Report on the Securities and Futures Commission's Review of the Exchange's Performance in Its Regulation of Listing Matters

December 2024

Contents

Section 1

Introduction

1. This report summarises the key findings and recommendations of the Securities and Futures Commission's (**SFC**) 2024 review of the performance of The Stock Exchange of Hong Kong Limited (**Exchange**) in its regulation of listing matters during 2022 and 2023.

2. The Exchange is a wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited (**HKEX**).

Objectives of our review

3. The SFC has a statutory duty under section 5(1)(b) of the Securities and Futures Ordinance (**SFO**) to supervise, monitor and regulate the activities carried on by the Exchange. Under the Listing MOU[1], it was agreed that the SFC would conduct periodic audits or reviews of the Exchange's performance in its regulation of listing-related matters as a means to discharge the SFC's statutory function to supervise and monitor the Exchange.

4. The First Addendum to the Listing MOU dated 9 March 2018 provides that in conducting these periodic audits or reviews, the SFC will focus on:

   (a) whether the Exchange, in carrying out its listing regulatory function, has discharged and is discharging its duties under the SFO; this includes assessing its work in developing, administering and implementing its Listing Rules[2] as well as the monitoring and enforcement of compliance with those rules;

   (b) the adequacy of the Exchange's systems, processes, procedures and resources for performing its listing function; and

   (c) the effective management of conflicts of interest within the Exchange as a regulator and as part of a for-profit organisation, including the supervisory functions performed by the Listing Committee.

Scope of the review

5. Our 2024 review covered the Exchange's regulation of listing matters in 2022 and 2023 (**review period**) and focused on the following areas:

   (a) the Exchange's handling of issuers' non-compliance with the Listing Rule requirements on disclosure of material information;

   (b) the Exchange's handling of issuers' unusual stock price and volume movements; and

   (c) the Exchange's vetting of initial public offering (**IPO**) applications.

[1] The Memorandum of Understanding between the Exchange and the SFC dated 28 January 2003 (**Listing MOU**).

[2] Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

How we conducted the assessment

6. In conducting our assessment, we considered:

   (a) HKEX's 2022 and 2023 annual reports, the Listing Committee Reports for 2022 and 2023, and the 2022 and 2023 Reports on the Exchange's Review of Issuers' Annual Reports;

   (b) the Exchange's published disciplinary procedures, listing decisions, guidance letters and other related documents on the HKEX website;

   (c) relevant internal documents, written policies, procedures and processes of the Listing Division's operational departments;

   (d) information received from the Listing Division in the ordinary course of our supervisory work, including its monthly reports and case data;

   (e) case files for sample cases;

   (f) minutes of meetings of the Listing Committee and the Listing Operation Governance Committee (**LOG Committee**), excerpts of minutes of meetings of the respective boards of directors of the Exchange and HKEX, and other relevant internal documents relating to the activities of the Listing Committee and the Listing Division;

   (g) relevant internal documents submitted to the Listing Committee and the LOG Committee by the Listing Division in relation to the activities of the Listing Division;

   (h) our discussions with the Chairman of the Listing Committee; and

   (i) our discussions with the Head of Listing, the heads of the operational departments and other senior personnel of the Listing Division, and written responses to our enquiries.

Our findings

7. Below is a summary of our findings and recommendations following the review. In arriving at our recommendations, we have taken into account initiatives and proposals undertaken by the Exchange after the review period. Our findings and recommendations are set out in more detail in Section 2 of this report. We also noted that the Exchange has taken steps in response to the recommendations set out in our 2021 and 2022 review reports.

8. The Head of Listing and the Chairman of the Listing Committee have reviewed this report. We wish to thank members of the Listing Committee and the staff of the Listing Division for their assistance in the review process.

Summary of observations and recommendations

9. The SFC's observations and recommendations are as follows:

The Exchange's handling of issuers' non-compliance with the Listing Rule requirements on disclosure of material information

The Exchange monitors issuers' activities for compliance with the Listing Rules. During the review period, the Exchange identified nearly 400 cases in which the issuers failed to comply with the Listing Rule requirements on timely disclosure of material information. Most of these cases involved a failure to comply with the announcement, circular and shareholders' approval requirements for either a notifiable transaction or a connected transaction. An estimated one fourth of these cases involved breaches of the requirements for major or more significant transactions or connected transactions. We reviewed the Exchange's processes and procedures for handling issuers' non-compliance with these Listing Rule requirements, and a sample of cases.

(a) Given (i) the particular importance of the notifiable and connected transaction rules in protecting the interests of public shareholders, (ii) the size of the transactions involved in those cases where no regulatory action was taken, and (iii) the high number of non-compliance by listed issuers during the review period, we recommend that the Exchange adopt measures designed to improve issuers' compliance and standards in these areas (paragraphs 33 to 35).

(b) We recommend that the Listed Issuers Regulation (**LIR**) department[3] actively follow up with listed issuers to enhance their systems and controls in order to improve their ability to comply with these Listing Rules. LIR should ensure (i) that all issuers that commit such a material Listing Rule breach take appropriate action to prevent a recurrence and (ii) that the issuer appropriately addresses the weaknesses in its internal systems, processes and controls and remains suitable for listing, regardless of whether the LIR department decides to refer the issuer in question to Listing Enforcement for investigation. Amongst other things, the issuer should issue an announcement regarding the Listing Rule breach that has taken place and draw up a remedial plan (paragraphs 36 to 38).

(c) We further recommend that, for at least one full financial year after an issuer announces its remedial plan, LIR follow up at appropriate time intervals, and request the issuer to report on its implementation of the plan and to publicly announce any material change or deviation therefrom (paragraph 39).

