

TOPIC 1 - OVERVIEW

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1. REGULATORY STRUCTURE

1.1 Overall

- The following laws apply to corporate finance activities in Hong Kong:
 - **Securities and Futures Ordinance (SFO)**
 - **Companies Ordinance (CO)**: came into force on 3 March 2014, covering all areas regulated under the previous Companies Ordinance, except the prospectus regime and winding-up insolvency provisions
 - **Companies (Winding Up and Miscellaneous Provisions) Ordinance**: the remainder of the previous ordinance covering the prospectus regime and winding-up insolvency provisions
- The following regulatory rules and codes apply to corporate finance activities in Hong Kong:
 - Issued by the **Stock Exchange of Hong Kong Limited (SEHK)**:
 - Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (**Main Board Listing Rules** or MBLR)
 - Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (**GEM Listing Rules** or GLR)
 - Issued by the **Securities and Futures Commission (SFC)**:
 - Code on Takeovers and Mergers (Takeovers Code)
 - Code on Share Buy-backs
 - Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission
 - Corporate Finance Adviser Code of Conduct (CFA Code)
- Advising on Corporate Finance is a Type 6 regulated activity:

1.2 Role of the Securities and Futures Commission (SFC)

1.2.1 Regulatory Objectives of the SFC

- As stated in the SFO, **the objectives of the SFC**, in relation to the securities and futures industry, are:
 - Maintain and promote the fairness, efficiency, competitiveness, transparency and orderliness of the industry
 - Promote understanding by the public of financial services including the operation and functioning of the industry
 - Provide protection to the investing public
 - Minimize crime and misconduct in the industry
 - Reduce systemic risks in the industry
 - Assist the financial secretary in maintaining the financial stability of Hong Kong by taking appropriate steps in relation to the industry

1.2.2 Functions and Powers of the SFC

- The functions and powers of the SFC are wide and set out in the SFO. The **principal functions** are to:
 - Take such steps as it considers appropriate to meet the first objective above
 - Supervise, monitor and regulate the activities of:
 - (i) recognised exchange clearing houses, exchange controllers and investor compensation companies or persons carrying on regulated activities; and
 - (ii) the activities of registered institutions that are regulated or to be regulated by the SFC under any relevant provisions
 - Promote, encourage and enforce the proper conduct, competence and integrity of persons carrying on regulated activities
 - Maintain and promote confidence in the industry
 - Cooperate with and provide assistance to other regulators
 - Secure appropriate degree of protection for the investing public
 - Promote, encourage and enforce internal control and risk management systems by persons carrying on regulated activities, including registered institutions in the case of any regulated activities they conduct
 - Suppress illegal, dishonourable and improper practices in the industry

1.2.3 Functions of the SFC's Operational Units

Five divisions, two departments. Here they are.

- **Corporate Finance Division** (important for Paper 5):
 - Vets listing applications together with the SEHK
 - Monitors listed companies' announcements to identify misconduct or irregularities
 - Administers the Codes on Takeovers and Mergers and Share Buy-backs
 - Supervises listing-related activities of Stock Exchange (SE administers listing process)
 - Reviews and recommends changes to Listing Rules
 - Reviews and authorises prospectuses and marketing materials for unlisted issuers for unlisted shares or debentures
 - Intervenes at an early stage in serious cases of suspected misconduct in listing applications and corporate transactions by the powers under the Securities and Futures (Stock Market Listing) Rules

- **Enforcement Division:**
 - Monitors the trading of Hong Kong's stock and derivative markets and enquires into irregularities
 - Investigates market misconduct and disciplines/prosecutes those responsible, including those that may be unlicensed
 - Inspects books and records of listed companies where impropriety is suspected which may involve directors, officers or substantial shareholders
 - Cooperates with domestic and overseas law enforcement agencies and regulatory bodies in investigations, if required
- **Investment Products Division:**
 - Develops regulatory platforms, including those for authorization applications of investment products, so as to facilitate market growth and product innovation
 - Regulates and approves investment products that are offered to the public and subject to the SFO
- **Supervision of Markets Division:**
 - Supervises conduct, operation and internal systems of the exchanges and clearing houses
 - Strengthens market infrastructure
 - Authorizes automated trading service providers
 - Regulates approved share registers
 - Supervises and monitors activities of the Investor Compensation Company
 - Ensures that markets are operated efficiently and that risk is minimized for market participants and for the image of Hong Kong as a financial centre
- **Intermediaries Division:**
 - Licensing department
 - Intermediaries Supervision Department
- **Licensing Department:**
 - Licenses corporations and individuals to enable them to carry out SFC-regulated activities
 - Issues codes and guidelines concerning the competence and suitability of corporations and individuals to remain licensed
 - Reviews continuing suitability of licensed corporations and individuals to be licensed
- **Intermediaries Supervision Department:**
 - Supervises the business conduct of licensed corporations and individual licensees on an ongoing basis by conducting on-site inspection and off-site monitoring, and monitors the financial integrity of licensed corporations

