

Greater compliance vigilance needed as Hong Kong intensifies listings scrutiny

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Financial institutions in Hong Kong need to be more vigilant about listing compliance as the territory's market regulator scrutinises companies that raise capital on the local bourse, sources said.



In recent months, the Securities and Futures Commission (SFC) has increased its direct presence in the regulation of listing matters, law firm Deacons said. The SFC did so through exercise of its statutory powers under the Securities and Futures (Stock Market Listing) Rules, to object to certain listing applications and to direct suspension of trading in the shares of certain listed companies.

"They [compliance and legal staff] will have to ensure that the banks are doing their work properly, whether the banks act as sponsors and/or underwriters/placing agents in initial public offerings (IPOs) or as compliance advisers to newly listed companies or financial advisers to listed companies. They will have to be prepared that the SFC will intervene at an early stage," said Ronny Chow, partner at the firm.

"That means, we will see not only disciplinary actions being taken at a later stage against bankers who failed to discharge their obligations properly, but also that more poorly managed deals would be put off due to the SFC's intervention," he said.

Legal and compliance staff had to be on their guard, said Mohan Datwani, head of technical and research standards at the Hong Kong Institute of Chartered Secretaries (HKICS).

"It is not an easy situation, and compliance staff could ill-afford not giving their all for legal and compliance matters," he said. "There are already rules relating to disclosure of information which attributes direct responsibilities and liabilities on officers, and now the new approach, this would no doubt keep legal and compliance professionals on edge."

On July 13, the SFC published "SFC Regulatory Bulletin: Listed Corporations" and a speech by Ashley Alder, chief executive. Alder was speaking about the SFC's new approach to listing issues as "front-loaded, transparent and direct" and "real-time" regulation.

In mid-July, the SFC objected to the listing of a company on the Growth Enterprise Market (GEM) of the Stock Exchange of Hong Kong Limited (SEHK) because of concerns over the high concentration of shareholding. This attracted attention because the listing was tightly held despite the fact its IPO was marketed through a public offer, Deacons said.

"That was followed by an announcement a few days later by another company that it decided to postpone its GEM IPO comprising public offer and placing on a 50:50 basis due to the regulators' enquiries on the presence of an open market. So far as listed companies are concerned, the SFC has directed the SEHK to suspend trading in eight stocks this year," the law firm said.

Datwani said: "There has been a lot of issues recently with the GEM board, which is now under consultation to be changed to be a standalone board for small and medium enterprise (SME) capital raising, and the whole issue of capital raising is no doubt on the agenda."

Tightly held listings

Recent incidences of small company share price declines and concerns about whether such entities are worthy of being listed on the local stock exchange have concerned both regulators and investors.

"The SFC wants to be more proactively involved in this. That's a good thing as the issues of any listing companies going wrong can have a more widespread impact," said Josephine Chung, director of CompliancePlus Consulting in Hong Kong.

The SFC's recent actions confirm its focus on cracking down on sponsor misconduct.

"The SFC expects that sponsors should have the required competence and integrity in assisting issuers in preparing and presenting the listing applications and that they should have conducted sufficient due diligence before submitting any listing applications and disclosed all material information and addressed major issues in the prospectuses," said Vicky Lam, partner at Norton Rose Fulbright in Hong Kong.

"The SFC will not hesitate to take enforcement action if those expectations were not met," she said.

"The signs were there"

Alder had said at the end of 2016 that the agency had re-examined the existing regulatory powers at its disposal. It decided to implement the new "front-loaded" approach to listing regulation. The move may be more of "an evolution of approach by the SFC," starting with the joint consultation paper issued by the SFC and Hong Kong Exchanges and Clearing (the SEHK's parent company) last summer.

"That also evidenced an intent by the SFC to be more actively involved in the listing process," said Stuart Rubin, partner with law firm Ashurst in Hong Kong.

Compliance needed to take the matter seriously because of its potential to add to the liability and reputational-related concerns for sponsor-related activity at financial institutions, he said.

Some lawyers said for sponsors, things would change little because the SFC has long been the local sentinel for IPO listings.

"The questions raised by the SFC go to applicants' fundamental qualities and suitability as listed entities. If applicants do not properly answer the regulator's questions, they run the risk of their applications being turned down," said James Fong, partner at Mayer Brown JSM in Hong Kong.

Compliance implications

SEHK-listed companies needed to ensure their compliance and corporate governance standards were sufficient to meet the SFC's requirements, Chung said.

Stephen Chan, partner at Dechert in Hong Kong, said for listed companies, compliance officers and directors should be mindful of the possibility of additional queries being raised by the SFC in relation to any proposed transactions.

"In addition to ensuring compliance with the relevant Listing Rules, compliance officers and directors should have a heightened sense of awareness of the commercial benefits of any proposed transactions, which will help to substantiate their views with the SFC in relation to any queries raised, such as whether the transaction is in the interests of shareholders as a whole," Chan said.

Additional time may be required for concurrent vetting by the SFC, he said. As such, listed companies should also factor in the time that would be needed when structuring their transactions. For new listings the move ought to be welcomed by applicants and other market participants, he said.

Historically, the SFC has participated in the vetting of the listing applications, but any comments would be passed through HKEx. Applicants and other professional parties have however had a hard time trying to have a direct discussion with SFC personnel to clarify their comments or questions, Chan said.

"We note that this is still the case now, but with respect to serious issues which may potentially warrant a letter of mindedness, the SFC may reach out directly to the listing applicants, which allows parties to resolve issues raised through direct communication. I personally think that this is a more efficient way of allowing the listing applicants and other market

participants to (i) understand what the critical issues are and (ii) address the SFC directly with respect to issued raised."

Fong welcomed the SFC's newer approach. "I want to know if the stock exchange or SFC has fundamental concerns over my application at its earliest opportunity and would like to have a direct communication with the relevant regulator regarding their concerns. It would further assist the market if there is more clarity as to when after submission of the listing application that the SFC would or would not issue such a letter of mindedness to object," he said.

"If the applicants become aware of such issues sooner, the applicants and their advisers could address them in a timely manner."

A spokesman for the SFC declined further comment.

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