure must be made in a manner that can provide for equal, timely and effective access by the public to the information disclosed

3.1 We agree with the principle that disclosure should be made in a manner that can provide for equal, timely and effective access by the public to the information disclosed. However, we see some practical difficulties in complying with the operative provisions (further discussed in 3.2 below). In addition, we are concerned that an overly strict approach in determining what constitutes information "generally known" to the market might unfairly restrict institutional investors from participating in capital raising activities (further discussed in 3.3 below).

3.2 HKEx-EPS

- The proposed disclosure mechanism appears to be overly restrictive. Under the current proposals, listed corporations can comply with the disclosure requirement by disseminating information via the Electronic Publication System adopted by the Hong Kong Exchanges and Clearing Limited ("**HKEx-EPS**"). While the draft legislation does not limit the manner of disclosure, the SFC has stated in its Draft Guidelines that the disclosure requirement is only likely to be satisfied by disseminating information via the HKEx-EPS. This will likely cause compliance difficulties for listed corporations, especially where a price sensitive event takes place outside of the operating hours of the HKEx-EPS.
- As such, we submit that:
  - (i) disclosure of information via other means should also be allowed, e.g., via widely subscribed news or wire services (such as Bloomberg and Reuters), and posting an announcement on the listed corporation's own website; or
  - (ii) if the Bureau is not prepared to accept other disclosure mechanisms, then the SEHK should at least enhance the HKEx-EPS to allow continuous disclosure.

3.3 "Generally known"

- To date, the institutional market has carried out capital raising activities (in particular, convertible bond offerings) on the basis that launch communication and news coverage published via widely subscribed news / wire services, such as Bloomberg or Reuters, are sufficient public disclosure of the relevant information to make it "generally known" among the institutional investor community.
- Accordingly, institutional investors who participate in capital raising activities have proceeded on the basis that they can borrow stock to hedge their exposure before the issuer's announcement on the SEHK.
- The Draft Guidelines, however, provide that widely circulated press reports cannot constitute sufficient public disclosure[5]. This suggests that the SFC

[5] para. 19 of the Draft Guidelines

considers disclosure via widely subscribed news / wire services not sufficiently public for the purposes of insider dealing prohibitions. If this is the case, any over-the-counter stock borrowing that happens before the issuer's announcement may risk contravening the insider dealing prohibition. In other words, the whole institutional market in the issuer's stock will effectively be restricted pending the formal announcement on the SEHK.

- Stock borrowing activity is critically important to certain capital raising activities. We urge that the SFC provides specific guidance as to its views on the application of the insider dealing prohibition to these stock borrowing activities. If the SFC is of the view, contrary to current market practice, that the launch communication of a deal is not sufficient public disclosure to make all relevant information "generally known" among the institutional investor community, and therefore that the stock borrowing activities by investors is inappropriate prior to the formal announcement by the issuers, it is likely to materially impact the willingness of institutional investors to participate in certain capital raising activities and, therefore, the continued viability of certain capital raising options for listed issuers.

- We understand that in some jurisdictions (e.g., the UK), disclosure via widely subscribed news information services is expressly permitted as a form of public disclosure, and in some other jurisdictions (e.g., Singapore and Australia) it is generally accepted that disclosure via widely subscribed news information services is sufficiently public among the institutional investor community, for the purposes of their respective insider dealing prohibitions.

4 The provision of the four proposed safe harbours

4.1 We welcome the provision of the four proposed safe harbours. However, we submit that certain of these safe harbours should be extended and additional safe harbours should be introduced – see our submission under paragraph 6 below.

5 The proposal that the SFC should be empowered to grant waivers, and to attach conditions thereto

5.1 We agree that the SFC should be empowered to grant waivers, and to attach conditions thereto.

5.2 We believe it would be helpful to the market if the SFC could publish on its website or otherwise in a manner that allows easy public access the details of the waivers granted and conditions imposed (or at least the more representative ones).

6 Additional safe harbours

6.1 We believe that certain of the proposed safe harbours should be extended and that additional safe harbours should be introduced. We discuss these below.