(d) We also recommend that the Exchange review its existing policy on sanctions in these cases. The requirements of the relevant Listing Rules on notifiable and connected transactions are clear and well established, and the fact that an issuer has failed to comply with those requirements can be established without a complex and prolonged investigation. Given the high number of non-compliance events found, we recommend that the Exchange, working in consultation with the Listing Liaison Forum (**LLF**) and the Listing Committee, review the current policy, system, processes and procedures for handling these types of Listing Rule breaches and impose meaningful sanctions more frequently to send a

[3] With effect from 1 October 2024, the LIR department and Listing Enforcement department have been integrated and renamed as the Listing Regulation and Enforcement department.

stronger deterrent message and reduce the incidence of such Listing Rule breaches among listed issuers (paragraphs 40 and 41).

(e) For novel, complex or difficult cases, the Exchange should publish its listing decisions detailing the facts and circumstances, any mitigating or aggravating factors considered, the Exchange's findings, the remedial actions taken by the issuer and any other sanctions imposed to send a stronger deterrent message to the market and help other issuers to avoid similar lapses in their disclosure and regulatory compliance controls and processes (paragraph 42).

(f) We also recommend that, in cases where the issuer shows bad faith (eg, a flagrant disregard for the Listing Rules or repeated breaches) or gross negligence, the Exchange adopt a stricter approach towards disciplinary sanctions to send a clear message to the market that such conduct is not tolerated. Save in exceptional circumstances, formal disciplinary proceedings should normally be brought in all such cases. When hearing the case, the Listing (Disciplinary) Committee should evaluate, amongst other things, whether the issuer remains suitable for listing given its inability to comply with such important Listing Rules. Amongst other things, the issuer should be required to demonstrate its ability and willingness to comply with all Listing Rule requirements (paragraph 43).

The Exchange's handling of issuers' unusual stock price and volume movements

The Exchange monitors stock price and trading volume movements daily to, amongst others, determine whether the issuer should publish an announcement to ensure that the market is properly informed. We reviewed the Exchange's processes and procedures for handling issuers' unusual stock price and volume movements, and a sample of cases.

(g) We recommend that the LIR department should update their desktop search on the issuer subject to an enquiry while the enquiry is pending, and maintain this monitoring for an appropriate time period after receiving a Negative Confirmation, before closing a case based on an issuer's Negative Confirmation (paragraph 62).

(h) We recommend that LIR staff be given more guidance regarding (i) the objectives of their monitoring and enquiries and (ii) matters that should be checked and considered in each enquiry (paragraph 63).

(i) We recommend that the relevant guidance and training for LIR staff be reviewed and, if needed, updated to highlight the importance of conducting critical assessment of the facts and circumstances of each case. We also recommend that the pre-set list of reasons in LIR's case database system for explaining their staff's decisions for closing a case be enhanced (paragraph 64).

(j) We recommend that the Exchange review its contact person(s) within each listed issuer to ensure that each issuer has designated at least one suitably senior employee with the requisite authority and knowledge of the issuer's business and affairs as the contact point to promptly respond to time-sensitive regulatory enquiries (eg, on unusual price movements) (paragraph 65).

The Exchange's vetting of IPO applications

The Exchange received a total of 187 and 136 new listing applications in 2022 and 2023, respectively. The number of applications vetted by the Listing Division in 2022 and 2023 were 361 and 249, respectively. We reviewed the IPO Vetting department's operational statistics in relation to its processing of IPO cases in 2022 and 2023, focusing on the time taken from the receipt of a listing application to the Listing Committee hearing. We also reviewed a sample of IPO cases that were considered by the Listing Committee during the review period.

(k) We noted that the time taken for the Exchange to issue first-round comments to listing applicants' sponsors was shortened during the review period, ie, the median time improved from 16 days[4] in 2022 to 12 days in 2023. The IPO processing time was longer in 2022 due to factors such as staff shortage (because of the high staff turnover in the previous year) and the large number of listing applications processed in 2022. The situation improved in 2023 as manpower shortage eased and the caseload stabilised (paragraph 73).

(l) The median time taken from the receipt of a listing application to the date of the Listing Committee hearing in 2022 and 2023 remained roughly the same at 149 days and 150 days, respectively, despite a reduction in the median total response time of the Exchange from 61 days in 2022 to 45 days in 2023. This was mainly due to an increase in sponsors' response time in 2023. The key factors affecting the IPO processing time, amongst others, are whether a listing application involves fundamental issues (such as suitability for listing) and whether the sponsor can satisfactorily address the Exchange's comments in a timely manner (paragraphs 74 to 77).

(m) The Exchange has implemented a suite of initiatives to enhance the efficiency and transparency of the IPO vetting process, including putting in place a mechanism to enable major issues identified by the vetting team to be escalated to the IPO Vetting department's senior management at an earlier stage of the vetting process and publishing more IPO-related operational statistics on its website (paragraphs 78 to 80).

(n) Subsequent to the review period, the SFC and the Exchange issued a joint statement on 18 October 2024 setting out an enhanced timeframe for the New Listing[5] application process (paragraph 81).

Follow-up from 2022 and 2021 reviews

(o) Following the publication of the Exchange's guidance letter on "Disclosure of the basis of consideration and business valuations in notifiable transactions" in October 2023, we noted from our review of sample cases that in the majority of the transactions, the issuers generally complied with the disclosure requirements set out in the guidance letter. In a small number of cases where no independent valuation was obtained, the disclosure on the basis of the transaction consideration appears to be insufficient. We recommend that the Exchange further improve issuers' disclosures and enhance its staff training for the vetting of these transactions (paragraph 86).

[4] References to "day" in this section denote business days.

[5] "New Listing" has the meaning ascribed to it in rule 1.01 of the Main Board Listing Rules (but excluding any new listing of interests in a REIT or any reverse takeover of a listed issuer which is a deemed new listing under the Listing Rules). The equivalent GEM rule is rule 1.01. For simplicity, references are made to a particular rule or chapter of the Main Board Listing Rules only. The GEM Listing Rules contain broadly equivalent rules.