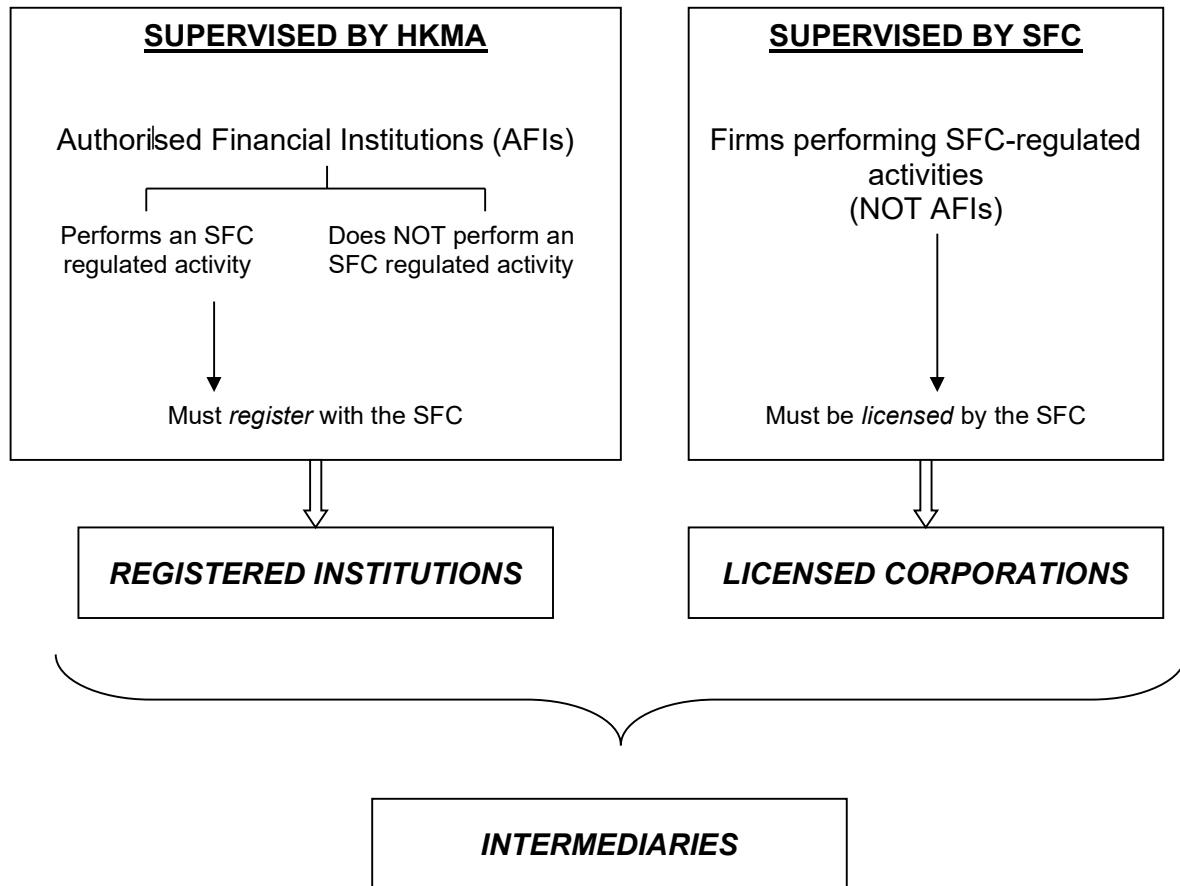
1.2.4 Committees, Tribunals and Panels

- **Examples of regulatory committees** established by the SFC to which it has delegated some of its functions, and relevant to Paper 5, are:
 - **Takeovers and Mergers Panel**
 - Hears disciplinary matters in the first instance
 - Reviews rulings by the Executive Director of the Corporate Finance Division at the request of a dissatisfied party
 - Hears matters referred to it by the Executive
 - **Takeovers Appeal Committee**
 - Reviews disciplinary rulings of the Panel
- **The following tribunals are independent** of the SFC:
 - **Securities and Futures Appeals Tribunal** – statutory body with full-time members headed by a judge appointed by the Chief Executive to hear appeals against decisions made by the SFC
 - **Market Misconduct Tribunal** – see below for further details

