

Rule Changes Consequential on Statutory Backing to Issuers' Continuing Obligation to Disclose Inside Information

Listing Division, HKEx

Agenda

- (1) Overview
- (2) Roles of Exchange and SFC
- (3) Issuer's obligations
- (4) Trading halt
- (5) Other specific obligations/amendments

Overview

May 2012	The Securities and Futures (Amendment) Ordinance (including the Inside Information Provisions (Part XIVA)) passed
August	Consultation paper on Rule changes consequential on the Inside Information Provisions
October	Consultation period end
November	Consultation conclusion
1 January 2013	Effective date of the Inside Information Provisions and new Rules

What is given statutory backing?

The Securities and Futures (Amendment) Ordinance codifies listed issuers' continuing obligation under the Rules to disclose price sensitive information (called "inside information" in the Ordinance)

Those statutory provisions are called "Inside Information Provisions" in the Rules [MB1.01/GEM1.01]

Objective of consequential Rule amendments:

- to enable Exchange to discharge its duty under s 21 SFO to, as far as reasonably practicable, ensure an orderly, informed and fair market for the trading of securities listed on Exchange

[MB2.01/GEM2.01]

What is given statutory backing?

General disclosure obligation under existing MB13.09(1)/GEM17.10	General disclosure obligation under new MB13.09/GEM17.10
<p>Issuer shall keep its members, holders of its listed securities and Exchange informed of information which:</p> <ul style="list-style-type: none">(a) is necessary to enable them and the public to appraise the position of the group; or(b) ... ; or(c) might be reasonably expected materially to affect market activity in and the price of its securities.	<ul style="list-style-type: none">(1)(2) (a) Where an issuer is required to disclose inside information under the Inside Information Provisions, it must also simultaneously announce the information.

Disclosure re: false market to be retained

General disclosure obligation under existing MB13.09(1)/GEM17.10

Issuer shall keep its members, holders of its listed securities and Exchange informed of information which:

- (a) ... ; or
- (b) is necessary to avoid the establishment of a **false market** in its securities; or
- (c)

General disclosure obligation under new MB13.09/GEM17.10

- (1) ... where in the Exchange's view **there is** or **there is likely** to be a **false market** in an issuer's securities, the issuer must, as soon as reasonably practicable after consultation with the Exchange, announce the information necessary to avoid a false market in its securities.
- (2)

Roles of Exchange and SFC

- Exchange has duty under s 21 SFO to ensure, so far as reasonably practicable, an orderly, informed and fair market [MB13.05(1)/GEM17.06(1)]
- To discharge its duty under s21 SFO, Exchange will **monitor the market, make enquiries** when appropriate or necessary, and may **halt trading** under the Listing Rules [MB13.06(3)/GEM17.07(3)]
- Exchange may require issuer to **make announcement** or halt trading where it considers it appropriate to preserve or ensure an orderly, informed and fair market [MB13.06(2)/GEM17.07(2)]

- The Inside Information Provisions impose **statutory obligations on issuers and directors to disclose inside information** as soon as reasonably practicable after the information has come to issuers' knowledge, and **give SFC the responsibility for enforcing those obligations.**
- SFC has issued Guidelines on Disclosure of Inside Information

[MB13.05(2)/GEM17.06(2)]

No overlap between Exchange and SFC

- Exchange will not give guidance on the interpretation or operation of the Provisions or the Guidelines [MB13.05(2)/GEM17.06(2)]
- Where Exchange becomes aware of possible breach of the Provisions, it will refer it to SFC. It will not take disciplinary action under the Rules unless SFC considers it inappropriate to pursue the matter under the Provisions and Exchange considers action under the Rules for a possible breach of the Rules appropriate [MB13.05(3)/GEM17.06(3)]

Case study 1

Day 1 - Issuer published a standard announcement in response to unusual price movement

Day 2 - It published a major transaction announcement

Queries

(1) Did issuer need to disclose inside information on Day 1?