(p) The Exchange has prepared internal guidance and provided staff training on review of placee lists via the Fast Interface for New Issuance (**FINI**) to assist its staff in vetting placee lists and identifying connected clients under the FINI system. Nevertheless, we observed that in isolated cases, the Exchange's staff failed to act on red flags relating to connected placees or overly relied on the independence confirmations provided by the applicant through the sponsor-overall coordinators without sufficient scrutiny. In some of these cases, significant issues were not escalated to senior personnel of the IPO Vetting department until a very late stage, thereby potentially affecting the clearance of the cases. We noted that the Exchange has enhanced its internal guidance to include a list of red flags based on past rejected consent applications and a compilation of novel issues to assist the IPO vetting staff to better identify problematic placees, and has provided additional training to its staff (paragraphs 90 to 92).

(q) With respect to listing policy initiatives, we noted that the minutes of the LOG Committee meetings have been enhanced to include the analysis presented by the Listing Division on public interest considerations and comments provided by the LOG Committee (paragraph 96).

(r) With respect to the management of conflicts of interest on the part of Listing Committee members and Listing Division staff, we noted that the internal guidance and procedures for the Listing Committee and the Listing Division have been revised to address our recommendations and Listing Compliance (renamed as Listing Operational Risk & Control) has conducted testing and review of the conflicts management processes of the Listing Division after the migration to the One-stop Processing and Approval System (**OPAS**) (paragraphs 98 and 99).

(s) The Exchange has implemented new processes, procedures and practices for the review of non-disciplinary matters to further address our recommendations from the 2021 review (paragraphs 101 to 104).

Review of the operations of the Listing Division in 2022 and 2023

(t) In recent years, Listing Enforcement continued to pursue more cases to maintain market integrity. In 2021, there began to be a notable increase in the number of disciplinary cases concluded, with a focus on how directors discharged their duties. Following the adoption of the revised sanctions framework, 42 unsuitability statements were imposed on directors in 2022 and 2023. In a case in 2023, two independent non-executive directors (**INEDs**) of a listed issuer received prejudice statements for serious failures to address the issuer's internal control deficiencies for an extended period of time. The decision sent an important message to the market about INEDs' duties to oversee listed issuers' Listing Rule compliance and corporate governance (paragraph 127).

Section 2

The Exchange's handling of issuers' non-compliance with the Listing Rule requirements on disclosure of material information

Introduction

10. We reviewed the Exchange's processes and procedures for handling cases where issuers failed to comply with the Listing Rule requirements on timely disclosure of material information, in particular Listing Rules relating to notifiable and connected transactions.

Relevant Listing Rule requirements

11. The Listing Rules require an issuer to publish an announcement as soon as possible after the terms of a notifiable transaction or connected transaction have been finalised[6]. For major or more significant transactions[7], an issuer is required to send a circular to its shareholders to seek their approval of the proposed transaction[8]. Connected transactions (ie, transactions that an issuer enters into with a controller or other connected persons of the issuer) are subject to similar requirements and must additionally be conditional on independent shareholders' approval[9] unless exempted (eg, because the transaction is *de minimis*)[10].

12. The Listing Rules also require an issuer to make an announcement where the amount of advances to an entity or financial assistance given to the affiliated companies of the issuer exceeds 8% under the assets ratio defined under rule 14.07(1)[11].

13. The notifiable and connected transaction rules are aimed at ensuring, amongst other things, that shareholders are properly informed about and have a collective say on significant transactions, and that all shareholders are treated fairly and equally when issuers enter into these transactions.

The Exchange's monitoring of issuers' compliance with the disclosure requirements and follow-up action on potential breaches

Monitoring and follow-up by LIR

14. According to the Exchange's internal procedures, when the LIR department suspects that a Listing Rule has been breached, it would (a) refer the incident to the Listing Enforcement department if it fits the referral criteria[12] or (b) if it decides that a case referral to Listing Enforcement is unwarranted or if Listing Enforcement does not accept the referral for investigation, consider issuing a warning letter or guidance

[6] Rules 14.34 and 14A.35.

[7] A transaction is regarded as (i) a major transaction if any of the percentage ratios (ie, assets ratio, consideration ratio, profits ratio, revenue ratio or equity capital ratio) is 25% or more, (ii) a very substantial acquisition if any of the percentage ratios is 100% or more, or (iii) a very substantial disposal if any of the percentage ratios is 75% or more. See rule 14.08.

[8] Rules 14.38A, 14.40, 14.48 and 14.49.

[9] Rule 14A.36.

[10] Rules 14A.73 and 14A.76. De minimis transactions are immaterial transactions that are conducted on normal commercial terms. A de minimis transaction is (i) fully exempt from the connected transaction rules if all the percentage ratios other than the profits ratio are less than 0.1%, and (ii) exempt from the circular and shareholders' approval requirements if all the percentage ratios other than the profits ratio are less than 5%.

[11] Rules 13.13 and 13.16.

[12] See paragraph 15.

letter[13] to the issuer and request, and follow up on, any appropriate remedial actions (eg, an internal control review) with the issuer[14].

15. The internal procedures provide that in considering whether a referral to Listing Enforcement is appropriate, the LIR department will consider the Exchange's duty to act in the interest of the public, having particular regard to the interest of the investing public, and the factors[15] set out in the Exchange's Sanctions Statement[16].

16. Under its existing policy, the Exchange can, in lieu of commencing formal disciplinary proceedings, issue a guidance letter or a warning letter to the issuer if it is satisfied that a Listing Rule breach has in fact occurred. Both types of letters are private letters issued to the issuer without any publicity or corporate announcement so the market is unaware of any such sanction by the Exchange. Warning letters, which can be issued either by LIR or by Listing Enforcement, are seen by the Exchange as a more serious penalty than guidance letters and need to be acknowledged, signed and returned by the relevant board members[17]. Both warning letters and guidance letters form part of the compliance record of the recipient.

