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[online version](http://www.charltonslaw.com/sfc-publishes-revised-guidelines-on-statutory-price-sensitive-information-disclosure-obligation/)

# SFC Publishes Revised Guidelines On Statutory Price Sensitive Information Disclosure Obligation

## Introduction

On 22 June 2011 the Securities and Futures Commission (**SFC**) published a [revised draft of its Guidelines on Disclosure of Inside Information](http://www.sfc.hk/sfc/doc/EN/speeches/public/consult/psi_guidelines_eng_m.pdf)(**Guidelines**) ([see archive](psi_guidelines_eng_m.pdf)) which provides guidance on the new statutory obligation to disclose price sensitive information (referred to as ‘inside information’ in the draft legislation) to be brought into effect by the Securities and Futures (Amendment) Bill 2011 (**PSI Bill**) which was introduced to the Legislative Council on 29 June 2011.

The SFC will be the enforcement authority for the new statutory disclosure regime and will be empowered to institute proceedings before the Market Misconduct Tribunal directly, without having to first refer the case to the Financial Secretary for his decision to do so. This process will also apply to the existing six types of market misconduct stipulated in the SFO. The SFC will provide informal consultation for listed corporations with regard to the disclosure requirements for 24 months initially and will publish frequently asked questions, but will not publish details of waivers granted.

The revised draft guidelines reflect public comments received by the SFC during the consultation process. The aim of the revisions, according to the SFC, is to ensure that the regulatory framework serves twin goals of guaranteeing the quality of Hong Kong’s capital markets and safeguarding the interests of shareholders. Once the final form of the bill is settled after its passage through the Legislative Council, the Guidelines may need to be revised further. The final version of the Guidelines will then be published in the Gazette and will take effect on the same day as the PSI Bill.

This newsletter summarises the main amendments made to the Guidelines.

## The Definition Of “Inside Information”

The definition of **inside information** to be introduced in new Section 307A SFO is the same as that of “relevant information” used in Section 245 SFO which applies to insider dealing. Under Section 307A, inside information, in relation to a listed corporation will mean “specific information that:

1. is about –
   1. the corporation;
   2. a shareholder or officer of the corporation; or
   3. the listed securities of the corporation or their derivatives; and
2. is not generally known to the persons who are accustomed or would be likely to deal in the listed securities of the corporation but would if generally known to them be likely to materially affect the price of the listed securities.”

## The Amendments

### 1. Status of the statutory obligations

The Guidelines now state that the obligations to disclose inside information under Part XIVA Securities and Futures Ordinance (**SFO**) are separate and distinct from the disclosure requirements under the Listing Rules and those under the Codes on Takeovers and Mergers and Share Repurchases (**Takeovers Codes**)(paragraph 7 of the Guidelines).

### 2. When is information ‘generally known’ by virtue of media comments/analysts’ reports?

On the issue of determining whether information is ‘generally known’ by virtue of being the subject of media comments, covered in analysts’ reports or carried on news service providers, paragraph 21 of the Guidelines provide that a corporation should consider not only how widely the information has been disseminated but also the accuracy and completeness of the information and the reliance the market can place on such information. In particular, a corporation should consider whether:

1. these sources contain the full information that would need to be disclosed as required under Section 307B(3) so that there are no material omissions, which may make the disclosure false or misleading;
2. the market will realise that the information in these sources reflects the information known to the corporation; and
3. the information will be regarded as speculation or opinion of persons outside the corporation.

Where information known to the market is incomplete or there are material omissions or there are doubts as to its bona fides, such information cannot be regarded as generally known and accordingly full disclosure by the corporation is necessary.

### 3. When is information likely to have a material price effect?

The Guidelines now provide that information that is likely materially to affect the price is information which may well materially affect the price. Put another way, it is more likely than less likely that the price will be affected materially. The further element of the statutory test concerns materiality. It may be that what is a material price increase in one case may not necessarily be a material price increase in another case. It all depends on the share and the circumstances obtaining at the time (paragraph 25 of the Guidelines).

The standard by which materiality is to be judged is whether the information on the particular share is such as would influence persons who are accustomed or would be likely to deal in the share, in deciding whether or not to buy or to sell that share. If generally known, it is the impact of the information on persons who are accustomed or would be likely to deal in the share, and thus on price, which has to be judged (paragraph 26).

### 4. Management accounts: Is information in analysts’ and media reports financial journals “generally known”?

The Guidelines state that while there may be a substantial amount of financial and economic information circulated in the market, it is not unusual that profit forecasts made on a corporation by different analysts vary considerably and media reports contain inconsistencies. As a result, analysts’ reports, financial journals and media reports often fall short of providing information which is accurate, complete and not misleading or deceptive. Accordingly, a corporation should not normally treat these as information that is generally known and disclosure of any inside information would be necessary (paragraph 33).