(2) Did issuer need to

- (a) publish information necessary to avoid false market on Day 1 under MB13.09(1)/GEM17.10(1); and
- (b) request a trading halt under MB13.10A/GEM17.11A?

Issuer's obligations

1. Disclosure requested by Exchange case by case

Exchange's enquiry power under new MB13.10/GEM17.11

Exchange may make enquiries of issuer concerning unusual price/trading volume movements, or possible developments of false market

1. Disclosure requested by Exchange case by case

Issuer's disclosure obligations under new MB13.10/GEM17.11

Issuer must respond promptly to Exchange's enquiry, and,

- (1) if Exchange requests, announce the information relevant to the enquiry, to inform the market or to clarify the situation (Clarification Announcement); or

1. Disclosure requested by Exchange case by case

(2) If:

- issuer's directors, **having made such enquiry with respect to issuer as may be reasonable in the circumstances**, are not aware of:
 - any matter or development that is or may be relevant to the unusual trading movement (**1st Confirmation**), or
 - information necessary to avoid a false market (**2nd Confirmation**), or
 - any information which needs to be disclosed under the Inside Information Provisions (**3rd Confirmation**); and
- Exchange requests,

issuer must announce the Confirmations (i.e. **Standard Announcement**).

1. Disclosure requested by Exchange case by case

- Standard Announcement:

“This announcement is made at the request of the Stock Exchange of Hong Kong Limited.

We have noted [the recent increases/decreases in the price [or trading volume] of the [shares/warrants] of the Company] or [We refer to the subject matter of the Exchange’s enquiry].

Having made such enquiry with respect to the Company as is reasonable in the circumstances, we confirm that we are not aware of any reasons for these prices [or volume] movements or of any information which must be announced to avoid a false market in the Company’s securities or of any inside information that needs to be disclosed under Part XIVA of the SFO. [i.e. the 3 Confirmations]

This announcement is made by the order of the Company. The Company’s Board of Directors collectively and individually accepts responsibility for the accuracy of this announcement.”

1. Disclosure requested by Exchange case by case

- “*such enquiry with respect to issuer as may be reasonable in the circumstances*”
 - Issuer should have in place an **adequate and effective internal control system** by which material information concerning it and its business would be **promptly identified, assessed and escalated** to the board for consideration and action from a Rule compliance perspective

1. Disclosure requested by Exchange case by case

Notes

- Issuer does not need to disclose inside information under the Rules if its disclosure is exempt under the Inside Information Provisions
- Exchange may direct a trading halt if announcement it requests cannot be made promptly

[Notes 2&3 to MB13.10/ Notes 2&3 to GEM17.11]

2. Disclosure to avoid false market

New MB13.09(1)/GEM17.10(1)

Where, in Exchange's view, there is or there is likely to be a false market in issuer's securities, issuer must, as soon as reasonably practicable after consultation with Exchange, announce the information necessary to avoid a false market

Note –

Obligation exists whether or not Exchange makes enquiries

3. Disclosure of inside information

New MB13.09(2)(a)/GEM17.10(2)(a)

Issuer required to disclose inside information under the Inside Information Provisions must **simultaneously announce** the information

3. Disclosure of inside information

SFC waiver application/decision [MB13.09(2)(b)/GEM17.10(2)(b)]

Issuer's application to SFC for a waiver of disclosure under the Inside Information Provisions

- Issuer must
 - simultaneously copy Exchange with such application; and
 - promptly copy Exchange with SFC decision

[MB13.09(2)(b)/GEM17.10(2)(b)]

Note:

If disclosure obligation under MB13.09(1)/GEM17.10(1) (i.e. information necessary to avoid false market) has been triggered but issuer is awaiting SFC's decision, it must request trading halt under MB13.10A/GEM17.11A

Trading halt

New MB13.10A/GEM17.11A

Issuer must, as soon as reasonably practicable, apply for a trading halt/suspension if announcement of the following information cannot be made promptly:

- (a) information required to be disclosed under MB13.09/GEM17.10 (i.e. information necessary to avoid false market and inside information); or
- (b) it reasonably believes that there is inside information which must be disclosed under the Inside Information Provisions; or

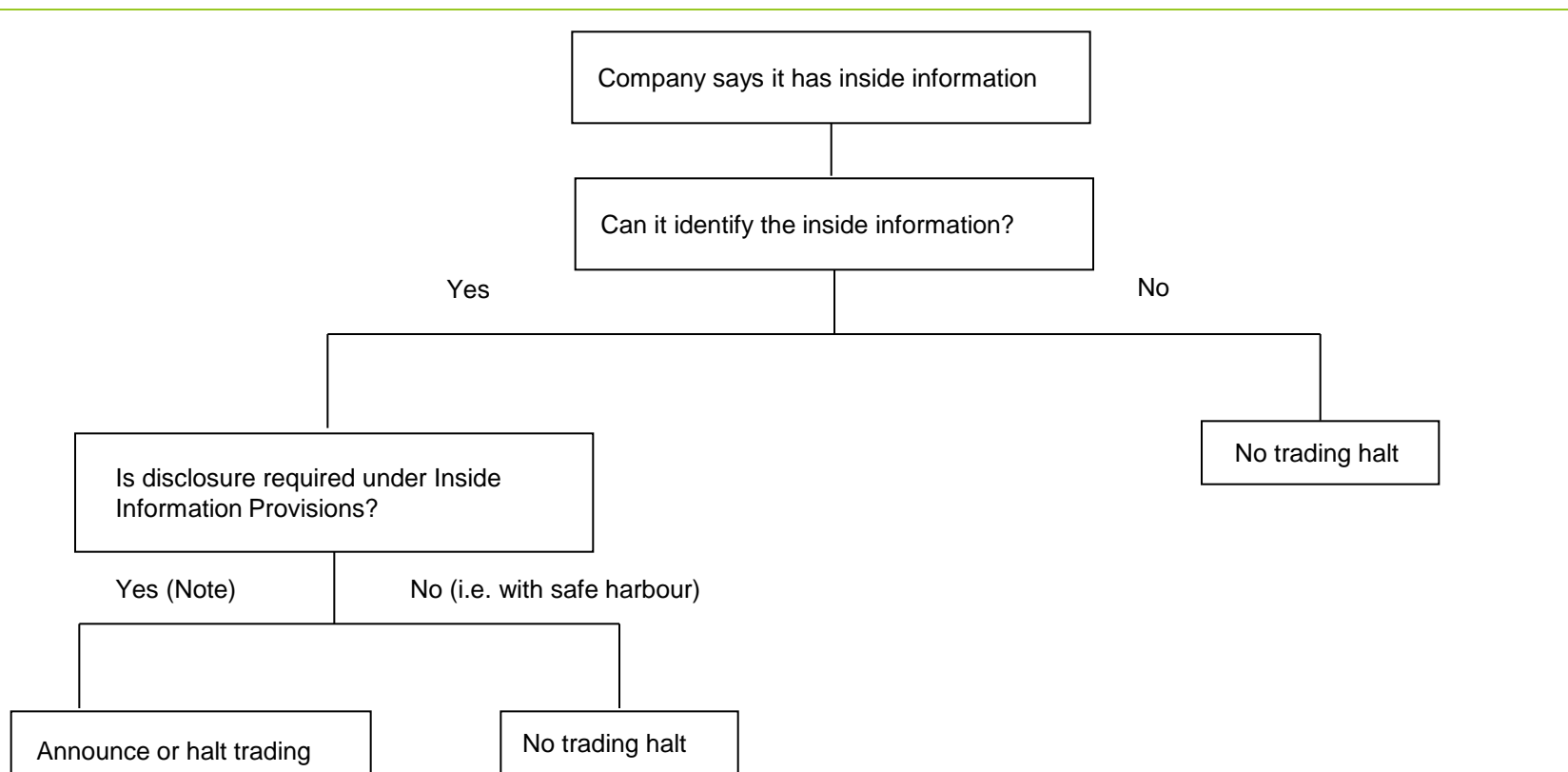
- (c) circumstances exist where it reasonably believes or it is reasonably likely that confidentiality may have been lost in respect of inside information which:
- is the subject of an application to SFC for a waiver; or
 - falls within any of the exceptions to the obligation to disclose inside information under the Inside Information Provisions in section 307D(2) of the SFO