Consideration by Listing Enforcement

17. The Listing Enforcement department is responsible for carrying out formal investigations of suspected breaches of the Listing Rules and, where applicable, for initiating and conducting disciplinary proceedings before the Listing (Disciplinary) Committee. Listing Enforcement has the discretion to issue a warning letter to an issuer instead of bringing proceedings before the Listing (Disciplinary) Committee.

18. The Enforcement Policy Statement[18], which outlines the Exchange's approach to enforcement of the Listing Rules and the criteria for assessing the appropriate level of enforcement action, provides that the Exchange's enforcement objectives are to deter future breaches, educate the market, influence compliance culture and attitude and enhance corporate governance.

19. According to the Statement, the Listing Enforcement department would focus its investigative resources on "cases where some form of public sanction may be warranted against the parties whose conduct is responsible for the breaches". The Listing Enforcement department's internal guidelines set out that, in deciding whether to accept a referral for investigation, the team will, amongst other things, be guided by the factors set out in the Enforcement Policy Statement[19].

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[13] See paragraph 16.

[14] As noted below, despite the guidance in the internal procedures, in practice LIR generally does not request or follow up on issuers' remedial actions. See paragraph 28.

[15] Including, amongst others, the compliance history of the parties, whether the parties fully assisted and cooperated with the Exchange in its investigation, whether the misconduct was negligent or intentional, whether the misconduct was an isolated instance or occurred over an extended period of time or repeatedly, whether the misconduct was an inadvertent oversight or was systemic or indicative of a pattern of non-compliance or relates to an internal control failure or deficiency, and whether the parties took steps to prevent any recurrence of the misconduct.

[16] Statement on Principles and Factors in Determining Sanctions and Directions Imposed by the Disciplinary Committee and the Listing Review Committee.

[17] See Consultation Paper on Review of Listing Rules Relating to Disciplinary Powers and Sanctions (August 2020).

[18] The Enforcement Policy Statement was first published by the Exchange in September 2013 and was last updated in July 2021.

[19] Including, amongst others, whether directors and other individuals responsible for the issuer's compliance and corporate governance cause or knowingly participate in a contravention of the Listing Rules, whether the issuer has appropriate and effective internal controls and culture for compliance and corporate governance, and whether the issuer and its directors cooperate with the Exchange's enquiries and investigations.

Cases reviewed

20. During the review period, the LIR department identified nearly 400 cases in which the issuers failed to comply with the Listing Rule requirements on timely disclosure of material information. Most of these cases involved a failure by listed issuers to comply with the announcement, circular and shareholders' approval requirements for either a notifiable transaction or a connected transaction[20]. An estimated one fourth of these cases involved breaches of the requirements for major or more significant transactions or connected transactions.

21. Only a small percentage of these cases were referred by LIR to Listing Enforcement for assessing whether a formal investigation should be commenced. The vast majority of the cases of non-compliance identified by LIR were disposed of by LIR issuing guidance letters to the relevant issuers.

22. We reviewed the case files for 22 cases, including (i) 13 cases that involved a failure by the issuers to obtain shareholders' approval for either a major or more significant transaction or a connected transaction, (ii) eight cases that involved a failure to announce either a discloseable transaction[21] or financial assistance given to affiliated companies, and (iii) one case that involved a failure to disclose other material information in a timely manner. Six of these issuers breached the relevant Listing Rules more than once in 2022 and 2023[22].

23. We assessed the actions taken by the LIR department in these non-compliance cases, including how the breaches were identified, how LIR assessed the rectification and remedial measures undertaken by the issuers and any other regulatory actions taken, including any referral to the Listing Enforcement department for investigation. We also reviewed Listing Enforcement's handling of the referrals from LIR.

Detection of non-compliance

24. The LIR department detected the issuers' non-compliance mainly through its post-vetting of issuers' financial reports and other corporate disclosures not directly related to the transactions in question[23]. A small number of cases were brought to LIR's attention because of media reports or self-reporting by the issuers in question.

Rectification of non-compliance and preventive remedial measures

25. Among the selected cases, 13 cases were more severe as they involved failures to obtain shareholders' approval either for major or more significant transactions or sizeable connected transactions. In five cases, the issuers published late announcements, despatched circulars and convened shareholders' meetings after the fact to ratify the transactions. In another six cases, late announcements were published but no subsequent shareholders' meeting was convened with the reason given being that the transactions had been completed or were ongoing and could not be unwound. In two cases, no announcement was published and no shareholders' meeting was convened despite the size and significance of the transactions in question.

[20] Other cases involved the failure to timely announce other material information, such as the receipt of a winding-up petition, the change of auditor or the indictment against a director.

[21] A transaction is regarded as a discloseable transaction if any of the percentage ratios is 5% or more but less than 25%.

[22] Including two issuers each committing three breaches and four issuers each committing two breaches.

[23] For example, in the course of reviewing some issuers' annual reports, LIR noted certain assets on the balance sheet, or impairment loss of loans on the income statement, and the acquisition of the assets or the making of the loans had not complied with the applicable announcement, circular or shareholders' approval requirements.

26. In the other nine cases, the Listing Rule breach was also serious in that the issuers failed to comply with the announcement requirements for discloseable transactions, financial assistance to affiliated companies or other material information. After the breaches were identified, in eight out of the nine cases, the issuers published late announcements. One issuer, however, took no action[24].

27. In most of the cases reviewed, the issuers submitted to the LIR department and/or included in their announcements the remedial measures that had been taken or proposed to be taken to prevent a recurrence of the breach. These measures usually included an internal review to enhance the issuers' internal control processes, and training to directors, senior management and staff. In a small number of the cases reviewed, the Exchange requested the issuers to provide some evidence of the implementation of the remedial measures, for example, by providing the amended internal control policies.

