Charltons - Hong Kong Law Newsletter - 27 June 2011

[online version](http://www.charltonslaw.com/consultation-paper-on-draft-short-position-reporting-rules-published/)

# Consultation Paper On Draft Short Position Reporting Rules Published

## Introduction

On 25 May 2011, the Securities and Futures Commission (**SFC**) published a consultation paper on the draft Securities and Futures (Short Position Reporting) Rules (**SPR Rules**). The draft SPR Rules are the result of a previous consultation concluded on 2 March 2010 on increasing short position transparency, but are slightly modified, taking into account further public comments. The SFC aims to implement the short position reporting requirement as soon as possible.

This newsletter summarises the draft SPR Rules, which together with the draft reporting template are set out in Appendix A and Appendix B to the consultation paper respectively. The consultation deadline is 30 June 2011.

The [Consultation on Securities and Futures (Short Position Reporting) Rules](https://www.sfc.hk/sfcConsultation/EN/sfcConsultFileServlet?name=shtpostrptrules&type=1&docno=1) ([see archive](openFile.pdf)) and the [Consultation Conclusions on Increasing Short Position Transparency](http://www.sfc.hk/sfc/doc/EN/speeches/consult/consultationconclusion2march2010english.pdf) ([see archive](consultationconclusion2march2010english.pdf)) are available on the SFC website.

## The Draft SPR Rules

### The Short Position Reporting Requirement

Section 3 of the draft SPR Rules requires a person who has a short position at the end of the last trading day of each week (usually a Friday) at or above the specified threshold to report the short position to the SFC. The specified threshold is the lower of:

* $30 million; or
* 0.02% of the issued share capital of the listed company.

The report must be submitted by the second business day of the following week (usually a Tuesday). Firms are also allowed to submit reports on short positions that do not reach the threshold, but such reports are optional.

The SFC is recommending to the Chief Executive in Council to make the breach of this requirement a criminal offence. The maximum penalties being considered are:

1. on conviction on indictment a fine of $500,000 and a term of imprisonment of 2 years;
2. on summary conviction a fine of $100,000 and a term of imprisonment of 6 months.

### Scope of and Exemptions from the Reporting Requirement

At the initial stage, only short positions in shares of the constituent companies of the Hang Seng Index, Hang Seng China Enterprises Index and other financial companies specified by the SFC need to be reported. In the future, derivatives or other shares may be included. Schedule 1 to the draft SPR Rules sets out the specified shares to which the reporting requirement applies.

Short selling transactions are excluded from the reporting requirement if they are not executed on the Stock Exchange of Hong Kong (**SEHK**) or an automated trading service (**ATS**) authorised by the SFC. Authorised ATSs are set out in Schedule 2 to the draft SPR Rules. Firms are allowed to report on short positions that are created off the SEHK or authorised ATSs, but such reports are optional. In the report, firms must indicate whether a component of the position reported was created on or off the SEHK (see Appendix B to the consultation paper).

### Submitting the Report

The obligation to report belongs to the person who is in the position to know the total outstanding short position. Usually, this would be the beneficial owner of the short position. In the case of trusts and funds, the obligation belongs to the trustee rather than the beneficiary or investment manager. The trustee should not aggregate or net the positions of different trusts that he administers separately. In the case of group structures, the obligation belongs to each individual legal entity within the structure. Reports may be submitted by authorised agents, but the principal remains legally responsible for reporting.

Short position reports must be submitted online using the SFC's electronic reporting facility, in the form specified by the SFC (see Appendix B to the consultation paper). The SFC will issue further guidance on the use of the electronic facility.

### Public Disclosure of Short Position Information

Under section 4 of the draft SPR Rules, the SFC will publish on its website aggregated short positions for each stock one week after the receipt of the reports. The results are anonymous, so the short positions of those who submitted the reports will not be publicly disclosed. The SFC will not begin to publish results until it is satisfied that the reporting system is free from significant problems. This may take a few months after the short position reporting regime is first implemented.

### Contingency Situations

In circumstances that would pose a threat to the financial stability of Hong Kong, section 5 of the draft SPR Rules empowers the SFC to require daily reporting of short positions that amount to or exceed the specified threshold at the end of each trading day. Such reports must be submitted the following business day. While the frequency of reports is increased, the threshold is unchanged. The SFC would continue to publish aggregated results weekly. Enhanced reporting is meant only to improve the quality of the short position information the SFC receives, not result in more frequently published aggregated results from the SFC.

In order to exercise its power under section 5, the SFC must publish an announcement, giving market participants at least 24 hours prior notice. When enhanced reporting is no longer necessary, the SFC must publish an announcement to inform market participants of the cessation date.

In the future, if the SFC finds these contingency measures inadequate, the public will be consulted before any changes are made to the Rules to tighten the contingency measures.

## Responding To The Consultation

Parties that wish to submit written comments may do so by one of the following methods on or before 30 June 2011:

Online submission:

<https://www.sfc.hk/sfcConsultation/EN/sfcConsultMainServlet?name=ShtPostRptRules>

Email:

[shortpositions@sfc.hk](mailto:shortpositions@sfc.hk)

Post:

Supervision of Markets Securities and Futures Commission 8th Floor, Chater House 8 Connaught Road Central Hong Kong

Fax:

(852) 2521 7917

This note constitutes a summary only of the SFC's [Consultation on Securities and Futures (Short Position Reporting) Rules](https://www.sfc.hk/sfcConsultation/EN/sfcConsultFileServlet?name=shtpostrptrules&type=1&docno=1) ([see archive](openFile.pdf)), which can be viewed on the SFC's website.

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