New Year, New Approach? The SFC's Current Enforcement Activities

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Recently, the market has seen the suspension of a number of listed companies by the Securities and Futures Commission ("**SFC**"). Notably, the SFC's power to suspend comes from the Securities and Futures (Stock Market Listing) Rules ("**Stock Market Listing Rules**"). Below, we take a brief look at the SFC's power and what affected companies can do under the Stock Market Listing Rules.

The Stock Market Listing Rules

The SFC has wide powers to suspend the trading of shares in listed companies under the Stock Market Listing Rules, when it deems, among other things:-

- materially false, incomplete or misleading information has been included in a listing prospectus, announcement or circular, etc. ("**section 8(1)(a)**");
- it is necessary or expedient in the interest of maintaining an orderly and fair market; or
- it is in the interest of the investing public or for investor protection (together, "**section 8**").

To some extent, the SFC's power under section 8 can be distinguished from the suspension powers of the Stock Exchange of Hong Kong ("**HKEx**"), which apply where the listed company is in severe financial difficulties, does not have sufficient operations, fails to publish financial results, has not published material information or has public float issues.

Therefore, a suspension under section 8 generally indicates that the SFC sees a fundamental issue with the listed company. The section 8 power is sometimes invoked during the course of investigation of an alleged breach of the Securities and Futures Ordinance (Cap. 571). The elements of section 8(1)(a) mirrors those of sections 277 and 298 of the Securities and Futures Ordinance ("**SFO**") in relation to disclosing false or misleading information of a listed company.

A new front-loaded approach

The HKEx is often referred to as the frontline regulator for listing applications and post-listing matters. This does not mean that the SFC takes a back seat; indeed, in the joint consultation paper of the HKEx and the SFC published in September 2017, the SFC has made clear that it will take a "*new front loaded approach to directly intervene in serious listing matters*" regarding listing applications and "*have a more direct presence in more serious areas of listing regulation*".[1]

Arguably, this new approach of the SFC does not only apply to listing applications but also to existing listed issuers who are allegedly involved in regulatory non-compliance matters (e.g. accounting irregularities, fraudulent activities etc). This can be seen from the SFC's increasing exercise of its power under section 8.

Between the years of March 2010 and March 2016, suspensions under section 8 were only invoked once or twice a year:-[2]

For the year ended 31 March	Number of instances that section 8 was exercised
2010/2011	0
2011/2012	1
2012/2013	1
2014/2015	1
2015/2016	2
2016/2017	4

Yet, from June 2017 onwards, we have seen at least six additional issuances of section 8 suspensions.

A right to review the SFC's suspension decision

It should be noted that once the trading of shares has been suspended under section 8, the Stock Market Listing Rules do provide the affected listed company with a right to a review of the SFC's suspension decision.

The affected listed company has the statutory right to make written representations to the board of the SFC (i.e. the chairman, the CEO, the executive directors

[1] Joint Consultation Conclusions of the HKEx and the SFC on the Proposed Enhancements to the Stock Exchange of Hong Kong Limited's Decision-Making and Governance Structure for Listing Regulation
[2] The SFC's annual reports 2012-2013 and 2016-2017

and the non-executive directors) regarding the SFC's suspension decision ("**review mechanism**").

Upon considering the representations from the listed company, the SFC board may direct:-

- trading to resume on conditions (if any); or
- the HKEx to cancel the listing of its shares.

Given the SFC's limited exercise of the section 8 power in the past, there had, accordingly, been scarce limited use of the review mechanism. One recent example is Hanergy Thin Film Power Group Limited ("**Hanergy**"), who has been suspended under section 8 since July 2015. It had invoked the review mechanism in January 2017.

In Hanergy's case, it was required to submit a disclosure document to the SFC board, setting out its activities, business, assets, liabilities, financial performance and prospects.[3] Hanergy remains suspended, while it takes steps to fulfil these requirements.[4]

The SFC's delisting order

If the SFC board under the review mechanism order the HKEx to delist the company, there is no further express right of appeal against the delisting decision under the Stock Market Listing Rules. Further, it appears that the Listing Rules do not prohibit an immediate delisting of the company.

It is noteworthy that the HKEx recently stated in a consultation paper "Delisting and Other Rule Amendments" that it intends to exercise its power to immediately delist where the issue faced by the listed company is "*so fundamental to the general principles for listing and are beyond remedy*", for instance, where "*it is found by the court that its management and controlling shareholder have operated a fraudulent scheme to overstate its business and profits*".[5]

Regardless of the conclusions of such consultation, it seems clear that the HKEx has adopted a more robust approach in delisting companies whose shares are suspended due to regulatory investigations.[6]

We observed that the HKEx can, and has, moved quickly to delist. For example, in the case of Qunxing Paper Holdings Company Limited ("**Qunxing**"). The SFC had exercised its powers to suspend the trading of its shares in December 2013 pending an investigation into an alleged exaggerated turnover figures in its prospectus. On 6 October 2017, the HKEx ordered that Qunxing would be given until 6 November 2017 (i.e. one month) to remedy various matters otherwise its shares would be delisted in November 2017. Its listing status was cancelled on 28 November 2017.[7]

Conclusion

From these recent events, it is clear that both the HKEx and the SFC have stepped up enforcement actions, particularly in relation to those suspected of serious market misconduct.

We await the HKEx's "Delisting and Other Rule Amendments" consultation conclusions on its proposed approach in handling prolonged suspension of companies affected by section 8. This is likely to have important regulatory implications for the market, the investing public and the companies that are currently or at risk of being suspended by the SFC under section 8 of the Stock Market Listing Rules.

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[3] SFC enforcement news dated 4 September 2017
[4] Hanergy's announcement dated 4 September 2017
[5] The HKEx's consultation paper entitled "Delisting and Other Rule Amendments" dated September 2017
[6] ibid
[7] Qunxing's announcement dated 28 November 2017