28. We were informed by the LIR department that the proposed remedial measures were volunteered by the issuers, and that in general LIR does not require an issuer to take any specific course of action, nor does LIR check on the implementation of the remedial measures proposed by the issuers. Instead, LIR's assessment focuses on whether the case should be referred to Listing Enforcement for investigation. When assessing appropriate regulatory actions, LIR would take into account the facts of the case in totality, including any remedial measures proposed by the issuer[25].

Regulatory actions taken against the breaches

29. Among the 22 cases reviewed by us, all of which involved suspected Listing Rule breaches that are considered to be serious, LIR referred eight cases to Listing Enforcement. Listing Enforcement accepted four of the eight referrals for investigation. In the four referrals that were rejected by Listing Enforcement, warning letters were issued instead. Some but not all of the warning letters reviewed by us included the reasons for Listing Enforcement's decision not to bring formal disciplinary proceedings.

30. In the other 14 cases that were not referred to Listing Enforcement, LIR issued guidance letters[26] to the issuers. These guidance letters routinely stated that the Exchange did not propose to take any further action given the particular circumstances of the matter and the material available to the Exchange. The letters normally included a summary of the facts and circumstances of the case without explicitly explaining the reasons or specific factors behind the Exchange's decision. These letters appear on their face to have limited deterrent effect on the recipient.

31. We noted that the majority of the 14 cases that were not referred to Listing Enforcement by LIR involved (i) a failure to announce and seek prior shareholders' approval for major or more significant transactions or sizeable connected transactions, or (ii) repeated breaches of the requirements to announce discloseable transactions or other material information. When asked why these cases were not referred despite the apparent severity of the Listing Rule breach, the LIR department responded that the decisions were based on a combination of factors, and that within the framework of

[24] LIR had concern as to the legitimacy of the transaction and referred the case to Listing Enforcement. The issuer only published an announcement upon the completion of an independent internal control review and investigation, more than one year after the relevant transaction was discovered.

[25] See footnote 15.

[26] We noted that LIR's internal procedures was amended in July 2023 to state that LIR staff has the discretion to issue warning letters; and LIR staff began to issue such letters in 2024.

the factors set out in the Exchange's Sanctions Statement[27], LIR may consider Listing Enforcement's caseload, available resources and assessment of the likelihood of success at the relevant time as Listing Enforcement may have communicated to LIR.

32. Besides the factors set out in the Enforcement Policy Statement[28], based on our review of the case files, we noted that Listing Enforcement would consider the following factors before deciding whether to accept a case for formal investigation:

    (a) the knowledge and involvement of the directors in the transactions in question;

    (b) whether there were suspected deficiencies in the issuers' internal control systems;

    (c) whether the issuer admitted the breach at an early stage;

    (d) whether the issuer has undertaken to take remedial actions to prevent similar breaches in the future;

    (e) whether the issuer has made some disclosure of the transactions in question; and

    (f) whether the issuer provided a reasonable explanation for the breach.

SFC observations

33. As noted above, based on the sample cases selected for review, only a small percentage of the breaches involving major or more significant transactions or sizeable connected transactions were referred to Listing Enforcement for formal investigation.

34. It is not unusual that only a selection of Listing Rule breaches are subject to disciplinary actions by the Exchange. It is notable, however, that (i) in three of the reviewed cases the issuers did not even publish a late announcement upon discovery of the relevant transaction[29], and (ii) six of the relevant issuers breached the Listing Rule requirements more than once in 2022 and 2023[30], indicating that those issuers were not sufficiently concerned about regulatory consequences.

35. Given (i) the particular importance of the notifiable and connected transaction rules in protecting the interests of public shareholders, (ii) the size of the transactions involved in those cases where no regulatory action was taken, and (iii) the high number of non-compliance by listed issuers during the review period, we recommend that the Exchange adopt measures designed to improve issuers' compliance and standards in these areas.

36. We recommend that LIR actively follow up with listed issuers to enhance their systems and controls in order to improve their ability to comply with these Listing Rules. LIR should ensure that (i) all issuers that commit such a material Listing Rule breach take appropriate action to prevent a recurrence and (ii) that the issuer appropriately addresses the weaknesses in its internal systems, processes and controls and remains suitable for listing.

[27] See paragraph 15.

[28] See footnotes 18 and 19.

[29] See paragraphs 25 and 26.

[30] See paragraph 22.

37. Accordingly, where a material breach[31] of the notifiable or connected transaction rules occurs, LIR staff should (i) carry out a thorough enquiry of the factors and circumstances to ascertain how and why the breach occurred, and (ii) require the issuer and its board of directors, working with its auditors and other professional advisors as necessary, to draw up a remedial course of action to review the issuer's internal controls for reporting notifiable and connected transactions to the board of directors. Upon discovery of a material breach, LIR staff should require the issuer to announce, as soon as practicable and subject to LIR's pre-vetting, (i) its failure to comply, (ii) a chronology of events and the failings or flaws that led to the breach (eg, any inadequacy or failure of the issuer's internal controls) so that the investing public are informed of these problems and risks within the issuer, and (iii) a date for publishing a remedial plan. Such a course of action should be taken by LIR regardless of whether a case is referred to Listing Enforcement as these separate actions serve different regulatory purposes.

38. Within a reasonable time period, the issuer should be required to submit its remedial plan for evaluation by LIR and obtain LIR's approval of the relevant announcement before publication. LIR should satisfy itself that the issuer has reasonably discharged its commitment to remedy the flaws in its internal controls. Where necessary, LIR should consider requesting that the issuer provide a certification from its chief executive officer, its chief financial officer and/or its auditors confirming that (i) all information required to be disclosed under the Listing Rules are recorded, processed, summarised and reported to the board of directors, and duly announced, within the time periods specified in the Listing Rules; and (ii) the relevant internal controls of the issuer, as amended and supplemented, are adequate and effective.