1.3 Role of the Hong Kong Monetary Authority (HKMA)

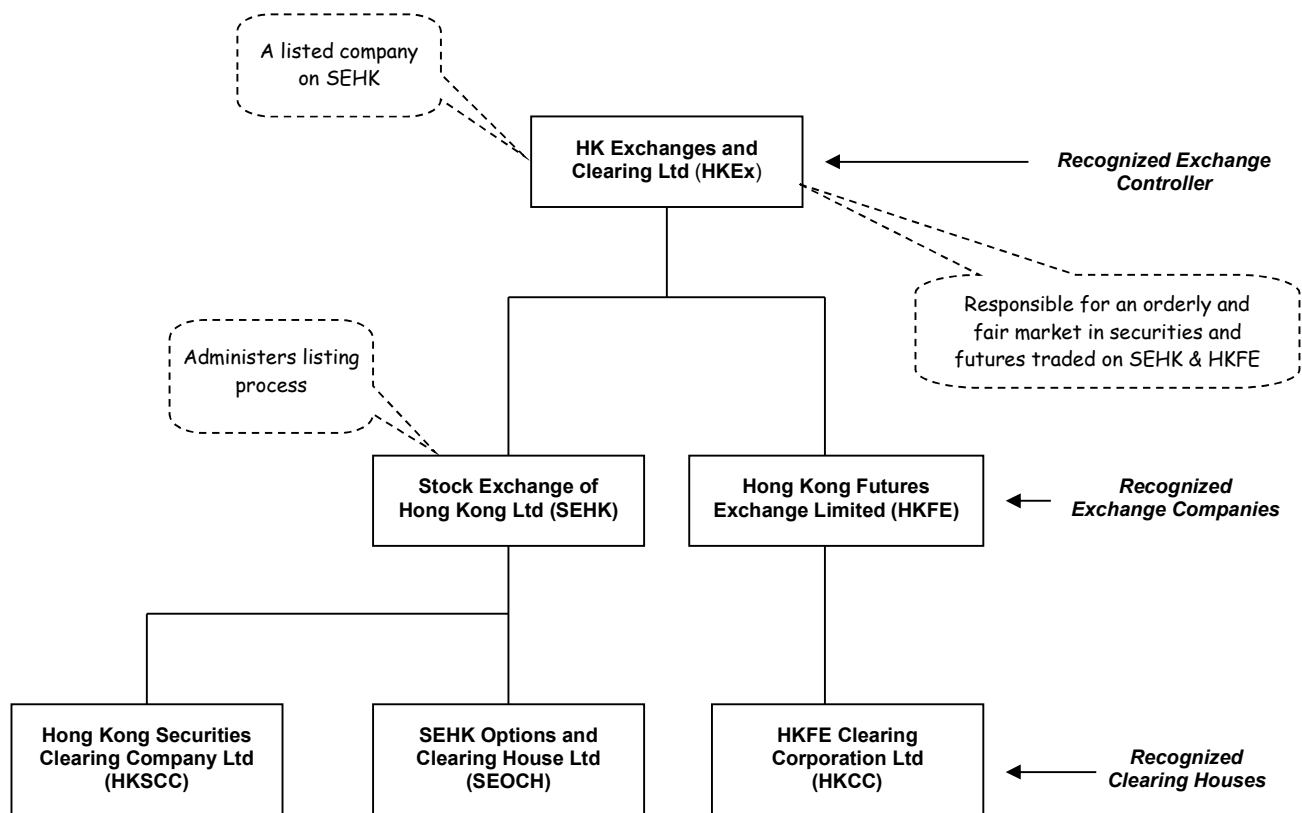
- Headed by a Chief Executive with several deputies
 - Manages the Exchange Fund
 - Manages Hong Kong's monetary policy
 - Required to maintain currency stability
 - Ensures the safety and stability of the banking system
 - Promotes the efficiency, integrity and development of the financial system
 - Supervises the banking system
- ↳
- Under the SFO and the Banking Ordinance, **Authorized Financial Institutions (AFI's)**, which are regulated by the HKMA and include banks, have to be registered with SFC as **registered institutions** if they wish to carry out an SFC-regulated activity, including corporate finance advising
 - HKMA is frontline regulator of AFIs and takes the leading role in vetting applications for registration with the SFC and in supervising their SFC-regulated activities, including on-site inspection
 - HKMA applies all SFC criteria in supervising AFIs registered with the SFC
 - AFIs are regulated by the HKMA under the Banking Ordinance, and those carrying out SFC regulated activities (including Corporate Finance) are also regulated by the SFC. Therefore, such AFIs are **regulated by both the HKMA and the SFC**

Supervision of Intermediaries – Registered or Licensed?



1.4 Role of Hong Kong Exchanges and Clearing Limited (HKEx)

- Responsible for an orderly and fair market in securities and futures traded on SEHK & HKFE
- SEHK is responsible for the listing of securities both on the Main Board and on the GEM
- SEHK is responsible for receiving notifications and disseminating information about changes in the shareholdings of directors, chief executives and substantial shareholders of listed companies
- According to the Listing Rules, “*substantial shareholder*” refers to a person who holds 10% or more of the voting power at any company general meeting
- See diagram below. Missing is OTC Clearing Hong Kong Limited



1.5 Role of Registrar of Companies

- Administers and enforces certain aspects of the: Companies Ordinance, Companies (Winding Up and Miscellaneous Provisions) Ordinance; Limited Partnerships Ordinance, Trustee Ordinance, Registered Trustees Incorporation Ordinance and Money Lenders Ordinance
- Maintains and makes available for public inspection financial and other returns made by companies
- May strike off companies for failure to make returns or for not carrying on business
- **Does not directly regulate companies**, but takes an active interest in corporate governance issues and may make recommendations
- No direct link between SFC and Companies Registry
- Responsible for **the registration of prospectuses** under the Companies Ordinance

