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[online version](http://www.charltonslaw.com/disclosure-of-interests-under-the-securities-and-futures-ordinance-update/)

# Disclosure Of Interests Under The Securities And Futures Ordinance - Update

The SFC issued a [revised outline](http://en-rules.sfc.hk/net_file_store/new_rulebooks/h/k/HKSFC3527_2980_VER10.pdf) ([see archive](HKSFC3527_2980_VER10.pdf)) of Part XV of the Securities and Futures Ordinance (**SFO**) on 6 August (the **Outline**) which summarises the provisions of Part XV and contains detailed examples of how they work. The revisions have been made in response to queries raised with the SFC since the SFO came into force. We have also up-dated our detailed note on Disclosure of Interests which can be viewed by [clicking here](latest_A_1.htm).

The purpose of this note is to summarise the principal issues highlighted by the revised Outline.

## Options

The Outline states that when a listed company allots shares or issues an instrument under which it agrees to allot shares, or grants an option over its **own** shares, the SFC's view is that the company is not taking a position in its own shares, short or long, but is simply issuing or agreeing to issue shares (Paragraph 2.4.3. of the Outline). Accordingly, the company does not need to disclose these events. Likewise, since the listed company is not taken to have a short position, a controller of the listed company will not be deemed to have a short position under the deeming provisions of the SFO and no disclosure is required. This view would appear to be at odds with a strict interpretation of the legislation and its wide definition of the term 'short position'. It seems likely therefore that this view has been adopted more on the basis of the spirit of the legislation whose focus is primarily on the disclosure of positions held in other listed companies.

The holder of an option or other right to receive shares **does** however acquire a long position in the shares which must be disclosed.

Where a company grants an option over the shares of **another** listed company, the former company will take a short position in the latter company's shares which will be discloseable if the former company is already a substantial shareholder (ie. already holds 5% of the latter company's shares) and the short position amounts to 1% or more.

Note also that when a listed company grants to a director or chief executive a right to subscribe for its shares or debentures it is required to record the following information in its register of the interests of directors and chief executives:

1. the date on which the right is granted;
2. the period during which, or the time at which, it is exercisable;
3. the consideration for the grant (or, if none, that fact); and
4. a description of the shares or debentures involved, the number of shares or amount of debentures, and the price to be paid for them (or the consideration, if otherwise than in money).

Further, when any such right is exercised by a director or chief executive, the listed company must record the following information against his name in the register:

1. the fact of the exercise (identifying the right);
2. the number of shares or amount of debentures in respect of which it has been exercised; and
3. if -
	1. they were registered in his name, that fact; or
	2. they were not registered in his name, the name or names in which they were registered and the number of shares or amount of debentures registered in each name, if applicable.

The time limits for the listed company to record the above information in the register are 3 business days after the date of the grant of the right to subscribe for shares or debentures and 3 business days after the exercise of any such right.

## Disclosure Of Short Positions

The revised Outline emphasises that the acquisition of a short position of 1% or more or any increase or decrease in the percentage level of a short position over 1% is only required to be disclosed if the holder (not being a director or chief executive of the company) is already a substantial shareholder (ie. he already holds 5% or more of a class of a listed company's voting share capital). If a person has less than 5%, no disclosure need be made of his acquisition of, or change in the level of, his short position in the shares of the company.

In the case of directors and chief executives, they must disclose all short positions (however small) in any shares (not just voting shares) irrespective of whether they already hold a long position in the shares or not. Similarly they must disclose all long positions (however small) in any shares of the company.

## Buying And Selling Shares

### Buyer

A buyer of shares acquires an interest in shares at the time he contracts to buy and must therefore give notice of his interest in the shares within 3 business days after the date of the contract. No further notice is required when the buyer subsequently takes delivery of the shares.

### Seller

A seller of shares normally only ceases to have an interest in shares on the settlement date when he actually transfers the shares to the buyer. The seller must therefore notify the cessation of his interest within 3 business days of the settlement date. If in fact a seller ceases to be interested in the shares on the date of the contract for sale (eg. due to the operation of the clearing system), then notice should be filed within 3 business days of the contract.

If the contract for sale provides for settlement within 4 days on which the Stock Exchange is open for business, the seller is not required to give notice on entering into the contract for sale. If however the contract specifies a settlement date which is 5 or more trading days after the date of the contract, then 2 notices are required: (i) a notice of change in nature of the interest which must be filed within 3 business days of the contract and (ii) a notice of cessation of interest to be filed within 3 business days of the settlement date.