39. We further recommend that, for at least one full financial year after an issuer announces its remedial plan, LIR follow up at appropriate time intervals, and request the issuer to report on its implementation of the plan and to publicly announce any material change or deviation therefrom.

40. We also recommend that the Exchange review its existing policy on sanctions in these cases. As noted above, in most cases, the issuers that breached the Listing Rules received only a guidance or warning letter[32]; both are private letters issued without any publicity or corporate announcement so the market is unaware that the Exchange sanctions such Listing Rule breaches. Over time, this may foster a lax attitude among some issuers as to compliance with the Listing Rules.

41. The requirements of the relevant Listing Rules on notifiable and connected transactions are clear, and the fact that an issuer has failed to comply with those requirements can be established without a complex and prolonged investigation. Given the high number of non-compliance events found, we recommend that the Exchange, working in consultation with the LLF and the Listing Committee, review the current policy, system, processes and procedures for handling these types of Listing Rule breaches and impose meaningful sanctions more frequently to send a stronger deterrent message and reduce the incidence of such Listing Rule breaches among listed issuers.

42. For novel, complex or difficult cases, the Exchange should publish its listing decisions detailing the facts and circumstances, any mitigating or aggravating factors

[31] Generally speaking, all incidents of non-compliance involving a major or more significant transaction or a sizeable connected transaction should be considered serious except in unusual circumstances.

[32] See paragraphs 21, 29 and 30.

considered, the Exchange's findings, the remedial actions taken by the issuer and any other sanctions imposed. This would both send a stronger deterrent message to the market and help other issuers to avoid similar lapses in their disclosure and regulatory compliance controls and processes.

43. We also recommend that, in cases where the issuer shows bad faith (eg, a flagrant disregard for the Listing Rules or repeated breaches) or gross negligence, the Exchange adopt a stricter approach towards disciplinary actions and sanctions to send a clear message to the market that such conduct is not tolerated. Save in exceptional circumstances, formal disciplinary proceedings should normally be brought in all such cases. When hearing the case, the Listing (Disciplinary) Committee should evaluate, amongst other things, whether the issuer remains suitable for listing given its inability to comply with such important Listing Rules. Amongst other things, the issuer should be required to demonstrate its ability and willingness to comply with all Listing Rule requirements.

The Exchange's handling of issuers' unusual stock price and volume movements

Introduction

44. The Exchange has a duty under section 21 of the SFO to ensure, so far as reasonably practicable, an orderly, informed and fair market.

Relevant Listing Rule requirements and guidance

45. Rule 13.06 provides that the Exchange, in discharging its duty under section 21 of the SFO, will monitor the market, will make enquiries when it considers them appropriate or necessary, and may halt trading in an issuer's securities in accordance with the Listing Rules as required.

46. Pursuant to rule 13.09, if there is or is likely to be a false market[33] in an issuer's securities, the issuer must, as soon as reasonably practicable after consulting the Exchange, announce the information necessary to avoid a false market in its securities[34]. This obligation exists whether or not the Exchange makes enquiries. Amongst other tools, monitoring of stock price and trading volume, and media monitoring are used by the Exchange to assess whether a false market might have developed.

47. Rule 13.10 further provides that where the Exchange makes enquiries concerning unusual movements in the price or trading volume of an issuer's listed securities, the possible development of a false market in its securities or any other matters, the issuer must respond promptly and, if requested by the Exchange, make a relevant announcement.

48. Pursuant to rule 13.10A, where an issuer has information which must be disclosed under rule 13.09 or inside information which must be disclosed under the SFO but cannot make an announcement promptly, the issuer must apply for a trading halt or a

[33] The term "false market" refers to a situation where there is material misinformation or materially incomplete information in the market which is compromising proper price discovery. Examples include where an issuer has made a false or misleading announcement, there is other false or misleading information including a false rumour circulating in the market, an issuer has undisclosed inside information, or a segment of the market is trading on the basis of undisclosed inside information. See Frequently Asked Questions Series 22 (released on 30 April 2013, last updated in December 2023).

[34] The issuer must also announce inside information required to be disclosed under the SFO.

trading suspension. The Exchange also reserves the right to direct a trading halt if an announcement under rule 13.10 cannot be made promptly[35].

49. The Exchange has provided guidance[36] to issuers which are the subject of market commentaries or rumours which have, or could have, caused intense price pressure in their listed securities. Issuers should announce information to clarify matters where, in the view of the Exchange, there is a possible development of a false or disorderly market in its securities, or apply for a trading halt if it cannot promptly publish the clarification announcement.

50. Rule 6.05 provides that the duration of any trading halt or suspension should be as short as possible and it is the issuer's responsibility to ensure that trading in its securities resumes as soon as practicable following the publication of an appropriate announcement[37].

51. Following the publication of the clarification announcement, the Exchange may continue to follow up with the issuer on any further disclosures, reviews or investigations it considers necessary, including requiring the issuer to support its responses to the allegations and demonstrate proper internal controls and risk management measures. Where the follow-up action reveals that any issuer announcement or document was materially inaccurate or misleading, or that there are serious concerns about the issuer's compliance with the Listing Rules, the Exchange may suspend the issuer's share trading pending further clarification and may make a referral to an appropriate law enforcement agency (eg, the SFC).

The Exchange's monitoring of unusual stock price and volume movements

52. According to the Exchange's internal procedures, the LIR department receives an alert when a stock price movement and trading volume exceed a pre-set threshold. Upon receiving an alert, the LIR department will search for news on the issuer and consider, amongst other things, the issuer's recent announcements, recent price and trading volume movements and any media reports.