Reminders:

- Recourse to trading halt/suspension should only be made whenever necessary in the interests of all parties
- Issuer publishing an announcement is normally preferable to unwarranted trading halt/suspension
- Application for trading halt/suspension must be supported by specific reasons which issuer wishes Exchange to take into account

[MB6.02/GEM9.03]

Trading halt request



Note: For example, if
(a) no safe harbour applies; or
(b) confidentiality of inside information covered by safe harbour has been lost

Case study 2

Company in final stage of VSA negotiation and confidentiality may have been lost

Company says it has inside information

Can it identify the inside information?

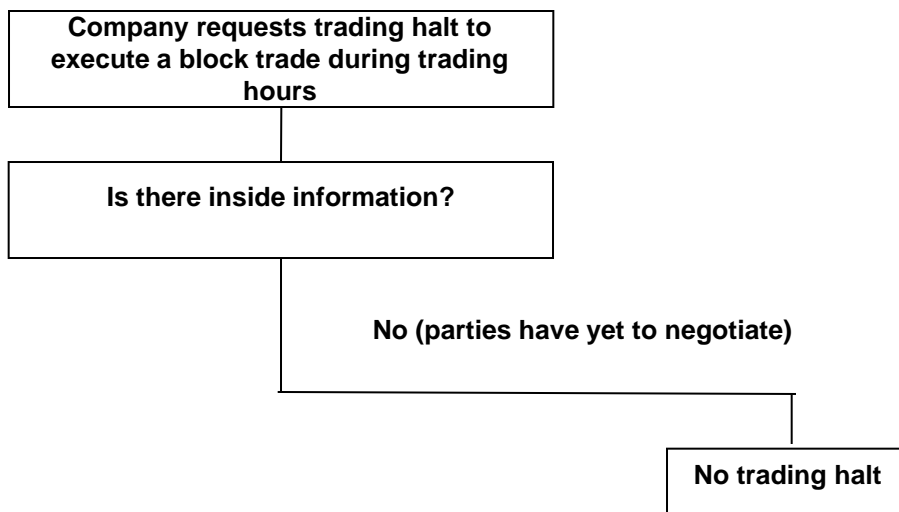
Yes – it is negotiating a VSA

Is disclosure required under Inside Information Provisions?

