

**Consultation on
Proposed Amendments to Listing Rules
relating to Share Schemes of Listed Issuers**

The Stock Exchange of Hong Kong Limited (the “**Exchange**”) issued a consultation paper on “Proposed Amendments to Listing Rules relating to Share Schemes of Listed Issuers” in October 2021 (“**Consultation Paper**”).

In response, the Law Society provides the following submissions on the questions posed. The same abbreviations and definitions appearing in the Consultation Paper are used in this paper.

Question 1 Do you agree with the proposal to amend Chapter 17 to also govern share award schemes involving the grant of new shares of listed issuers? Please provide reasons for your views.

Law Society’s response:

We support the Exchange’s proposal to amend Chapter 17 to also govern share award schemes involving the grant of new shares of listed issuers. Share award schemes involving the grant of new shares are becoming a main stream choice of incentive schemes for listed issuers or unlisted companies aspiring to seek a listing in Hong Kong.

While share option schemes may be the prevailing choice of incentive schemes historically and Chapter 17 had not also governed share award schemes, there is no specific regulatory reason not to update Chapter 17 to also regulate share award schemes involving the grant of new shares.

Question 2 Do you agree with the proposed definition of eligible participants to include directors and employees of the issuer and its subsidiaries (including persons who are granted shares or options under the scheme as an inducement to enter into employment contracts with these companies)? Please provide reasons for your views.

Law Society’s response:

Agree.

Question 3 Do you agree with the proposal that eligible participants shall include Service Providers, subject to additional disclosure and approval by the remuneration committee? Please provide reasons for your views.

Law Society's response:

We agree in principle that the Listing Rules should provide more tangible guidance on who may become "eligible participants" so as to provide a context in which a participant's contribution can be measured.

We agree with the proposal to include Service Providers as "eligible participants" and the proposed additional disclosure and approval. We offer the following observations:

- (a) the 17th Schedule of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) ("**17th Schedule**") sets out in its Part 1 safe harbours where certain "offers of securities" fall outside the "prospectus" regime. For example, paragraph 8 of Part 1 of the 17th Schedule includes a safe harbour for offer to "qualified persons" which is defined as "bona fide director, employee, officer, consultant, former director, former employee, former officer, former consultant..." and "consultant" is defined as a person who, pursuant to a contract for services, renders services....which are commonly rendered by an employee..."*
- (b) paragraph 33 of the Consultation Paper also cited examples for the need to extend "eligible participants" to include Service Providers "the continuity and frequency of their services are akin to those of employees..."*
- (c) We are conscious that there is no direct regulatory reason to import the definition of "qualified persons" in the 17th Schedule as the new Service Providers definition under the Listing Rules as the 17th Schedule and the proposed Chapter 17 of the Listing Rules regulate different matters. The following, however, may serve to clarify the difference:*
 - Adding a drafting note to Rule 17.03A(c) to the effect that: Issuers should assess the need and applicability of any safe harbours in the 17th Schedule of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) ("**17th Schedule**") where certain "offers of securities" fall outside the "prospectus" regime. Compliance with this Chapter 17 does not imply that any particular safe harbour in the 17th Schedule will be automatically available to "offer of securities" made under a scheme.*
- (d) We believe that the intention is for Service Providers to mean an individual who provides services to an issuer. If a service provider is a business entity which provides the services via its personnel (e.g. employees), such personnel, strictly, is providing services to the service provider and not to the issuer and is not captured by the proposed definition of Service Providers. We welcome clarification if the proposed definition of Service Providers include employees or other personnel of such Service Provider if it is a business entity.*

Question 4 Do you agree with the proposal that eligible participants shall include Related Entity Participants, subject to additional disclosure and approval by the remuneration committee? Please provide reasons for your views.

Law Society's response:

Agree.

Question 5 Do you agree with the proposal to allow the scheme mandate to be refreshed once every three years by obtaining shareholders' approval? Please provide reasons for your views.

Law Society's response:

Agree.