53. The focus of LIR's monitoring at this stage is to determine whether the situation is such that the issuer should publish an announcement to ensure that the market is properly informed. If the facts and circumstances give rise to a concern that the issuer may possess unpublished inside information or that a false market may be developing, the LIR department will contact the issuer to ask (i) whether it is aware of any reason for the significant price or volume movement, (ii) whether it is in possession of any undisclosed inside information, and (iii) if the unusual price movement is downward, whether the issuer is aware of any forced disposal of shares held by any director as a result of share pledges made with a lender.

54. According to the Exchange's internal procedures, if the issuer confirms to the Exchange that it is not aware of any particular reason for the significant price or trading volume movement and does not possess any undisclosed inside information (**Negative Confirmation**), and the Exchange is satisfied that there is no concern that a false market may be developing, trading in the issuer's securities will be allowed to

[35] Note 3 to rule 13.10. See also Practice Note 11.

[36] Guidance for issuers subject to market commentaries or rumours, HKEX-GL87-16 (April 2016).

[37] Under the Exchange's Guidance on trading halts, HKEX-GL83-15 (updated in May 2024), issuers are expected to establish procedures to actively monitor their share price and any news, comments or reports relating to them, and have in place an appropriate delegation of authority to allow for timely release of information to the Exchange and the public.

continue while the Exchange keeps monitoring any further price or trading volume movement.

Cases reviewed

55. During the review period, the LIR department received a large number of alerts on significant stock price and volume movements and made more than 700 enquiries with issuers. Among these cases:

    (a) In 42 cases, trading was halted pending the publication of the relevant announcement.

    (b) In 27 cases, announcements were published at LIR's request without a trading halt.

    (c) In 12 cases, the issuers provided Negative Confirmation upon LIR's enquiry on the unusual stock price and volume movements but, shortly after the enquiries, published announcements which raised concerns on the issuer's compliance with the relevant rule requirements or the SFO. LIR made further enquiries with the issuers[38].

    (d) In six cases, referrals were made to the SFC for suspected breaches of the SFO.

    (e) In the remaining cases, the issuers provided Negative Confirmation upon LIR's enquiry and LIR had no regulatory concern with the issuers' compliance with the relevant rule requirements or the SFO.

56. We reviewed the case files of 17 cases to understand the Exchange's approach in the monitoring of unusual stock price and trading volume movements and its enquiries and follow-up actions. We also reviewed the Exchange's processes and procedures for handling unusual stock price and volume movements. For the avoidance of doubt, the selected cases may not be representative of the approach taken in relation to all unusual movement alerts. The cases highlighted for discussion below illustrate the key issues that we consider the Exchange should be mindful of when handling such cases.

Enquiries upon receiving unusual movement alerts

57. As stated above, upon receiving a significant movement alert, the LIR department will make an enquiry with the issuer if there are other facts and circumstances that give rise to a concern that the issuer may possess unpublished inside information or that a false market may be developing[39]. If the case officer decides that an enquiry is unnecessary, the basis for the decision is recorded in the case database by selecting from a pre-set list of reasons[40]. We noted that, in a few of the cases reviewed, LIR did not make any enquiry despite large stock price movements because "the pricing or

[38] In 58 other cases, the issuers provided Negative Confirmations upon LIR's enquiries and published voluntary announcements afterwards. These announcements generally contained the issuers' Negative Confirmations on the unusual price and volume movement, or clarification of media news or reports, and did not raise LIR's concern on the issuers' compliance with relevant disclosure requirements.

[39] See paragraph 53.

[40] The pre-set reasons include, amongst other things, pricing or volume threshold not triggered, announcement made recently and others. The Exchange informed us that there are no numerical thresholds for the reasons and the LIR case officers decide whether an enquiry is necessary on a case-by-case basis.

volume threshold was not triggered" or "no relevant news was noted". These reasons in the pre-set list did not adequately explain the "no-further-action" decision taken at the time by LIR staff.

58. The LIR department's enquiries are normally conducted verbally with the issuer's authorised representative and it would usually rely mainly on the response provided by the issuer to decide that no further action is needed.

59. In one case, the issuer's share price fell by more than 20% with significant trading volume. LIR made an enquiry with the issuer's authorised representative and received a Negative Confirmation within two hours[41]. While LIR's enquiry was pending, articles appeared on the internet alleging that the issuer had disclosed its target profit, which was below market expectation, to a selected group of audience. The LIR department did not notice the emergence of the internet articles and took no further action after receiving the issuer's Negative Confirmation[42].

Further follow-up actions

60. When an issuer provided Negative Confirmations to the Exchange and subsequent development (such as announcements published by the issuer) gave rise to a suspected breach of the issuer's disclosure obligations or other irregularities, we noted that the Exchange followed up appropriately and referred six cases to the SFC for potential breaches of the SFO. In a few cases, however, the Exchange did not follow up on suspected breaches such as late disclosure of material information or internal control deficiencies.

61. In one case, the issuer's share price plunged by more than 90% on one day and rebounded by more than 300% in aggregate during the following three days. During this four-day period, the issuer provided two Negative Confirmations in response to LIR's enquiries. On the day after the four-day period, the issuer unexpectedly published a profit warning disclosing an expected loss and, on the next business day, published its interim results. In response to LIR's further enquiries on the issuer's compliance with its disclosure obligations with respect to the loss, the issuer replied that the first draft of its consolidated accounts only became available on the date of the profit warning announcement and that its directors had been unaware of the "expected" loss before then. The Exchange did not question the implausible submission, nor did it follow up on the issuer's admission that it failed to provide its directors with the monthly update in a timely manner[43].

SFC observations

62. The Exchange's internal procedures require the LIR staff to look for news on the issuer upon receiving a significant movement alert to decide whether an enquiry with the issuer is necessary[44]. However, there are no guidelines on whether the staff should conduct further searches, whether while an enquiry is pending or after a Negative Confirmation is received from the issuer, before deciding to take no further

[41] The authorised representative was a member of an external corporate support service provider and had no personal knowledge of the issuer's affairs. To address LIR's enquiry, the authorised representative had to contact the issuer's internal personnel and await their response for an extended time. The LIR staff made multiple follow-up calls to the authorised representative in light of the delay. Based on the record, there also appeared to be certain miscommunication when the authorised representative relayed the information received from the issuer's internal personnel to LIR staff.