6.2 Safe Harbour B (incomplete negotiations or proposals)

- There are incomplete negotiations or proposals the outcome of which may not be prejudiced if the information is disclosed prematurely (and therefore the proposed Safe Harbour B would not be applicable), but the information so disclosed may be misleading due to the lack of integrity, certainty or details. The following are a couple of examples:
  - Management accounts: The Draft Guidelines[6] seem to suggest that once a listed corporation becomes aware that its financial results may not meet the market expectation, it should immediately disclose such information even if the final accounts are not yet available. We would like to ask the SFC to confirm whether this understanding is correct. If it is, we submit that listed issuers should not be required to make a disclosure if the information subject to disclosure may be misleading to the market. Information may be misleading if it is based on preliminary results which have not been verified or are pending expert reports;
  - Share placing: The Draft Guidelines[7] provide that the contemplation of a forthcoming share placing will need to be disclosed if the placing is likely to materially affect the price of the shares. Disclosure is required even if the details of the placing are not known. Since the details of a placing (such as the size, price and timing of it) can materially affect the price of the shares, the announcement of a contemplation of a share placing without details of the placing can be misleading.
- Accordingly, we propose that Safe Harbour B be amended as follows:

  "When the information is related to impending negotiations or incomplete proposals:

  (i) *the outcome of which may be prejudiced if the information is disclosed prematurely; or*

  (ii) *the information may be misleading to the persons who are accustomed or would be likely to deal in the listed securities of the corporation."*

6.3 Safe Harbour D (liquidity support)

- Safe Harbour D currently only applies when the Government Exchange Fund or a central bank provides liquidity support to the listed corporation.
- We ask the Bureau to consider extending this safe harbour to cover all types of liquidity support, financing proposal and rescue plan, whether provided by the Government Exchange Fund or a central bank or otherwise. This is because the same problems with immediate disclosure arise regardless of the type of support, and who provides the support. Immediate disclosure of the receipt of liquidity support or other types of assistance by a listed corporation could lead to a loss of confidence in the corporation, resulting in further liquidity difficulties and the support /

[6] Para. 27 of the Draft Guidelines

[7] Para. 16(b) of the Draft Guidelines

assistance having insufficient time to serve its intended purpose of helping the corporation resolve its difficulties.

6.4 Trading suspension

- We ask the Bureau to consider adding a safe harbour for a listed corporation which has suspended trading of its securities on the SEHK pending release of an announcement containing inside information. Of course, listed companies must not abuse the ability to suspend trading. As already reflected in the Listing Rules, suspension of trading must be kept to a minimum.

6.5 We note that a listed corporation is required to preserve the confidentiality of the inside information if it wishes to take advantage of the safe harbours. Once there is a leak, the listed corporation must disclose the information. In the case of a leakage of information regarding an impending negotiation or incomplete proposal, this would mean that the listed corporation will have to disclose the information even if doing so will prejudice the outcome of the negotiation or the proposal. We submit that in such circumstances, rather than requiring the listed corporation to disclose all relevant information, it should be allowed to just make a clarification announcement so that the market will be kept generally informed.

Appendix

Joint Submission of Clifford Chance and Linklaters to the Financial Services and the Treasury Bureau in response to the Consultation Paper on the Proposed Statutory Codification of Certain Requirements to Disclose Price Sensitive Information by Listed Corporations (March 2010)

Financial Services and the Treasury Bureau

Consultation Paper on the Proposed Statutory Codification of Certain Requirements to Disclose Price Sensitive Information by Listed Corporations (March 2010)

Joint Submission of Clifford Chance and Linklaters

Executive Summary:

- This paper sets out the views of Clifford Chance and Linklaters on the Consultation Paper on the Proposed Statutory Codification of Certain Requirements to Disclose Price Sensitive Information by Listed Corporations released by the Financial Services and the Treasury Bureau in March 2010.
- Clifford Chance and Linklaters have also made a joint submission to the Securities and Futures Commission ("**SFC**") in response to its related Consultation Paper on the Draft Guidelines on Disclosure of Inside Information released in March 2010. The joint submission is appended to this Paper.
- Clifford Chance and Linklaters do not seek to challenge the Bureau's regulatory objective to codify certain requirements to disclose price sensitive information ("**PSI**") and note, in particular, that the sanctions behind the proposed statutory regime are restricted to civil sanctions. We also do not seek to challenge the primary proposal to adopt the definition of "relevant information" from the insider dealing regime under the Securities and Futures Ordinance ("**SFO**") to define PSI.
- However, we have comments on certain specific aspects of the proposals, including: the SFC's views on what constitutes information "generally known" to the market; the limited disclosure mechanism; the wide definition of "officers"; the provision that deems the listed corporation to have knowledge of the PSI if its officers "ought reasonably to have" known the information; and the proposal to remove the Financial Secretary as the decision-maker concerning the commencement of Market Misconduct Tribunal inquiries.
- Our responses to the questions posed for consultation are set out below.

1 Question 1(a)

Do you agree with the proposal to adopt the existing definition of "relevant information" from the insider dealing regime under the SFO to define PSI?

1.1 We do not disagree with the adoption of the definition of "relevant information" from the insider dealing regime under the SFO to define PSI.

1.2 The Draft Guidelines on Disclosure of Inside Information ("**Draft Guidelines**") published by the SFC set out to summarise the key aspects of what has been viewed by the tribunals in Hong Kong as constituting "relevant information". We believe it would be helpful to include principles from the ***case relating to the listed securities of Tingyi (Cayman Islands) Holding Corp.***, which was omitted from the cases listed in the Draft Guidelines, including that:

- Information will be "specific" if it is capable of being "pointed to, identified and unequivocally expressed", which, in the case of financial information about a listed group means whether the information carried such particularity about aspects of the listed group's financial and economic functioning so as to allow those matters to be identified and coherently described and the information about them to be understood.
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- In most cases only net profit figures ("bottom line results") are likely to be price-sensitive, and therefore raw financial data would not be price-sensitive unless it was possible to calculate net profit data from them.
- In most cases, an understanding of the market's knowledge of a company's affairs is obtainable only by considering what has been said or published in the media, or in other materials which are readily accessible by the market. An assessment must be made of the completeness of the information released into the market and the degree of penetration of the market.

2 Question 1(b)

Do you agree that a listed corporation should be obliged to disclose to the public as soon as practicable any "inside information" that has come to its knowledge, and that it should be regarded to have knowledge of the inside information if a director or an officer has come into possession of that information in the course of the performance of his duties?

2.1 "As soon as practicable"

- We agree with the general principle that a listed corporation should disclose PSI as soon as practicable. However, the Draft Guidelines suggest that "as soon as practicable" means "immediately"[8]. We do not think this is correct. We ask that the SFC provides further guidance on what actions a listed corporation could take to comply with the "as soon as practicable" requirement in circumstances where immediate disclosure is not practicable, for instance:
  - Upon the receipt of a whistle blower's report or discovery of a potential problem, the scale of which is completely unknown, on a matter that is potentially price sensitive, the listed corporation may need some time to verify whether the allegations have any substance or the potential scope of what may need to be investigated to get to the bottom of the issue, before deciding whether to disclose the matter (be it in a "holding announcement" or a "full

[8] para. 32 of the Draft Guidelines

announcement"), otherwise the market may be inundated with information that lacks integrity and that may even mislead investors.

- There may be some time lag between the time when an officer comes into possession of a piece of inside information and the time when the decision makers in the listed corporation are made aware of the information. This is especially the case for larger size listed corporations. Please also see our submission below in relation to the definition of "officer".

- We ask that the regulators take a practical and reasonable approach in determining whether disclosure has been made "as soon as practicable".

2.2 "Officer"

- We agree with the principle that a listed corporation should be regarded to have knowledge of the inside information if certain of its officers have come into possession of that information in the course of the performance of their duties.