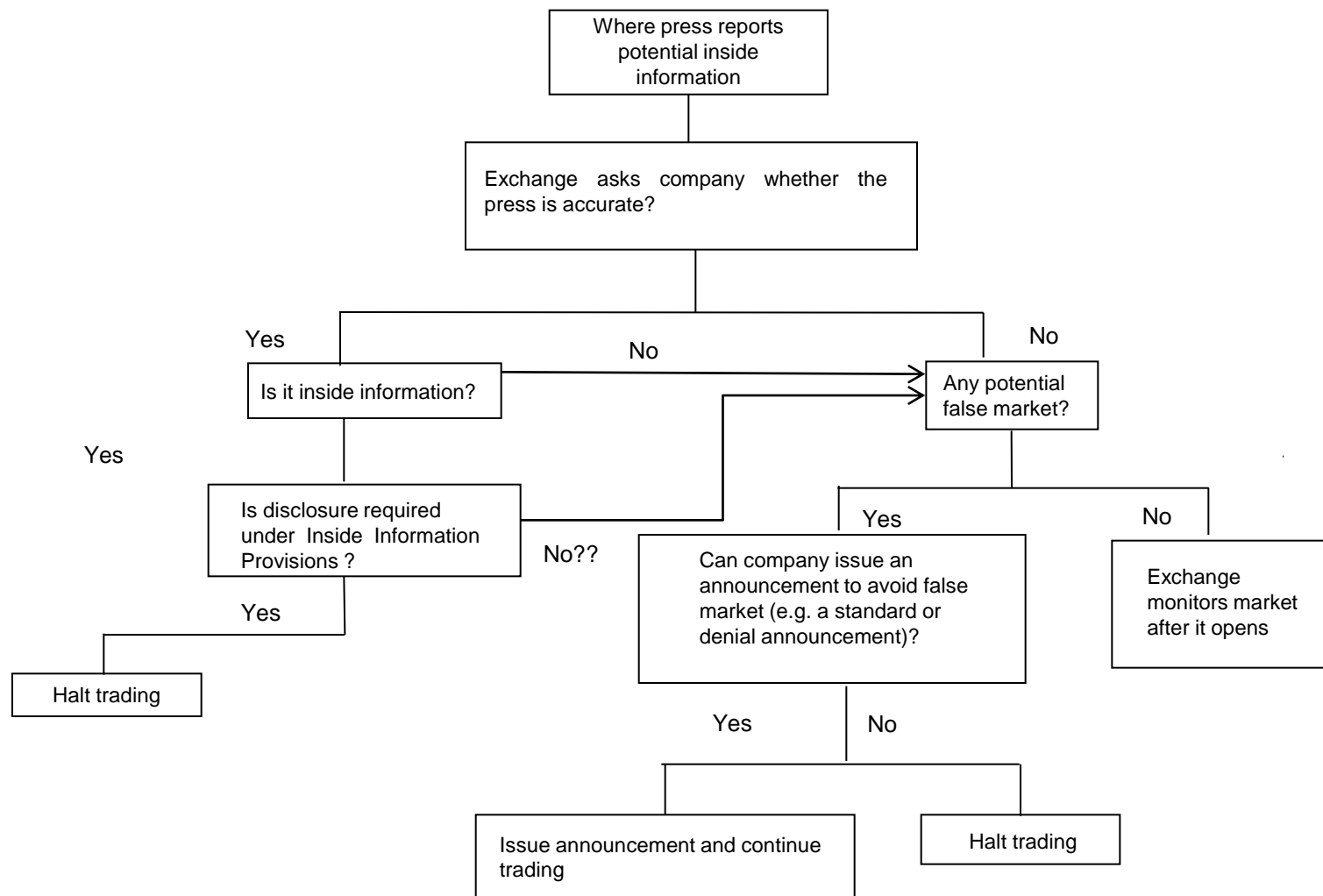
Yes - company is concerned that confidentiality may have been lost (hence no safe harbour)

