香 港 上 市 公 司 商 會
THE CHAMBER OF HONG KONG LISTED COMPANIES

June 28, 2010

The Securities and Futures Commission
8/F Chater House
8 Connaught Road Central
Hong Kong
Attention: Corporate Finance Division

Dear Sirs,

Re: Consultation Paper on the Draft Guidelines on Disclosure of Inside Information ("Consultation Paper")

The Chamber of Hong Kong Listed Companies (the "Chamber" or "We") is pleased to submit a response to the Consultation Paper.

Providing the guidelines is important, but equally important is for the SFC to give guidance to listed companies as to the procedures to be followed when a PSI event is developing and what and how a listed company should do to satisfy itself whether there is an obligation to disclosure. We noted the Guidelines are not legally binding. We would like the SFC to clarify the status of the Guidelines and the consequence of compliance or non-compliance with them; the same clarification should be given to the status of any informal advice and guidance given by the SFC on informal consultation and the consequence of compliance and non-compliance with such advice and guidance. We believe that listed companies should be able to use due compliance with the SFC guidelines and informal advice by the SFC during informal consultation as a line of defense where liabilities arise from failure to disclose.

That said, we would provide our comments to the guidelines, or where we would seek clarification, under their respective headings in the Consultation Paper as follows:

1. What may constitute inside information

Paragraph 16(b) states that inside information must be specific but may not be precise. It cites "contemplation of a forthcoming share placing even if the details are not known" as an example of inside information. Paragraph 16(b) continues to say that a proposal "described as under contemplation should have more substance than merely at the stage of vague exchange of ideas or a 'fishing expedition'" to be regarded as specific information. Where SFC draws the line between a "contemplation with unknown details" and a "contemplation with substance" needs to be better defined in order to avoid market confusion.

Concerning the materiality test, paragraph 23 puts that *"whether the information is likely to materially affect the price is a hypothetical one"* and *"the exercise in determining how the general investor would behave ... has necessarily to be an assessment."* In other words, what amounts to "material" effect are practically no clear cut matter and are difficult to be put in precise terms. Determining what is price sensitive or not, and over the timing of disclosure, if deemed necessary, will always to some extent be a matter of subjective

香港灣仔皇后大道東183號合和中心21樓2102室
Room 2102, 21st Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong
電話 Tel: (852) 2970 0886 傳真 Fax: (852) 2970 0555 網址 Website: http://www.chklc.org

judgment and discretionary based on what is known at the time as such decision is made. Therefore, it is important that when determining whether the disclosure obligation is breached, the SFC must satisfy itself that both the elements of "*mens rea*" and "*actus reus*" are present, and the strict liability concept must not be applied. The draft clause 101G(2) of the legislation recognises this in relation to 'officers', but the requirement for the non-disclosure to be intentional, reckless or negligent also needs to be recognized in relation to the company itself.

In this regard, the Chamber has in our submission to the FSTB recommended a safe harbour which provides relief to a listed company and its directors the obligation to disclose when they had duly and carefully considered a piece of inside information and concluded in good faith that the information would not materially affect the share price. Under this Safe Harbour, if subsequently the information is found to be causing material price change -- due to unexpected market reaction or change in market circumstances which is unforeseeable at the time the non-disclosure decision was made, the corporation and its directors will not be held liable as long as it can show clear and proper records of proper board deliberations leading to a reasonable conclusion that, without the benefit of hindsight, the information needed not to be disclosed at the material time.

2. Examples of possible inside information concerning the corporation

The range of events which could be considered as inside information listed in the paragraph 29 contains many that are covered by Chapter 14 of the Listing Rules under Notifiable Transactions and Connected Transactions already. Given this, would a failure to disclose any such transactions and hence in breach of chapters 14 and 14A of the Listing Rules will mean and imply a breach of the PSI rules? If so, this is no different from legalising or codify the Listing Rules by this PSI regime; incurring sanctions including fine and disqualification. The market needs to be explained about the implication.

It is also important that double regulation be avoided. The PSI regime must strictly take precedence over the Listing Rules, otherwise listed corporations would be subject to both civil remedies under the PSI regime and disciplinary actions under the Listing Rules.

Certain events listed in this section are currently not discloseable, such as pledging of shares by controlling shareholders, which is currently governed by SFO and is not required to be disclosed if the shares are pledged to banks, and changes in directors' service contracts. Although it is stated in paragraph 30 that the events are not 'automatically' inside information, the market would be benefitted if the guidelines can specifically say that events included on the list does not mean they are presumed to be inside information, and a mere failure to disclose any of these events does not in itself constitute a suspected case of breach of the disclosure requirement. This will clear the market of worries of over-disclosure.

3. When and how should inside information be disclosed

Paragraph 32 states that "a corporation must disclose any inside information to the public "as soon as practicable"..... [which] means that the corporation should immediately take all necessary steps that are reasonable in the circumstances to disclose the information." We agree in principle a listed corporation has the duty to disclose "inside information", however

we are concerned that the notions of "as soon as practicable" and of "immediately" are not easy to comply with and disputes may arise. A company will take time to conduct investigation, assess implications and seek legal advice. The guidelines should state clearly that the company is allowed time to do so. Alternatively, SFC should provide guidance on how long is "as soon as practicable" and "immediate".