### 5. How and when should inside information be disclosed?

Section 307B(1) SFO will provide that:

“a listed corporation must, as soon as reasonably practicable after any inside information has come to its knowledge, disclose the information to the public.”

Section 307B(3) states that:

“Without limiting subsection (1), a listed corporation fails to disclose the inside information required under that subsection if:

1. the information disclosed is false or misleading as to a material fact, or is false or misleading through the omission of a material fact; and
2. an officer of the corporation knows or ought reasonably to have known that, or is reckless or negligent as to whether, the information disclosed is false or misleading as to a material fact, or is false or misleading through the omission of a material fact”

The Guidelines provide that the information contained in an announcement must not be false or misleading but must be accurate and complete in all material respects and there must be no omissions that would make the information misleading. The information must be presented in a clear and balanced way, which requires equal disclosure of both positive and negative facts (paragraph 42).

The SFC expects a corporation to use the electronic publication system operated by the Stock Exchange (HKEx-Eps) for dissemination of inside information. In addition, the Listing Rules require a corporation to publish announcements of inside information through the electronic publication system of the Exchange (paragraph 47). The Guidelines (paragraph 48) state that while additional means may be used (such as press releases issued through a news or wire service, holding a press conference in Hong Kong and/or posting an announcement on a corporation’s own website, such additional means may not be sufficient to satisfy the obligation to disclose “in a manner that can provide for equal and effective access by the public to the inside information disclosed” (as required by Section 307C(1) SFO).

### 6. Responsibility for compliance and management controls

Section 307B(2) of the SFO states that:

“For the purposes of subsection (1), inside information has come to the knowledge of a listed corporation if –

1. information has, or ought reasonably to have, come to the knowledge of an officer of the corporation in the course of performing functions as an officer of the corporation; and
2. a reasonable person, acting as an officer of the corporation, would consider that the information is inside information in relation to the corporation.”

Section 307G(1) provides that:

“Every officer of a listed corporation must take all reasonable measures from time to time to ensure that proper safeguards exist to prevent a breach of a disclosure requirement in relation to the corporation.”

#### Who is an “officer”?

Part 1 of Schedule 1 of the SFO defines an “officer”, in relation to a corporation, as “a director, manager or secretary of, or any other person involved in the management of, the corporation”.

On the question of who is a “manager”, the Guidelines state that a manager normally refers to a person who, under the immediate authority of the board, is charged with management responsibility affecting the whole of the corporation or a substantial part of the corporation (paragraph 52).

### 7. Safe harbours that allow non-disclosure of inside information

#### Where disclosure is prohibited by law

Section 307D(1) SFO provides that a listed corporation is not required to disclose any inside information under Section 307B if and so long as the disclosure is prohibited under, or would constitute a contravention of a restriction imposed by, an enactment or an order of a court. Paragraph 57 of the Guidelines mirrors this in stating that statutory disclosure is not required for information if its disclosure would breach an order of a Hong Kong court or any provision of any Hong Kong statute.

Paragraph 57 of the Guidelines states that where a corporation or any of its officers is subject to an investigation by the ICAC and such investigation constitutes inside information, disclosure would not be required to the extent that it is prohibited statutorily. Nonetheless, disclosure of other information, which would not contravene the relevant statutory requirement, is still required.

Paragraph 58 of the Guidelines further confirms that the Section 307D(1) safe harbour does not apply to information the disclosure of which is prevented by a contractual duty. The terms and conditions of a contract do not override the statutory requirement

#### Information concerning incomplete proposals or negotiations

Section 307D(2)(c) SFO provides a safe harbour from the statutory disclosure obligation for information concerning incomplete proposals or negotiations. In paragraph 67 of the Guidelines, the SFC has deleted the additional requirement that the outcome of the incomplete proposal or negotiation may be prejudiced if the information is released prematurely.

Paragraph 67 of the Guidelines gives the following examples of proposals or negotiations that do not need to be disclosed:

* when a contract is being negotiated but has not been finalised;
* when a corporation decides to sell a major holding in another corporation;
* when a corporation is negotiating a share placing with a financial institution; or
* when a corporation is negotiating the provision of financing with a creditor.

The following circumstances, which were included in the original draft Guidelines, have now been removed from the examples of proposals/negotiations covered by the safe harbour:

* where a premature disclosure may threaten the loss of the contract to another party;
* when the deal may fail with premature disclosure; and
* where a public disclosure may undermine the conclusion of such negotiation.