Question 6 Do you agree with the proposal to allow the scheme mandate to be refreshed within three years from the date of the last shareholders' approval by obtaining independent shareholders' approval? Please provide reasons for your views.

Law Society's response:

Agree.

Question 7 Do you agree with the proposal to remove the 30% limit on outstanding options? Please provide reasons for your views.

Law Society's response:

Agree.

Question 8 Do you agree with the proposal to require a sublimit on Share Grants to Service Providers? Please provide reasons for your views.

Law Society's response:

We agree with the proposal to require a sublimit on Share Grants to Service Providers but would invite the Exchange to clarify whether as a matter of policy Related Entity Participants should also be subject to such additional requirement.

Question 9 Do you agree with the proposal to require a minimum of 12-month vesting period? Please provide reasons for your views.

Law Society's response:

Response combined with Question 10's. Please see below.

Question 10 Do you agree with the proposal that Share Grants to Employee Participants specifically identified by the issuer may vest within a shorter period or immediately if they are approved by the remuneration committee with the reasons and details disclosed? Please provide reasons for your views.

Law Society's response:

We agree with the proposal but would note that mandating a minimum vesting period may be too prescriptive. We also note the views of other stakeholders as set out in paragraph 52 of the Consultation Paper. Having remuneration committee as the gatekeeper on this issue appears appropriate.

Question 11 Do you agree with the proposed disclosure requirements relating to (a) performance targets; and (b) clawback mechanism? Please provide reasons for your views.

Law Society's response:

We agree with the proposed disclosure requirements relating to clawback mechanism.

We believe that performance targets and performance related measures in respect of a grant may be very specific and are normally commercially sensitive. In addition, with reference to paragraph 57 of the Consultation Paper, we believe that most, if not all, issuers are likely to seek a waiver, and such waiver could possibly evolve into a "standard" or "procedural" waiver in practice. We therefore assume that the proposal does not intend to require specific disclosure of "targets levels and performance related measures", and from a more practical standpoint suggest the following drafting adjustment to the proposed Rule 17.06B(7):

(7) a narrative description of the performance targets attached to the options or awards granted (including a qualitative description of the target levels and performance related measures).....

Question 12 Do you agree that it is not necessary to impose a restriction on the grant price of shares under share award schemes? Please provide reasons for your views.

Law Society's response:

Agree.

Question 13 Do you agree with the proposal to apply the 1% Individual Limit to Share Grants (including grants of shares awards and share options) to an individual participant? Please provide reasons for your views.

Law Society's response:

We agree with the proposal to apply the 1% Individual Limit to Share Grants (including grants of share awards and share options) to an individual participant.

Question 14 Do you agree with the proposal to require approval from the remuneration committee instead of INEDs for all Share Grants to Connected Persons? Please provide reasons for your views.

Law Society's response:

Agree.

Question 15 Do you agree with the proposal to relax the current shareholder approval requirement for grants of share awards to a director (who is not an INED) or a chief executive set out in paragraph 65 above? Please provide reasons for your views.

Law Society's response:

We agree with the proposal to introduce a de minimis threshold for shareholder approval requirement regarding grants of share award involving issuance of new shares to a director (who is not an INED) or a chief executive.

Question 16 Do you agree with the proposal to also relax the current shareholder approval requirement for grants of share awards to an INED or substantial shareholder of the issuer set out in paragraph 68 above? Please provide reasons for your views.

Law Society's response:

Agree.

Question 17 Do you agree with the proposal to relax the current shareholder approval requirement for grants of share awards to a controlling shareholder of the issuer set out in paragraph 69 above? Please provide reasons for your views.

Law Society's response:

We disagree to the relaxation of the shareholder approval requirement for grants of share awards to controlling shareholders. Whilst there is a proposed de minimis of 0.1% per year, the share awards to controlling shareholders could still amount to a large transfer of value in a very big cap stock. Given a controlling shareholders' influence over the board, we are concerned about checks and balances. The Exchange does not seem to have provided much justification for the proposal.