1.6 Relationships Among Legislation, Codes, Listing Rules etc

- SFO and CO provide the legal framework for securities and futures markets in Hong Kong
- SFC is empowered by the SFO to make subsidiary legislation in relation to specified matters
- Subsidiary legislation has the force of law and can be enforced through the courts
- SFO also empowers the SFC to issue codes and guidelines, however they do not have the force of law
- The Listing Rules do not have the force of law – they operate on a contractual basis between the SEHK and the issuer and its related parties

2. CORPORATE GOVERNANCE

- Hong Kong listed companies are required to comply with the Corporate Governance Code and Corporate Governance Report, as per the MBLR and the GLR

2.1 Principles of Good Governance

- The Corporate Governance Code gives SEHK's views on the **principles of good corporate governance**, covering:
 - Directors
 - Remuneration of directors and senior management and board evaluation
 - Accountability and audit
 - Delegation by the board
 - Communication with shareholders
 - Company secretary
- Where an issuer deviates from any of the code provisions, considered reasons must be given in interim and annual reports
- **Important code provisions** include:
 - Regular board meetings should be held, at least four times per year approximately quarterly
 - Any material conflict of interest should be dealt with at a board meeting in the presence of independent non-executive directors
 - Roles of Chairman and Chief Executive should be conducted by different people
 - An explanation should be given to shareholders as to how a proposed new INED with 7 or more listed company directorships will be able to devote sufficient time to the board
 - Newly appointed directors should receive comprehensive, formal and tailored inductions
 - Remuneration committee should consult Chairman/CE about remuneration proposals for executive directors
 - Effectiveness of internal controls should be reviewed annually by directors and reported to shareholders in the Corporate Governance Report
 - Full minutes of audit committee meetings should be kept

2.2 Corporate Governance Report

- Issuers must include a Corporate Governance Report in their interim and annual reports
- Reasons for any deviation from the Code should be given in the Report

2.3 Environmental, Social and Governance Reporting Guide (ESG)

- The ESG Guide sets out “comply or explain” provisions that allow flexibility to issuers along with mandatory disclosure requirements
- ESG reflects developments internationally including Mainland China, UK, US, Singapore and Australia
- Two subjects that need to be reported on:
 - Environmental**
 - Emissions
 - Use of resources
 - Policies on minimising environmental and natural resources
 - Climate change
 - Social**
 - Labour issues, including employment laws, health and safety and development and training
 - Supply chain management
 - Product responsibility
 - Anti-corruption measures
 - Community engagement
- Issuer will need to report ESG information on both the issuer’s website and the HKEx’s website. It may also choose to report the information in its annual report
- Where the issuer elects not to include the ESG report in the annual report, it is encouraged to publish the ESG report at the same time as the publication of the annual report
- The issuer should publish the ESG report within five months of the relevant financial year end and inform any intended recipient of how to access the report on its website
- The information reported should be based around four reporting principles:
 - Based on the materiality of the issue to investors and other stakeholders
 - Based on quantitative assessment of the KPIs
 - Presents a balanced and unbiased picture of the issuer’s performance
 - Use of consistent methodologies to facilitate meaningful comparisons over time
- Issuer may also consider whether to obtain independent assurance to strengthen the credibility of the disclosed ESG information

3. RELEVANT LAWS

- The two principal pieces of legislation concerning corporate finance advisers in Hong Kong are the **SFO** and the **CO**
- Important aspects of the **SFO** to be considered are:
 - Activities constituting the regulated activity of **corporate finance advising**
 - Regulation of **public offers of investments**
 - Types of **market misconduct**
 - **Disclosures of interest** in the voting capital of a listed issuer
 - Disclosure of **inside information**

3.1 Securities and Futures Ordinance

3.1.1 Advising on Corporate Finance

- Advising on corporate finance, as a Type 6 regulated activity, **means giving advice**:
 - On compliance with the Listing Rules
 - On compliance with the Takeovers Code or Share Buy-backs Code
 - On disposing or acquiring securities from the public
 - To a listed corporation/public company on corporate restructuring in respect of securities
- The following activities are **excluded from the definition** of “advising on corporate finance”:
 - **Professional accountants, solicitors, counsel and trust companies** giving corporate finance advice wholly incidental to their profession
 - A person **licensed/registered for Type 1** regulated activity gives corporate finance advice wholly incidental to dealing in securities
 - Corporate finance advice is given in **publicly available printed media/radio broadcast/television broadcast**
 - Corporations giving corporate finance advice solely for their **wholly owned subsidiaries**, holding companies holding all their issued shares or other wholly owned subsidiaries of the holding company
- A **responsible officer** is a licensed representative who:
 - Actively participates in or supervises a regulated activity;
 - Is nominated by the licensed corporation; and
 - Is approved by the SFC