Announce or halt trading

Block trade

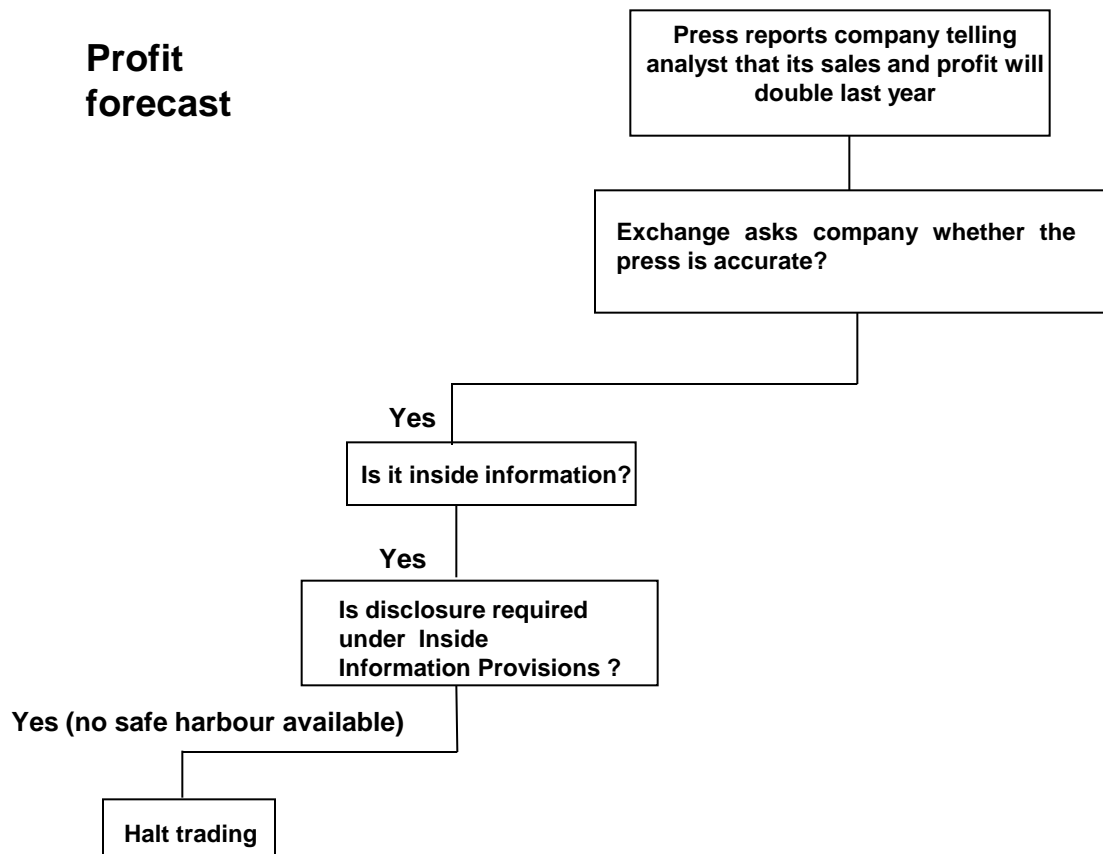


Exchange monitoring – before market opens

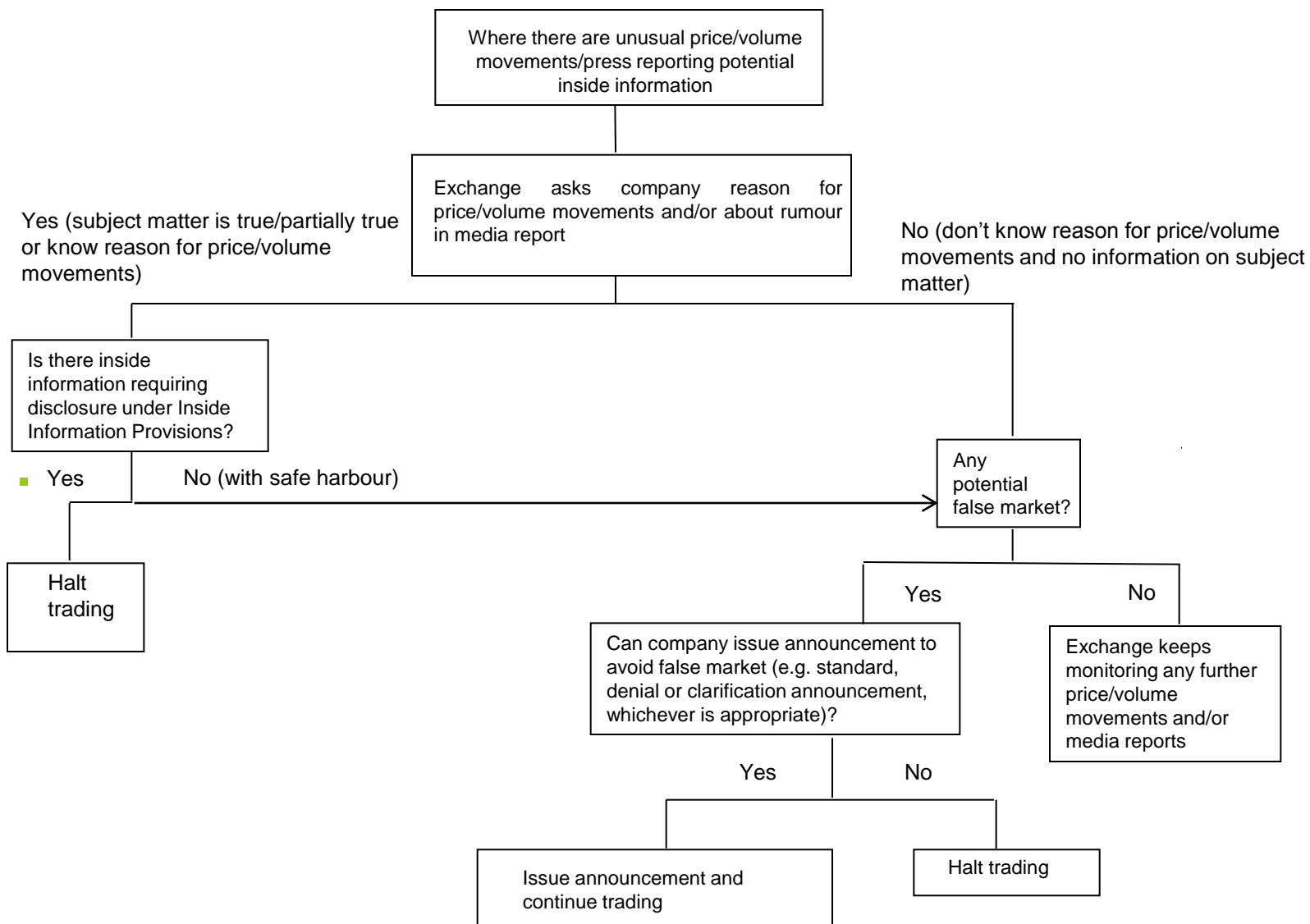


Case study 4

Profit forecast

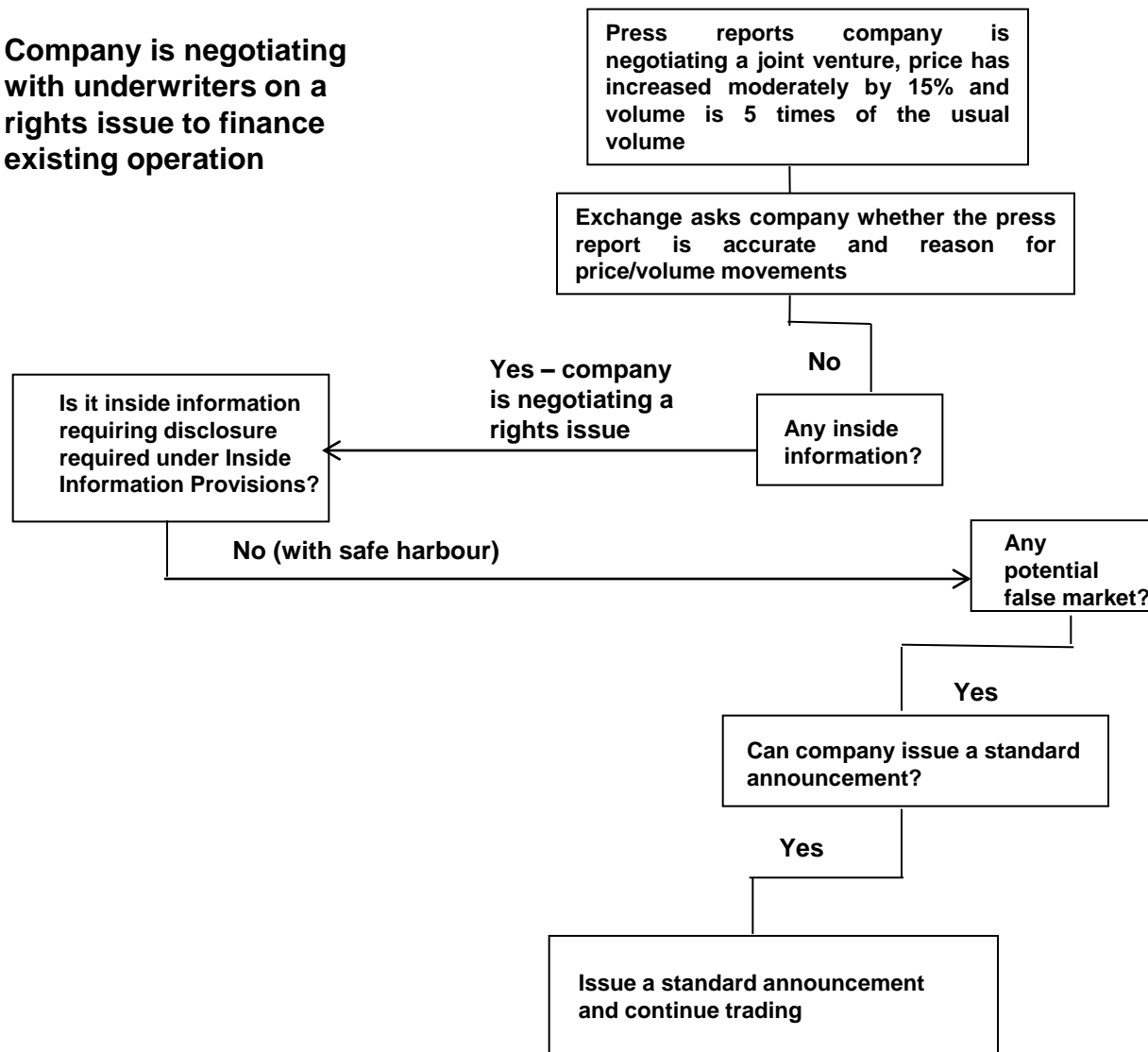


Exchange monitoring – after market opens



Case study 5

Company is negotiating with underwriters on a rights issue to finance existing operation



- Definition:
 - interruption of trading in an issuer's securities requested or directed pending disclosure of information under the Rules and extending for no more than 2 trading days
- Issuer should request trading halt (instead of suspension) if it reasonably expects the trading interruption to last not more than 2 trading days
- Trading halt lasting over two trading days will automatically become trading suspension - no announcement is required for the change

[MB1.01/GEM1.01]