Question 18 Do you agree with the proposal to remove the HK\$5 million de minimis threshold for grants of options to an INED or substantial shareholder of the issuer? Please provide reasons for your views.

Law Society's response:

Agree.

Question 19 Do you agree with the proposals to require disclosure of Share Grants to Related Entity Participants or Service Providers on an individual basis if the grants to an individual Related Entity Participant or Service Provider exceed 0.1% of the issuer's issued shares over any 12-month period? Please provide reasons for your views.

Law Society's response:

Agree.

Question 20 Do you agree with the proposed disclosure requirement for the grant announcement? Please provide reasons for your views.

Law Society's response:

We agree in principle with the proposed disclosure requirement for the grant announcement, for the reason set out in paragraph 76 of the Consultation Paper. Please also note our response to Question 11 above.

Question 21 Do you agree with the proposed disclosure requirements for Share Grants in an issuer's interim reports and annual reports? Please provide reasons for your views.

Law Society's response:

We agree in principle with the proposed disclosure requirement for Share Grants in an issuer's interim reports and annual reports. Please note our response to Question 11 above. Please also clarify if Rule 17.07(1)(c) requires qualitative description (as opposed to specific description) of "performance targets".

Question 22 Do you agree with the proposal to require disclosure of matters reviewed by the remuneration committee during the reporting period in the Corporate Governance Report? Please provide reasons for your views.

Law Society's response:

Agree.

Question 23 Do you agree with the proposal to require changes to the terms of share award or option granted be approved by the remuneration committee and/or shareholders of the issuer if the initial grant of the award or option requires such approval? Please provide reasons for your views.

Law Society's response:

Agree.

Question 24 Do you agree with the proposal to provide a waiver for a transfer of share awards or options granted under Share Schemes as described in paragraph 86? Please provide reasons for your views.

Law Society's response:

Agree.

Question 25 Do you agree with the proposal to restrict the voting rights of unvested shares held by the trustee of a Share Scheme and require disclosure of the number of such unvested shares in monthly returns? Please provide reasons for your views.

Law Society's response:

We agree, for the reasons set out in paragraph 88 of the Consultation Paper. However, trustees of share scheme may be required or permitted to vote their holdings, e.g. at a scheme of arrangement court meeting where the holdings are "disinterested". It is not clear whether Rule 17.05A intends to apply in such scenario and we would invite the Exchange to clarify this.

Question 26 Do you agree with the proposed disclosure requirements for Share Schemes funded by existing shares of listed issuers? Please provide reasons for your views.

Law Society's response:

Agree.

Question 27 Do you agree with the proposal to restrict the voting rights of unvested shares held by the trustee of a Share Scheme and require disclosure of the number of such unvested shares in monthly returns? Please provide reasons for your views.

Law Society's response:

We agree, for the reason set out in paragraph 88 of the Consultation Paper. Please note our response to Question 25 above.

Question 28 Do you agree with our proposal to amend Chapter 17 to also govern share award schemes funded by new or existing shares of subsidiaries of listed issuers? Please provide reasons for your views.

Law Society's response:

Agree.

Question 29 Do you agree with the proposed exemption for Share Schemes of Insignificant Subsidiaries? Please provide reasons for your views.

Law Society's response:

Agree.

Question 30 Do you agree with our proposal to amend Chapter 17 to also govern Share Schemes involving grants of shares or options through trust or similar arrangements for the benefit of specified participants? Please provide reasons for your views.

Law Society's response:

We agree with the proposal to amend Chapter 17 to also govern Share Schemes involving grants of shares or options through trust or similar arrangements for the benefit of specified participants, as such arrangement is becoming increasingly popular.

Question 31 Do you agree with our proposal to remove the recommended disclosure requirement for the fair value of options as if they have been granted prior to the approval of the scheme? Please provide reasons for your views.

Law Society's response:

Agree.

Question 32 Do you agree with our proposals to amend the Rules described in paragraph 100? Please provide reasons for your views.

Law Society's response:

We agree with the proposed consequential amendments.

The Law Society of Hong Kong
21 December 2021