- Although the SFO does not provide a **definition of responsible officer**, the SFC has stated:
 - **Every executive director*** of a licensed corporation is required to obtain the approval of the SFC as a responsible officer; and
 - Every licensed corporation must have, for each regulated activity for which it is licensed, **at least two responsible officers** approved by the SFC – at least one of them must be an executive director
- * *A director who actively participates in, or is responsible for directly supervising, the business of a regulated activity for which the corporation is licensed (s113, SFO)*
- For **registered institutions**: the Banking Ordinance requires at least **two executive officers** to be responsible for supervising regulated activities – at least one to be available at all times

3.1.2 Offers of Investments

- It is an offence under the SFO to issue **advertisements, invitations or documents** relating to investments in certain situations unless the issue is authorized by the SFC – offers by prospectus are exempt
- Corporate finance advisers should not issue false statements to the SFC or SEHK. Doing so, knowingly or recklessly, is an offence

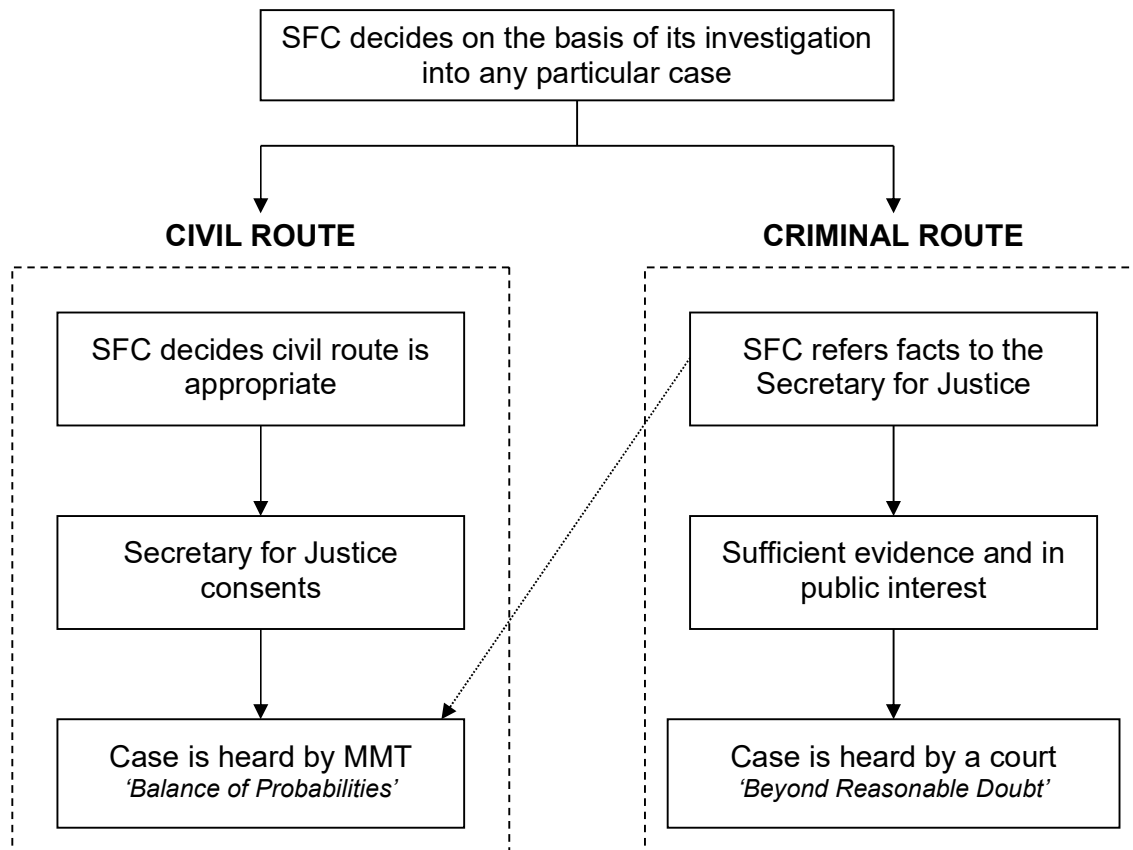
3.1.3 Market Misconduct

- There are six categories of market misconduct:

- Insider dealing
- False trading
- Price rigging
- Disclosure of information about prohibited transactions
- Disclosure of false or misleading information inducing transactions
- Stock market manipulation

- Legal proceedings against the accused can be **criminal** in the courts or **civil** under the Market Misconduct Tribunal (MMT), but not both

Criminal or Civil?



- The SFC has the power to prosecute minor cases summarily in a magistrate's court
- The MMT is chaired by a judge with 2 other members who cannot be public officers. **All 3 are appointed by the Chief Executive** of HKSAR
- Can compel and receive evidence relevant to hearings
- A '**balance of probabilities**' standard of proof is applied
- At the conclusion of proceedings, the **MMT will issue a public report** giving details of the market misconduct and the disciplinary orders handed out
- **Appeals** against MMT findings can be made to the Court of Appeal
- The MMT is subject to **judicial review**