## Disclosure Obligations Resulting From Share Repurchases And Placements

Disclosure obligations arise not only from the actions of shareholders but can also arise from actions taken by third parties. For example, if a listed company buys back shares thereby reducing the number of shares in issue, an increase in the percentage level of the interests of the remaining shareholders is discloseable.

Conversely, in the case of a placement and top-up, where new shares are issued to a major shareholder to replace shares he has placed with a third party, the number of shares in issue will increase. Any consequent reduction in the percentage level of the interests of the other shareholders is discloseable.

In both the above situations, the 3 business day time limit for disclosure runs from the date the person concerned became aware of the facts that led to the change in the percentage level of his interest, ie. the date on which he became aware that the number of shares in issue had been increased or reduced.

## Wholly Owned Group Exemption

This exemption whereby a wholly owned subsidiary is exempted from notifying an interest if its ultimate holding company has disclosed its interest in the relevant shares **is not available in certain circumstances**. These circumstances are those where notice is required under Sections 310(2) and (3) which are as follows:

1. where a person has 5% or more of the shares of a company which is being listed;
2. where a person has 5% or more of shares of a class which is being listed or given full voting rights;
3. where a person had a notifiable interest on 1 April, 2003 which had not been disclosed under the previous regime; and
4. where a person has a notifiable interest on either the 5% threshold or 1% threshold for short positions being reduced.

These notices are referred to as 'Initial Notifications' in the SFC Outline. The other point to note about such notices is that the time limit for notification is 10 business days rather than 3 business days after the relevant event. Hence, when a wholly owned subsidiary has an interest of 5% or more in a company which is to be listed, it cannot rely on the wholly owned group exemption : instead both the subsidiary and its holding company must each disclose the interest in the shares held by the subsidiary.

## Rights Issues

The underwriter of a rights issue acquires an interest in all rights shares that he agrees to take up if they are not taken up by the shareholders. The underwriter will then need to file notice of cessation of his interest in the number of rights shares taken up by shareholders on completion of the rights issue.

## Disaggregated Group Interests

The SFO removes the obligation of a holding company to aggregate the interests of controlled companies who are investment managers, custodians or trustees whose interest in the shares arises solely from their obligation or entitlement to invest in, manage, deal in or hold interests in those shares on behalf of customers in the ordinary course of their business as such. For the exemption to apply the controlled company must exercise any rights to vote in respect of the shares and any power to invest in, manage, deal in or hold the shares, independently of its controlling company or any other company within the same group.

The SFC stresses in its Outline that this exemption is available only to the fund management industry. It does not entitle family members whose interests in the shares of 'family controlled' listed companies are held by trustees to disaggregate such interests. A trustee of a trust does not have 'customers' and will probably not be carrying on a business as an investment manager, custodian or trustee.

## Exempt Security Interests

An 'exempt security interest' in shares is not required to be disclosed. To qualify as such the interest must be held by a qualified lender by way of security only for a transaction entered into in the ordinary course of his business as such. The new Outline clarifies that in determining when an interest is held 'by way of security only', a distinction is drawn between a security interest in, and a transfer of title to, shares. If the lender has a right to return equivalent shares (ie. not the actual shares given by the borrower) and can deal with the shares as if they are his own in the meantime, this is a transfer of title to the shares and not the creation of a security interest.

## Interaction Of The Securities Borrowing And Lending Rules And The Wholly Owned Group Exemption

The revised SFC Outline contains detailed explanations and examples of the interaction of the wholly owned group exemption with the exemptions available under the Securities Borrowing and Lending Rules at paragraphs 2.13.18 to 2.13.27 of the Outline.

## Deemed Interests Of Directors And Chief Executives

In calculating the number of shares in which they are interested, directors and chief executives are required to include shares held by their spouse and children under 18 unless the spouse or children are themselves also directors or chief executives of the company.

However, if a director is also a substantial shareholder, he must include the interests of his spouse and children under 18 irrespective of whether they are also directors or chief executives of the company in disclosing his interest as a substantial shareholder in the shares of the company.

This note is intended as a summary only of the principal issues highlighted by the SFC's revised outline of Part XV of the SFO. Specific advice should be sought in relation to any particular situation.

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