4. Responsibility for compliance and management controls

Paragraph 43 states that "an officer means a director, manager or secretary of, or any other person involved in the management of, the corporation". We consider this definition of "officer" too wide. For a large corporation, there may be many manager-grade employees and it would be very difficult to ensure that all managers report inside information immediately. We also observe that fact that under the UK regime for price sensitive information disclosure, it is only the directors who *knowingly* breach the disclosure requirement would be held liable, not even company secretaries. It is inappropriate for individual employees such as managers, as opposed to directors, to be held liable for the company's breach, even if they have acted intentionally, recklessly or negligently, but this would be the effect of Clause 101G(2). We agree with the UK approach of holding only directors liable since it is they who make the decision. We recommend that Hong Kong follows the UK regime and require only directors to be subjected to the proposed legislation. The definition of "officer" should therefore include only "director" throughout the draft legislation.

The same paragraph further says that "the corporation is considered to have knowledge of the inside information when one or more of its officers come into possession of that information in the course of performing functions as officers of the corporation." This is onerous. As stated above, if the definition of the officers remains to be so wide, it is hard for the company to ensure all "officers" to report inside information, disregard the systems and procedures in place. We would argue that in the case of a corporation having established and maintained appropriate and effective systems and procedures to require its officers or employees of any level to report inside information, and should the officers or employees fail to follow them, it is they who are primarily at fault, not the corporation.

Likewise, for what is stated in paragraph 44, the corporation should have a good defense if it could demonstrate that appropriate and effective systems and procedures are in place and officers and employees are made aware of them, yet it has never had knowledge of the information, because the officers or employees possessing the price sensitive information had failed to inform it, and it has not acted intentionally, recklessly and negligently.

Paragraph 46 follows s.101G and states that "officers are obliged to take all reasonable measures to prevent the corporation from breaching the statutory disclosure requirement". Our views on this are that, as said before, the definition of officers, which include "managers", is too wide. At most, "managers" should be expected to follow the safeguards put in place by the listed corporation but not assuming the obligations to "ensure that proper safeguards exits". As for directors, the civil remedies of breaching the disclosure requirement for them are deterrent enough and would provide sufficient disincentive to non-compliance. It would be excessive to impose further obligations on them and therefore this requirement should be abolished. The onus is on the company to ensure it would not breach any statutory disclosure requirement.

5. Safe harbours that allow non-disclosure of inside information

Paragraph 47 refers to s.101D(1)(b) that if the information intended to be kept confidential is leaked, any safe harbours will no longer apply and the corporation has the obligation to disclosure. There is a need to further clarify the handling of leakage or rumours under the safe harbours. For example, under Safe Harbour A, disclosure of an investigation by the ICAC can be withheld except there are market rumours about the investigation or the investigation is leaked. However, a disclosure will still be seen as contravening the Prevention of Bribery Ordinance putting the listed corporation in a dilemma. More guidance from the SFC as to the extent of disclosure should be made without prejudicing the criminal investigations (or even the judicial process) would be necessary.

Sometimes, an inside information may be leaked but the leakage is not caused by the company and is beyond its control. To withdraw the safe harbour in this circumstance is too restrictive. If a leakage does not contain extensive and accurate information about the event that requires disclosure, for example, it only suggests a major acquisition is being negotiated and no crucial details are given, it is only fair the company can seek a waiver from the SFC from making a disclosure. This will allow the company to continue its negotiation and not divulge crucial information prematurely that would jeopardise the negotiation.

We also notice some incongruities between the wording of the draft Guidelines and the Government's proposed legislative provisions as in the followings:

- In paragraph 49, the SFC states that the safe harbours will no longer apply if the company becomes aware that confidentiality has been lost. However, the draft clause 101ID (1)(b) implies that the safe harbours would no longer apply, and the disclosure obligation triggered, even if the company had no knowledge of the leak. The SFC's position is preferred since it is fairer.

- Paragraph 55 states that the safe harbour in question will apply not just where the outcome of a proposal or negotiation may be prejudiced but also where its normal pattern may be prejudiced. However, draft clause 101ID(1)(c)(ii) states that the safe harbour will only apply where the outcome may be prejudiced. The draft clause is too restrictive, and the wordings of paragraph 55 are therefore preferable.

6. Dealing with rumors

Paragraph 62 states that "if a corporation wishes to respond to rumours, the corporation should do so by making a formal announcement, rather than making a remark to a single publication or by way of a press release". However, there are times when a single or a limited few publications report a rumour that is not true or contains no accurate facts and the corporation may still want to make a denial, then it should be allowed to make the denial or clarification to those media concerned, provided that no inside information is given. Publishing a formal announcement responding to the rumour would unwittingly spread the rumour further and arouse further speculation unnecessarily.

7. Publications by third parties

Paragraph 70 states that a third party report, for example, from a rating agency which is expected to have significant consequences directly affecting the corporation may be inside

information and should be disclosed. It is often the case that a rating agency would share the draft of the rating report with the corporation or inform it of its intended rating before publication or announcement. Under the guidelines, upon seeing the report or knowing the intended rating, the corporation is under obligation to disclose immediately. Such disclosure may pre-empt the publishing of the report or the announcement of the rating itself and is not practicable. The company should be allowed to hold the disclosure until the rating report is published so that it can make reference to the report itself directly.

I hope you would give our comments due consideration and make clarifications to our queries. If you wish to discuss any of these further, please feel free to contact us.

Yours faithfully,

Mike Wong
Chief Executive Officer
The Chamber of Hong Kong Listed Companies