- Orders that may be made by MMT against those found to have committed market misconduct include:
 - **disqualification** for up to 5 years from holding office as director, liquidator, receiver or taking part in the management of a corporation;
 - **prohibition on investing** or trading in HK markets for up to 5 years (cold shoulder order);
 - **prohibition of further market misconduct** as specified in the order;
 - **payment of profits made or loss avoided**, plus compound interest, to the Government;
 - **payment of reasonable costs** incurred by the Government and the SFC; and
 - **disciplinary referral orders** recommending that a professional body of which the person is a member should take disciplinary action against him

Insider Dealing

Dealing

- A person dealing in Hong Kong listed securities of a corporation or its related corporation or their derivatives where the person:
 - Is **connected with the listed corporation** and knowingly has **inside information** in relation to the listed corporation; or
 - Is contemplating making a **take-over offer** for the listed corporation, which is known to the person as inside information in relation to the listed corporation
 - Has received such information which he knows is inside information directly or indirectly **from a person known to be connected** with the listed corporation

Tipping-off

- A person **connected** with a listed corporation disclosing **inside information** or **knowledge of a take-over offer** to another person knowing that the other person will make use of that information for dealing/counseling/procuring:

Inside Information

- Specific information in relation to a corporation:
 - Which is **not generally known** to persons who deal in its listed securities; but
 - If such information was known to them, it would be likely to **affect the security price** (ie price sensitive information)

Connected Persons

- A person connected with the corporation includes:
 - Directors/employees/substantial shareholders (at least 5% of total number of shares)
 - Professionals who have a business relationship with the corporation (eg auditors)
 - Connected person of another corporation and the inside information relates to transactions between the two corporations
- There a number of possible defences against a charge of insider dealing per the SFO, including:
 - **Chinese wall** – an institution has both relevant information and trades the relevant securities, but the persons trading are not those possessing the inside information
 - The purpose of the insider dealing was **not for the purpose of making a profit** or avoiding a loss
 - The dealing was a **market contract**
 - Dealing where the other party to the dealing knows or should know **the person dealing is a connected person**
 - **Exercising an existing right**, where the right was acquired prior to becoming aware of the inside information

Disclosure of False or Misleading Information Inducing Transactions

- If someone:
 - who is **party to a prohibited transaction**, or has received a benefit from such an act
 - **discloses, circulates or disseminates information** about the transaction, and its effect on prices of securities or futures contracts
 - he will have engaged in market misconduct
- Can be committed by both an issuer and a corporate finance adviser (CFA)
- Important that a CFA verifies all information before its release

Stock Market Manipulation

- Stock market manipulation occurs when a person wishes to influence the investment decisions of other persons by:
 - Entering into two or more transactions which have the effect of increasing/reducing/maintaining/stabilizing the price of securities
 - Safe harbour rules apply (Price Stabilising) – see Topic 2

3.1.4 Disclosure of Interests

- Reflects modern trend towards greater disclosure and transparency
- **Two basic rules** concerning the duty to disclose interests in the relevant share capital of a listed company:
 - Directors and chief executives are required to disclose all interests
 - Other persons must make disclosures once their interests in the relevant share capital reach 5%
- **'Interest in relevant share capital'** is widely defined to include:
 - Both long and short positions, without any netting
 - Interests in equity derivatives
 - Attributed interests, including trust arrangements, corporate shareholdings and family arrangements
- Persons subject to disclosure requirements are **required to make disclosures when**:
 - Having reached (and reported) the 5% disclosure level, their holdings rise or fall through a whole percentage level
 - The level of interest falls below 5%
 - The nature of their interest changes (eg acquiring shares on the exercise of a call option)
- Disclosure must be made:
 - To the listed company
 - To the exchange on which the company is listed
 - Within 3 business days after the relevant date

3.1.5 Disclosure of Inside Information

Duty of Disclosure

- A relatively new development, effective from 1 January 2013
- Gives statutory backing to disclosure obligations imposed by the Listing Rules of the SEHK
- Listed companies have an **obligation to disclose inside information**¹ to the public as soon as reasonably practicable after the information has come to their attention

¹ See Topic 9 for definition of Inside Information

Exception to Disclosure Requirement

- A listed corporation is not required to disclose inside information in the following situations:
 - Disclosure is prohibited by an enactment or a court order
 - Confidentiality of the information is preserved, and
 - Information concerns an incomplete proposal/negotiation
 - Information is a trade secret; or
 - SFC grants a waiver

Breach of Disclosure Requirement

- An officer of a listed corporation, which is in breach of the disclosure requirement, will be liable if:
 - Breach is caused by his intentional, reckless or negligent conduct; or
 - Reasonable measures to prevent the breach have not been taken
- The listed corporation and/or its directors may be subject to a civil liability of a fine up to HK\$8 million and/or other sanctions

Guidelines on Disclosure of Inside Information

- SFC Guidelines to assist corporations with their obligations to disclose inside information. They do not have the force of law