Other specific Rule obligations/amendments

Other specific Rule obligations

- (1) Duty of confidentiality
- (2) Profit forecast
- (3) Spin off application
- (4) Periodic announcements of developments after suspension

Duty of confidentiality

Issuer and its directors must take all reasonable steps to maintain strict confidentiality of inside information until it is announced

Issuer must not (i) divulge any information in such a way as to place in a privileged dealing position any person or class or category of persons; or (ii) release any information in such a way that Exchange transactions may be entered into at prices which do not reflect the latest available information

[MB13.06A, 13.06B (escalated from notes 1&2 to existing MB13.09(1))/GEM17.07A, 17.07B(escalated from notes 1&2 to existing GEM17.10)]

- The term “price sensitive information” is replaced by “inside information” in the Rules
 - Before announcing inside information, issuer must not
 - purchase own shares [MB10.06(2)(e)/GEM13.11(4)]
 - grant options [MB17.05/GEM23.05]
 - Model code [MB appendix 10/GEM appendix 15]

Exchange is guided by published MMT decisions and SFC guidelines when interpreting whether information is “inside information” to enforce these rules

Other consequential Rule amendments

	<u>Existing rule/note</u>	<u>New rule</u>
Announce material change to assumptions of previously published profit forecast	Notes 9&10 to MB13.09(1)/ Note 11 to GEM17.10	MB13.24B/GEM17.26A
Disclosure of spin off applications	MB practice note 15 (para.3(g))/GEM practice note 3 (para. 3(g))	MB practice note 15 (para. 3(g))/GEM practice note 3 (para. 3(g))
Periodic announcements of developments after suspension	MB practice note 17 (para 3.1)	MB13.24A

Thank you