#### Preservation of confidentiality

Reliance on the Section 307D(2) safe harbours (for information that relates to an incomplete proposal or negotiation, is a trade secret, concerns the provision of liquidity support from the Exchange Fund or other central bank, or where disclosure has been waived by the SFC) is conditional upon the corporation taking reasonable precautions to preserve the confidentiality of the information and confidentiality being preserved.

A listed corporation has not failed to take reasonable precautions for preserving the confidentiality of any inside information only because the corporation has, in the ordinary course of business, disclosed the information to any person who –

1. requires the information to perform the person’s functions in relation to the corporation; and
2. by virtue of any enactment, rule of law, contract, or the articles of association of the corporation, is under a duty to the corporation not to disclose the information to any other person.

In those circumstances, the confidentiality of the information is to be regarded as having been preserved.

The Guidelines add that the information should be given on the basis that restricts its use to the stated purpose and the recipient should recognise its resulting obligations. The SFC has now set out in paragraph 62 of the Guidelines the following categories of persons who may receive the information:

1. The corporation’s advisers and advisers of other persons involved in the matter in question;
2. Persons with whom the corporation is negotiating, or intends to negotiate, any commercial, financial or investment transaction (including prospective underwriters or placees of the securities of the corporation);
3. The corporation’s lenders;
4. The corporation’s major shareholders; and
5. Any government department, statutory or regulatory body or authority (e.g. the SFC or the Stock Exchange).

The Guidelines provide that a corporation that has relied on any of the safe harbours should keep under review whether confidentiality of the information has been maintained. Once confidentiality is lost, the safe harbour ceases to apply and the corporation must disclose the inside information as soon as reasonably practicable (paragraph 64).

The revisions to the Guidelines now clarify that where confidentiality has been lost and the safe harbour falls away, a corporation will not be regarded as in breach of the disclosure requirement if the corporation:

1. proves that it has taken reasonable measures to monitor the confidentiality of the information; and
2. discloses the information in accordance with Section 307C as soon as reasonably practicable after the corporation becomes aware that the information has leaked (paragraph 65).

#### Where information concerns a trade secret

Paragraph 69 of the Guidelines deals with what information can be regarded as a trade secret, for which no statutory disclosure is required. A trade secret is stated to generally refer to proprietary information owned by a corporation: (a) used in a trade or business of the corporation; (b) which is confidential; (c) which, if disclosed to a competitor, would be liable to cause real or significant harm to the corporation’s business interests; and (d) which the corporation must limit its dissemination.

The SFC has now added that a corporation cannot regard the commercial terms and conditions of a contractual agreement or the financial information of a company as trade secrets as these are not proprietary information or rights owned by the corporation.

#### Where disclosure is waived by the SFC

The Guidelines now state that the SFC may, on application by a corporation, grant an exemption to waive disclosure of information, where its disclosure is prohibited under or would contravene a restriction imposed by:

* the legislation;
* an order of a court exercising jurisdiction under the law;
* a law enforcement agency; or
* a government authority in the exercise of a power conferred by the legislation,

of a place outside Hong Kong, especially where the corporation or certain of its subsidiaries are incorporated or operate outside Hong Kong (paragraph 71 of the Guidelines).

An exemption may be granted unconditionally or subject to specified conditions. No statutory disclosure is required of information for which an exemption has been granted if any conditions imposed in relation to the exemption have been complied with.

According to paragraph 73 of the Guidelines, an application for exemption from disclosure would be considered by an SFC executive committee that would make a first instance decision after considering all relevant facts and circumstances. If the waiver is rejected by the executive committee, the corporation may request that he decision be reviewed by a committee appointed by the Commission for the purposes of handling reviews (**Review Committee**). A request for such a review must be made by the applicant to the Review Committee within 2 business days after the refusal of the waiver. Any member of the SFC who was involved in the first instance decision shall not participate in the deliberation or voting of the Review Committee in considering the review. A decision made by the Review Committee would be final and binding.

### 8. Analysts’ reports

Paragraph 80 of the Guidelines provides that a corporation should ensure that no inside information is given when answering an analyst’s questions or reviewing an analyst’s draft report. The Guidelines now state that in some circumstances, for example where a corporation’s business is complex and/or comprised of a many different divisions, it is possible that analysts may draw on out of date data, or misread or misinterpret historical information. in such cases, unless the corporation knows inside information which has not been disclosed, strictly speaking the corporation is not obliged to make correction or clarification under the SFO. As a matter of good practice, however, it may be appropriate for a corporation to clarify historical information and correct any factual errors in analysts’ assumptions which are significant to the extent that they may mislead the market, provided that any clarification is confined to drawing analysts’ attention to information that has already been made available to the market. Under the Listing Rules the Stock Exchange may require a corporation to make disclosure or clarification beyond that required by the SFO as is necessary to ensure a fair and orderly market.

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