- However, many listed corporations in Hong Kong are very sizeable and may have thousands of managers. The proposed definition of "officer" is so wide that many staff who do not have the authority to influence the decision on PSI disclosure, or from whom there are a few levels of reporting before the information will reach the decision makers, are considered as "officers". To deem a listed corporation to have the knowledge that any of its officers (which can include junior managers) has would make the legislation very difficult and costly to comply with, and again may lead to "over-disclosure" if officers choose to "play it safe" and make disclosure indiscriminately.

- We note that the Chinese translation of "officer" in the proposed legislation refers to "senior officer" but the English definition does not contain the same qualification. We propose that for the purpose of the new Part IIIA of the SFO, the definition of "officer" be refined so that it will only include:

  - directors; and

  - senior officers who are expected to come into possession of PSI because of the nature of their role within the listed corporation. We suggest that such senior officers should be company secretaries, senior public relations managers, and senior legal counsel / senior compliance officers.

2.3 Corporations listed on Hong Kong and PRC exchanges

- Whilst the Draft Guidelines provide guidance on disclosure in cases where inside information is released to another market when the market in Hong Kong is closed (including the possibility of requesting a suspension in trading its securities pending the issue of the announcement in Hong Kong[9]), there is no similar guideline addressing the situation where the release of inside information in Hong Kong is on hold pending a synchronised release in another market.

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[9] para. 65 and 66 of the Draft Guidelines

- We understand that a corporation that is dual-listed on a PRC stock exchange and the Stock Exchange of Hong Kong ("**SEHK**") cannot post announcements directly on the websites of the PRC exchange, and as a result the timing of posting announcements in the PRC is beyond the corporation's control. We further understand that the periods for posting announcements on PRC exchange websites are more restrictive than those for posting announcements through HKEx-EPS. In order for a PRC / Hong Kong dual-listed corporation to ensure equal dissemination of information to its shareholders, there may be a delay in the disclosure in Hong Kong. We therefore ask that:
  - the regulators take into account the need to wait for the PRC exchange(s) to post the announcement when determining whether a disclosure in Hong Kong has been made "as soon as practicable"; and
  - the SFC provides guidance on disclosure in a case where disclosure in Hong Kong needs to be delayed pending disclosure in the PRC (including the possibility of a trading suspension in the meantime).

2.4 "ought reasonably to have"

- The proposed legislation[10] provides that a listed corporation is deemed to have knowledge of the inside information if an officer of the corporation ought reasonably to have come into possession of the information in the course of performing functions as an officer of the corporation.
- Since a breach of the proposed disclosure obligation might not involve a clear deliberate act or behaviour, we are of the view that if:
  - as proposed, there is already a requirement to take all reasonable measures to ensure that proper safeguards exist to prevent the breach of a disclosure requirement[11];
  - the officers have indeed taken all reasonable measures to ensure compliance; and
  - the officers do not have actual knowledge of the inside information,

  then the listed corporation should not be liable for a failure to disclose. The requirement under the proposed s.101G(1) should provide enough protection to the public. To include an additional deeming provision on the basis of constructive knowledge would suggest that there is something else the officers should do on top of taking all reasonable measures to ensure compliance. Any such additional obligations may (i) create undue administrative burden on the listed corporations and their officers; and (ii) result in listed corporations making disclosure indiscriminately in order to "play it safe".

[10] s.101B(2) of the SFO

[11] s.101G(1) of the SFO

3 Question 1(c)

Do you agree with the proposal that the disclosure must be made in a manner that can provide for equal, timely and effective access by the public to the information disclosed?

3.1 We agree with the principle that disclosure should be made in a manner that can provide for equal, timely and effective access by the public to the information disclosed. However, we see some practical difficulties in complying with the operative provisions (further discussed in 3.2 below). In addition, we are concerned that an overly strict approach in determining what constitutes information "generally known" to the market might unfairly restrict institutional investors from participating in capital raising activities (further discussed in 3.3 below).