3.2 Companies Ordinance (CO) and Companies (Winding Up and Miscellaneous Provisions) (CWUMPO)

- Corporate finance advisers need to consider CWUMPO requirements regarding company **prospectuses** when offering shares and debentures to the public
- Shares or debentures regarded as “**structured products**” (as per SFO) may not be offered to the public under the CWUMPO prospectus regime. They must either be SFC authorized or listed on the SEHK
- **SFC functions** listed in the CWUMPO have been transferred to SEHK
- **SFC retains the power** to issue a certificate of exemption from compliance with the CWUMPO prospectus requirements
- **SEHK vets every prospectus** and has the power (from CWUMPO) to authorize registration by the **Registrar of Companies**
- **SEHK reviews a prospectus** for compliance with MBLR and relevant provisions of the CWUMPO
- Once the SEHK is satisfied that a prospectus complies with MBLR, the **prospectus will be authorized for registration** and a certificate will be issued. It is the issuer’s responsibility to then **deliver the prospectus to the Companies Registry** for registration
- A certificate of authorization from SEHK is not confirmation that the prospectus complies with the CWUMPO

4. RELEVANT REGULATIONS

- In addition to the legislation covered in the previous section, corporate finance advisers (CFA) are also regulated by the Listing Rules, the Takeovers Code and the Share Buy-backs Code (the Three Codes)
- The SFC will regard any breach of the Three Codes as casting doubt on the fitness and properness of a CFA

4.1 Corporate Finance Adviser Code of Conduct

- The CFA Code covers all licensed/registered corporate finance advisers and sets out requirements governing their conduct
- Any breach may affect fitness and properness
- The CFA Code covers the following:

Conduct of Business

- Directors and representatives of a corporate finance adviser conducting Type 6 regulated activities should be properly licensed/registered
- A corporate finance adviser should maintain an effective compliance function headed by a designated compliance officer
- A licensed corporation's senior management include persons who are managers-in-charge of core functions (MICs) and who are responsible for any of the following functions:
 - Overall management oversight
 - Key business line
 - Operational control and review
 - Risk management
 - Finance and accounting
 - Information technology
 - Compliance
 - Anti-money laundering and counter-terrorist financing

Competence

- A CFA should be honest, of good repute and character and should maintain a high standard of integrity and fair dealing
- Where appropriate, a CFA should seek proper professional advice in respect of compliance with applicable laws and regulations

Conflicts of Interest

- A Corporate Finance Adviser should withdraw from, or not take on, a mandate where there is an **irresolvable conflict of interest** with its client
- When a Corporate Finance Adviser is part of a group conducting other activities, it should ensure that there is an effective system of functional barriers (**Chinese wall**) to prevent leakage of confidential/price-sensitive information
- Any giving or receiving of **gifts** should be disclosed – there should be written policies and procedures regarding gifts
- A Corporate Finance Adviser acting as a Sponsor should ensure that, in giving a view on the suitability of an issuer for listing, it can provide **impartial advice** to its client

Standard of Work

- A Corporate Finance Adviser is encouraged to **record the terms of its engagement** in writing with the client
- When a Corporate Finance Adviser depends upon **the work of experts** and other professionals, he should check on the experience of the experts
- Where a Corporate Finance Adviser **acts as a financial adviser to a listing applicant**, the adviser should co-operate fully with the listing sponsor for an equity listing, all material information disclosed to analysts must appear in the prospectus or listing document

Duties to Client

- A Corporate Finance Adviser should use all reasonable efforts to ensure that its client understands the relevant regulations and should **ask the client** to report any non-compliance to the regulators. If the client refuses, the Adviser should **consider** declining to act and should cooperate with the regulator

Communication with Regulators

- Where a regulatory issue arises on a transaction, corporate finance advisers are encouraged to consult with the regulators at an early stage to seek guidance

Personal Account Dealings

- As with Fund Managers, all personal account dealings of **relevant persons** should be monitored by the designated compliance officer
- **Relevant persons** are employees/directors of a corporate finance adviser who are likely to have access to confidential information
- A **watch list** and a **restricted list** system should be maintained for the proper monitoring of personal account dealings and proprietary trading
- A corporate finance adviser must have a **written policy** specifying whether or not relevant persons can deal or trade for their own accounts and if they can, the policy must specify the following:
 - the conditions on which relevant persons may deal or trade;
 - that relevant persons should generally be required to deal through their principal or its affiliates;
 - duplicate trade confirmations should be provided to senior management if relevant persons are permitted to deal through another dealer;
 - that employees should identify all related accounts (including amounts of their minor children and those in which the employees hold beneficial interests) and report them to senior management;
 - such transactions are reported to the designated compliance officer; and
 - the designated compliance officer should actively monitor the accounts of relevant persons and should not have any beneficial interest in the transactions/accounts monitored

4.2 Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited

- Rules covering various aspects of the SEHK functions:
 - SEHK participation
 - SEHK trading
 - Clearing house participation
 - Listing on SEHK
- SEHK's principal function is to **provide a fair, orderly and efficient market for the trading of securities**
- The **Main Board and GEM Listing Rules** are intended to ensure:
 - the suitability of applicants for listing;
 - the fair and orderly issue and marketing of securities;
 - the provision of sufficient, material and timely information by issuers which might concern the investors and the public and affect the prices of listed securities;
 - the fair and equal treatment of shareholders;

