FRESHFIELDS BRUCKHAUS DERINGER

HONG KONG
11th floor
Two Exchange Square
Hong Kong
T+852 2846 3400
Direct T+852 2913 2617
F+852 2810 6192
Direct F+852 2810 6192
G4 F+**852 2502 2009**
E julian.gooding@
freshfields.com
W freshfields.com

富而德律師事務所
香港中環交易廣場
第2座11樓
電話+852 2846 3400
圖文傳真+852 2810 6192
DOC ID HK003801.846/3+
OUR REF KIN/JG
YOUR REF

SFC (Stock Market Listing Rules)
Attn: Corporate Finance Division
12/F, Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

7 June 2002

Dear Sirs

Securities and Futures (Stock Market Listing) Rules

Thank you for allowing us the opportunity to comment on the draft Securities and Futures (Stock Market Listing) Rules (the ***Rules***) and on the draft Securities and Futures (Transfer of Functions-Stock Exchange Company) Order (the ***Order***). We are content for this submission to be published on the SFC's website.

General

We share the SFC's view that the Hong Kong market should benefit from an effective disclosure regime backed up by proper enforcement, encompassing both appropriate investigatory powers and sanctions. However we are not convinced that the proposals set out in the Consultation Paper will assist in achieving this goal in a manner conducive to the proper operation of the market.

Disclosure to the SFC

The Consultation Paper suggests that there are two purposes in requiring listed companies to file disclosures with the SFC: first, so that the company may face an additional liability under s384 of the Securities and Futures Ordinance (the ***Ordinance***) for any false or misleading disclosure to the public; and secondly, so that the SFC may use its investigatory powers under section 182 of the Ordinance. The SFC seeks to use these powers to regulate the quality of disclosure by listed companies to the public.

However the Ordinance already includes at sections 277 and 298 provisions dealing with the public disclosure of false or misleading information. The Legislative Council included in these provisions a safeguard to the effect that a wrong would only be committed if the information was likely to induce a subscription, sale or purchase of securities or likely to maintain, increase, reduce, or stabilize the price of securities. Proceedings brought for false and misleading disclosure under section 384 of the Ordinance in relation to listing documents would not include this safeguard and effectively lower the threshold for liability. We do not believe that it is appropriate (and it may even be *ultra vires*) for the SFC to create secondary legislation with this effect.

This concern is reinforced by a consideration of the purpose of section 384 of the Ordinance, which creates an offence for the knowing or reckless submission of false or misleading information to the SFC (or other specified recipients) in compliance with a requirement to provide information. The provision (introduced into Hong Kong legislation in 2000) is intended to ensure that when the SFC requests information as part of a regulatory enquiry or consistent with its regulatory functions it can take action when the information it receives is false or misleading. We believe that the provision was intended to be used to regulate disclosure of information to the regulator and not to the public.

Paragraph 14 of the Consultation Paper suggests that following implementation of the Rules the SFC will be able to invoke its powers under section 182 of the Ordinance to carry out investigations into cases of false or misleading disclosure to the public. However, even without the Rules, the SFC can invoke these powers where it has reasonable cause to believe that market misconduct (including a breach of section 277 of the Ordinance) has taken place. The proposed requirement in the Rules to file disclosure with the SFC does not appear to extend the circumstances in which the SFC's investigatory powers can be used.

Section 23 of the Ordinance gives the power to a recognized exchange company to make rules for the proper regulation and efficient operation of the market that it operates. These rules may include matters relating to applications for the listing of securities and the requirements to be met before securities may be listed (section 23(2)). In the event that HKEX re-make the Listing Rules under this power when the Ordinance comes into force, section 384 would apply to any false or misleading information submitted to HKEX. For the purposes of section 384, a "specified recipient" includes a recognized exchange company. It is not clear that disclosure of information to the SFC is required to ensure that section 384 applies to listing documentation.

This proposal will also give concern in the market as to how the SFC and HKEX will resolve differences between themselves as to the required level of disclosure in listing documents. Differences may also arise over whether the issuer and its securities are suitable for listing. We suggest that the Memorandum of Understanding to be entered into between HKEX and the SFC should be made public. There is also a market concern as to the resources the SFC will need to devote to reviewing each Hong Kong listing prospectus within 10 days of submission, given that the Consultation Paper states that it intends the power to be a "reserve power", and will continue to rely on the frontline regulation of the HKEX.

Costs

At paragraph 9 the Consultation Paper asserts that the proposals would not lead to additional costs to listed companies or to the market. From a practical point of view it seems that an applicant for listing may need to respond to comments on the draft listing document from both HKEX and the SFC. Any exercise of the power by the SFC will therefore increase costs through compliance with the SFC's requests.

Exercise of the power set out in rule 5(4) may lead to significant delay: once the request has been made, and the information been supplied, it is still open to the SFC to require further information. The significant delay to the application process in circumstances where the HKEX may itself be satisfied with the level of disclosure may render the Hong Kong market less attractive to applicants for listing. This is especially true for those applicants seeking a listing in more than one jurisdiction, where an unforeseen delay in Hong Kong will have a significant impact on the international listing. While it is sensible for a full merit review of the new Securities and Futures Appeals Tribunal to be available, will in practice an applicant for listing be able to obtain a prompt resolution of any dispute?

International best practice

Paragraph 24 of the Consultation Paper suggests that the proposals would bring the Hong Kong regulatory regime into line with international practice. In the sense that all major jurisdictions provide for statutory investigation and enforcement against false or misleading disclosure this is true. However in the UK an applicant for listing need only liase with a single regulator, the UK Listing Authority, to determine the adequacy of disclosure in the listing documents. The London Stock Exchange plays no part in pre-vetting documents in relation to the listing of securities. We are of the view that it is preferable for there to be only one regulator with responsibility for pre-vetting documents, as is the norm in international securities markets.

Comment on the Rules

Rule 5

The aim of these proposals is to give the SFC the power properly to regulate disclosure of information to the public. As such, the SFC has the power under the Rules to require the disclosure of further information or to object to a listing in circumstances where it considers the disclosure to be false or misleading. However the Rules also give the SFC the power to object to a listing where it would not be in the interest of the investing public or in the public interest for the securities to be listed (clause 5(6)(d)). This does not sit easily with the sole aim of regulating disclosure. It also duplicates the residual power of the HKEX under the Listing Rules not to admit securities to listing unless it considers the issuer and its business to be suitable.

Inclusion of such a power will inevitably lead to pressure on the SFC to object to a listing as part of "merit regulation" on the grounds that the listing would not be in the interest of the investing public. It also suggests that in certain circumstances it may be prepared to regulate corporate transactions despite the view set out in paragraph 29 of the Consultation Paper and in recent open correspondence by the SFC. It is also not clear what information the SFC would have available to make such a decision if it were not solely based on the inadequacy of disclosure: what power would the SFC rely on to collect evidence as to the suitability of securities to be listed? In consequence, we recommend the deletion of clause 5(6)(d).

We have no comments on the Order.

Please do not hesitate to contact Kay Ian Ng or Julian Gooding if you would like to discuss any of the matters raised in this letter.

Yours faithfully

Freshfields Bruckhaus Deringer

Freshfields Bruckhaus Deringer