3.2 HKEx-EPS

- The proposed disclosure mechanism appears to be overly restrictive. Under the current proposals, listed corporations can comply with the disclosure requirement by disseminating information via the Electronic Publication System adopted by the Hong Kong Exchanges and Clearing Limited ("**HKEx-EPS**"). While the draft legislation does not limit the manner of disclosure, the SFC has stated in its Draft Guidelines that the disclosure requirement is only likely to be satisfied by disseminating information via the HKEx-EPS. This will likely cause compliance difficulties for listed corporations, especially where a price sensitive event takes place outside of the operating hours of the HKEx-EPS.
- As such, we submit that:

  (i) disclosure of information via other means should also be allowed, e.g., via widely subscribed news or wire services (such as Bloomberg and Reuters), and posting an announcement on the listed corporation's own website; or

  (ii) if the Bureau is not prepared to accept other disclosure mechanisms, then the SEHK should at least enhance the HKEx-EPS to allow continuous disclosure.

3.3 "Generally known"

- To date, the institutional market has carried out capital raising activities (in particular, convertible bond offerings) on the basis that launch communication and news coverage published via widely subscribed news / wire services, such as Bloomberg or Reuters, are sufficient public disclosure of the relevant information to make it "generally known" among the institutional investor community.
- Accordingly, institutional investors who participate in capital raising activities have proceeded on the basis that they can borrow stock to hedge their exposure before the issuer's announcement on the SEHK.

- The Draft Guidelines, however, provide that widely circulated press reports cannot constitute sufficient public disclosure[12]. This suggests that the SFC considers disclosure via widely subscribed news / wire services not sufficiently public for the purposes of insider dealing prohibitions. If this is the case, any over-the-counter stock borrowing that happens before the issuer's announcement may risk contravening the insider dealing prohibition. In other words, the whole institutional market in the issuer's stock will effectively be restricted pending the formal announcement on the SEHK.
- Stock borrowing activity is critically important to certain capital raising activities. We urge that the SFC provides specific guidance as to its views on the application of the insider dealing prohibition to these stock borrowing activities. If the SFC is of the view, contrary to current market practice, that the launch communication of a deal is not sufficient public disclosure to make all relevant information "generally known" among the institutional investor community, and therefore that the stock borrowing activities by investors is inappropriate prior to the formal announcement by the issuers, it is likely to materially impact the willingness of institutional investors to participate in certain capital raising activities and, therefore, the continued viability of certain capital raising options for listed issuers.
- We understand that in some jurisdictions (e.g., the UK), disclosure via widely subscribed news information services is expressly permitted as a form of public disclosure, and in some other jurisdictions (e.g., Singapore and Australia) it is generally accepted that disclosure via widely subscribed news information services is sufficiently public among the institutional investor community, for the purposes of their respective insider dealing prohibitions.

4 Question 2(a)

Do you agree to the provision of the four proposed safe harbours?

4.1 We welcome the provision of the four proposed safe harbours. However, we submit that certain of these safe harbours should be extended and additional safe harbours should be introduced – see our submission under Question 2(c) below.

5 Question 2(b)

Do you agree that the SFC should be empowered to grant waivers, and to attach conditions thereto?

5.1 We agree that the SFC should be empowered to grant waivers, and to attach conditions thereto.

5.2 We believe it would be helpful to the market if the SFC could publish on its website or otherwise in a manner that allows easy public access the details of the waivers granted and conditions imposed (or at least the more representative ones).

[12] para. 19 of the Draft Guidelines

6 Question 2(c)

Do you think that the legislation should provide for additional safe harbours? If so, what are these additional safe harbours?

6.1 We believe that certain of the proposed safe harbours should be extended and that additional safe harbours should be introduced. We discuss these below.

6.2 Safe Harbour B (incomplete negotiations or proposals)

- There are incomplete negotiations or proposals the outcome of which may not be prejudiced if the information is disclosed prematurely (and therefore the proposed Safe Harbour B would not be applicable), but the information so disclosed may be misleading due to the lack of integrity, certainty or details. The following are a couple of examples:
  - Management accounts: The Draft Guidelines[13] seem to suggest that once a listed corporation becomes aware that its financial results may not meet the market expectation, it should immediately disclose such information even if the final accounts are not yet available. We would like to ask the SFC to confirm whether this understanding is correct. If it is, we submit that listed issuers should not be required to make a disclosure if the information subject to disclosure may be misleading to the market. Information may be misleading if it is based on preliminary results which have not been verified or are pending expert reports;
  - Share placing: The Draft Guidelines[14] provide that the contemplation of a forthcoming share placing will need to be disclosed if the placing is likely to materially affect the price of the shares. Disclosure is required even if the details of the placing are not known. Since the details of a placing (such as the size, price and timing of it) can materially affect the price of the shares, the announcement of a contemplation of a share placing without details of the placing can be misleading.
- Accordingly, we propose that Safe Harbour B be amended as follows:

  "When the information is related to impending negotiations or incomplete proposals:

  (i) *the outcome of which may be prejudiced if the information is disclosed prematurely; or*

  (ii) *the information may be misleading to the persons who are accustomed or would be likely to deal in the listed securities of the corporation."*

6.3 Safe Harbour D (liquidity support)

- Safe Harbour D currently only applies when the Government Exchange Fund or a central bank provides liquidity support to the listed corporation.

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[13] Para. 27 of the Draft Guidelines

[14] Para. 16(b) of the Draft Guidelines

- We ask the Bureau to consider extending this safe harbour to cover all types of liquidity support, financing proposal and rescue plan, whether provided by the Government Exchange Fund or a central bank or otherwise. This is because the same problems with immediate disclosure arise regardless of the type of support, and who provides the support. Immediate disclosure of the receipt of liquidity support or other types of assistance by a listed corporation could lead to a loss of confidence in the corporation, resulting in further liquidity difficulties and the support / assistance having insufficient time to serve its intended purpose of helping the corporation resolve its difficulties.

6.4 Trading suspension

- We ask the Bureau to consider adding a safe harbour for a listed corporation which has suspended trading of its securities on the SEHK pending release of an announcement containing inside information. Of course, listed companies must not abuse the ability to suspend trading. As already reflected in the Listing Rules, suspension of trading must be kept to a minimum.

6.5 We note that a listed corporation is required to preserve the confidentiality of the inside information if it wishes to take advantage of the safe harbours. Once there is a leak, the listed corporation must disclose the information. In the case of a leakage of information regarding an impending negotiation or incomplete proposal, this would mean that the listed corporation will have to disclose the information even if doing so will prejudice the outcome of the negotiation or the proposal. We submit that in such circumstances, rather than requiring the listed corporation to disclose all relevant information, it should be allowed to just make a clarification announcement so that the market will be kept generally informed.

7 Question 2(d)

Do you agree that the SFC should be empowered to prescribe further safe harbours in the form of rules under the SFO?

7.1 We agree that the SFC should be empowered to prescribe further safe harbours in the form of rules under the SFO.

8 Question 3(a)

Do you agree to extend the jurisdiction of the MMT to handle breaches of the statutory disclosure requirements?

8.1 Assuming the definition of "relevant information" is adopted for continuous disclosure obligations of listed companies in the manner that is contemplated, there is a high degree of overlap, in terms of the legal questions and factual enquiries that would need to be undertaken, between the existing jurisdiction of the MMT, as regards insider dealing, and the proposed new statutory provisions. In principle, therefore, it would appear to make sense for the MMT to be given extended jurisdiction to handle breaches of the statutory disclosure requirements.

8.2 Also, we would certainly prefer to see any such breaches investigated and dealt with by a tribunal that is independent of the SFC itself, to ensure the avoidance of

any perception of absence of adequate due process and fairness, given the other aspects of the SFC's role (as enforcement authority and the provider of guidance) in regard to the proposed new provisions.