- that the directors act in the interests of the shareholders as a whole, particularly where the public shareholders are a minority; and
- that all new issues are first issued to existing equity shareholders as rights issues unless they agree otherwise
- Both new applicants and listed issuers are encouraged to seek informal and confidential guidance from the SEHK
- Listing Rules are approved by the SFC and covered in detail in Topic 2

4.3 Code on Takeovers and Mergers and Code on Share Buy-backs

- The Codes have been issued by the SFC, in consultation with the Panel, and **aim to ensure**:
 - equal treatment of shareholders
 - full and prompt disclosure of information by persons concerned with offers
 - there is a fair and informed market in the shares of companies affected
 - an orderly framework for takeover/merger/buy-back activity
- The Codes represent a **consensus of opinion** and do not have the force of law, however Listing Rules require compliance with the Codes
- The Codes **apply to**:
 - Company directors
 - Management companies and trustees of REITs
 - Persons seeking to gain/consolidate control of companies
 - Professional advisers
- **Financial/professional advisers** must have the competence, professional expertise and adequate resources to discharge their responsibilities under the Codes
- Codes are not concerned with the **financial merits of a merger/takeover**, which are matters for of the company and its shareholders
- Codes apply to public companies in Hong Kong and companies/REITs with a primary listing in Hong Kong
- To determine **whether a company is a public company in Hong Kong**, the following circumstances will be considered:
 - Number of Hong Kong shareholders
 - Extent of share trading in Hong Kong
 - Location of head office and place of central management
 - Location of business and assets, including registration under companies legislation and tax status
 - Protection for Hong Kong shareholders under statutes/codes
- Codes covered in detail in **Topic 3**

4.4 SFC Codes and Guidelines

- Corporate finance advisers should be aware of other codes and guidelines issued by the SFC, specifically:
 - Code of Conduct for Persons Licensed by or Registered with the SFC
 - Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC
- Para 17 of the Code of Conduct specifies the following requirements for **sponsors**:
 - Provide advice and guidance to a listing applicant
 - Complete all reasonable due diligence on a listing applicant
 - Ensure that public disclosures about a listing applicant are true, accurate and complete
 - Ensure truthful, cooperative and prompt communication with regulators
 - Keep proper books and records to show compliance with Code of Conduct
 - Ensure proper implementation and oversight of sponsor work through sufficient resources and effective systems
 - Ensure that public offers are conducted in a fair and orderly manner
 - Take steps to ensure that analysts do not receive material information that is not disclosed in the listing document
- Internal control guidelines cover: management and supervision, segregation of duties and functions, personnel and training, information management, compliance, audit, operational controls and risk management

4.5 Enforcement Actions

- When exercising powers of enforcement, SFC's primary concerns are to:
 - Protect investors
 - Maintain market integrity and confidence
 - Hold wrongdoers accountable for their actions
- SFC's enforcement process involves three steps:
 1. Identify suspected breaches
 2. Investigate breaches
 3. Take steps to protect investors and punish wrongdoers appropriately
- **SEHK** may require issuers to appoint compliance advisers for advice on Listing Rules compliance matters or for performing internal control reviews. Directors may have to undergo training on the Listing Rules and directors' duties
- HKEx and the SFC may, at times, alert the market and public to areas of particular concern – in December 2016, **rights issues and open offers were closely scrutinised** to monitor the effects of substantial dilution of non-subscribing minority shareholders
- Corporate finance advisers should keep abreast of latest developments in the market to ensure that they can give appropriate advice

5. CHARACTER OF THE HONG KONG INITIAL PUBLIC OFFERING MARKET

5.1 Introduction

- The Hong Kong market has evolved significantly since:
 - Establishment of the SFC in 1989
 - Resumption of sovereignty over Hong Kong in 1997
 - Demutualisation of the stock exchange in 2000
- The Hong Kong market has developed from a small regional market to one of the largest exchanges in the world in terms of market capitalisation and funds raised through IPOs

5.2 Growing Links with the People's Republic of China

- Traditionally, the Hong Kong market was dominated by family-controlled businesses, however it is increasingly dominated by Mainland businesses and is now dominated by both family and state controlled public companies
- The Stock Connect programme has further bolstered the connection between the Hong Kong and mainland markets
- Connections between Hong Kong and Mainland markets continue to develop, a recent example being the Bond Connect pilot scheme allowing international investors access to bond trading on the China Foreign Exchange Trade System

5.3 Companies Incorporated in Offshore Jurisdictions

- Jurisdictions accepted for listing in Hong Kong have expanded to over 25, while the most popular remain Hong Kong, the PRC, the Cayman Islands and Bermuda
- Popular jurisdictions for incorporation of offshore listed companies are the Cayman Islands and Bermuda
- SEHK ensures that overseas companies listed in Hong Kong have appropriate standards of shareholder protection, at least equivalent to those under Hong Kong law
- To keep Hong Kong on a par with international best practices, new listing avenues have been introduced covering weighted voting rights and pre-profit companies engaged in the biotech sector – see Topic 2 for further details