8.3 We would be anxious to ensure that only, "serious" breaches become the subject of MMT inquiries, not least because the MMT will inevitably have limited resources and it is important that those resources are devoted to serious cases. The involvement of the Financial Secretary was a way of ensuring that this filtering occurred. If the filter is to be removed, we believe it is important that some form of guidelines be developed to ensure that this filtering process continues to be effective. This is particularly important if, as envisaged, the removal of the Financial Secretary's involvement is to be extended to market misconduct matters as well. We do recognize that the filtering system has slowed down the process of cases getting before the Tribunal and lengthy delays corrodes the perception of effectiveness of the Tribunal system as well as, in certain cases, being disadvantageous to those whom are subject to inquiries. However, some form of effective filter, which can be independently monitored is important. Amongst other things, we would not want to see respondents feeling under pressure to settle disciplinary or civil actions in the face of threatened Tribunal proceedings, where the matters are on any objective basis not serious enough to warrant Tribunal proceedings. We suggest that this issue be carefully explored further before any change is made to the existing legislative provisions.

8.4 In addition in the case of alleged breaches that are referred to the tribunal, it is likely that the tribunal would be faced with a new subset of issues, which it does not have to deal with in the context of insider dealing inquiries. This subset of issues concern the exercise of judgement by directors as to: (i) the appropriate timing for the making of an announcement; (ii) in cases of alleged negligence by directors in particular INEDs (independent non-executive directors) who were not directly involved in the decision whether to make an announcement or not, an assessment of whether they did what they reasonable could in the circumstances to prevent the alleged breach from occurring. Directors of listed companies facing the prospect of such scrutiny by the tribunal, are entitled to be assured that the members of the tribunal have sufficient practical experience of the challenges and complexities involved by being a director of a listed company so as to reach conclusions in respect of these issue of judgement which are fair and appropriate in all the circumstances. Nothing in the Consultation Paper indicates a clear intention to review the panel of potential members of the tribunal. We believe that this should be addressed.

9 Question 3(b)

Do you agree with the proposed range of civil remedies as set out in paragraphs 2.31, 2.35 and 2.36?

9.1 We note that the maximum fine of HK$8 million is a considerably high amount for directors of PRC state-owned enterprises. The fine together with disqualification orders should be sufficiently deterrent. We are concerned that the remedy set out in paragraph 2.35 will lead to so high a financial exposure for listed corporations that they would choose to disclose information indiscriminately, resulting in the

market being inundated with too much information which may not help the investors in making an informed decision.

9.2 We would also be concerned to ensure that the approach adopted to imposing civil remedies does not have an undue deterrent effect on good quality individuals being willing to become directors of listed companies.

10 Question 3(c)

Do you agree to grant the SFC direct access to the MMT to institute proceedings on breaches of the statutory disclosure requirements?

10.1 See comments above in response to question 3(a).

11 Question 4

Do you agree that the SFC should provide informal consultation for the listed corporations with regard to the statutory disclosure requirements, initially for a 12-month period?

11.1 We agree that the SFC should provide informal consultation for the listed corporations with regard to the statutory disclosure requirements, initially for a 12-month period, subject to review as to whether an additional period would be necessary.

11.2 We believe it would be helpful to the market if the SFC could publish on its website or otherwise in a manner that allows easy access by the public FAQ type guidance (containing questions asked by the enquirers and answers provided by the SFC, as well as any views of the SFC on issues raised) during and at the conclusion of the consultation period.

11.3 We understand that the SFC expects that the questions for consultation will generally relate to the application of the safe harbours, rather than deciding for a listed corporation whether certain information has to be disclosed. In other words, the SFC expects that the listed corporations have decided whether or not the information in question is inside information before they consult the SFC in relation to the application of the safe harbours. This limited approach to the SFC's role appears correct to us – the question in particular of whether information is price-sensitive must be left ultimately to the judgement of directors, who are best placed to answer that question. Kindly confirm whether this understanding is correct.

12 Question 5

Do you think the administration and enforcement arrangements proposed by the SFC and SEHK in paragraphs 3.8 – 3.9 are appropriate? Do you have any comments on the respective roles of the SFC and SEHK to further enhance clarity?

12.1 We are of the view that the regime would be more efficiently regulated by one regulator rather than two. This would minimise the possibility of conflicting decisions or approaches between two regulators and compliance costs. To this end, the SFC can be the frontline regulator and as pointed out in the consultation

paper, SEHK may bring disciplinary action against a listed corporation and/or its directors based on infringements found in proceedings brought by the SFC.