[42] The next day the issuer published an announcement seeking to clarify the content of the online articles. In light of the announcement, LIR department made enquiries with the issuer subsequently.

[43] See Corporate Governance Code, Part 2, D.1.2.

[44] See paragraph 52.

action[45]. We recommend that the LIR department should update their desktop search while an enquiry is pending, and maintain this monitoring for an appropriate time period after receiving a Negative Confirmation, before closing a case based on an issuer's Negative Confirmation.

63. In addition, there are no guidelines on how LIR staff should evaluate an issuer's response to its follow-up enquiries to determine whether further regulatory action is necessary. The case discussed in paragraph 61 above is an instance where the Exchange failed to follow up on suspicious circumstances. We recommend that LIR staff be given more guidance regarding (i) the objectives of their monitoring and enquiries and (ii) matters that should be checked and considered in each enquiry.

64. LIR staff exercise a fair amount of discretion and judgment when deciding whether an enquiry should be made upon receiving an unusual movement alert. We recommend that the relevant guidance and training for LIR staff be reviewed and, if needed, updated to highlight the importance of conducting critical assessment of the facts and circumstances of each case. We also recommend that the pre-set list of reasons in LIR's case database system be enhanced to address the observation in paragraph 57 above.

65. Listed issuers should ensure that the person(s) whom they appoint as authorised representatives are able to respond promptly and appropriately to enquiries from the Exchange[46]. We noted a case where the authorised representative was an external service provider that was unfamiliar with the issuer's day-to-day affairs and this resulted in undue delay and misunderstanding in the issuer's communication with the Exchange[47]. We recommend that the Exchange review its contact person(s) within each listed issuer to ensure that each issuer has designated at least one suitably senior employee with the requisite authority and knowledge of the issuer's business and affairs as the Exchange's contact point to promptly respond to time-sensitive regulatory enquiries (eg, on unusual price movements).

The Exchange's vetting of IPO applications

Introduction

66. The Exchange's IPO Vetting department is responsible for processing listing applications and providing guidance to listing applicants or their advisers seeking clarification on listing matters.

IPO vetting process

67. New listing applications filed with the Exchange are routed to the IPO Vetting department to decide whether to accept the application for vetting. Rule 9.03(3) provides that the information in the listing application must be substantially complete except in relation to information that by its nature can only be finalised and incorporated at a later date. If the IPO Vetting department decides this information is not substantially complete, it will not continue to review any documents relating to the application.

68. After the application is accepted for vetting, if the relevant vetting team identifies any material issues, for example, regarding the eligibility and/or suitability for listing or

[45] See paragraph 59.
[46] See footnote 37.
[47] See footnote 41.

disclosure in the prospectus, the team will issue comment letters to the listing applicant's sponsor, who will be given an opportunity to address the matter and make the necessary corrections in the prospectus.

69. As stated on the Exchange's website, (i) there is no pre-set timeframe for a listing timetable, which will depend on the applicant's response time and quality of response; and (ii) first round of comments will generally be provided within 15 business days from the receipt of the application.

70. If more than six months have lapsed since the date of a listing application and the listing applicant wishes to continue its listing exercise, it will have to submit a new listing application.

Operational statistics and cases reviewed

71. The Exchange received a total of 187 and 136 new listing applications in 2022 and 2023, respectively. The number of applications vetted by the Listing Division in 2022 and 2023 were 361 and 249, respectively.

72. We reviewed the IPO Vetting department's operational statistics in relation to its processing of IPO cases in 2022 and 2023. The focus is on the time taken from the receipt of a listing application to the Listing Committee hearing as any subsequent launch of an IPO would often depend on market conditions. We also reviewed a sample of IPO cases that were considered by the Listing Committee in 2022 and 2023 to understand the department's approach to vetting listing applications.

SFC observations

IPO case processing time

73. We noted that the time taken for the Exchange to issue first-round comments was shortened during the review period. The median time for the issuance of first-round comments by the IPO Vetting department improved from 16 business days in 2022 to 12 business days in 2023. The IPO Vetting department explained that (i) the longer processing time in 2022 was mainly due to a shortage of staff as a result of high staff turnover in 2021 and a large number of listing applications processed in 2022 (including a backlog of cases brought forward from 2021), and (ii) the improvement in 2023 was mainly attributable to an easing of manpower shortage and caseload as well as training of new staff members.

74. The median time taken from the receipt of an application to the date of the Listing Committee hearing (**Time to Hearing**) in 2022 and 2023 was 149 and 150 business days, respectively, despite a reduction in the median total response time of the IPO Vetting department from 61 business days in 2022 to 45 business days in 2023. This was mainly due to an increase in the response time of sponsors in 2023.

75. The IPO Vetting department explained that one key underlying driver for the Time to Hearing is whether a listing application involves fundamental issues, such as suitability for listing, and whether the sponsor can satisfactorily address the Exchange's comments in a timely manner. If the sponsor fails to address the issues within the 6-month application period, a new listing application will be needed. In some cases, new developments may also lengthen the process, such as a deterioration of financial performance identified in the updated listing document.

76. The IPO Vetting department further explained that the length of the overall IPO vetting process also depends on other factors, for example, whether an applicant has provided sufficient information in its application materials and the quality of the sponsor's responses to the Exchange's comments.

77. This is consistent with our observations in reviewing the sample cases. For example, in one case, the quality of the sponsor's responses to the Exchange's comments was found to be substandard, leading to the issue of two "incomplete reply" emails[48] by the Exchange to the sponsor. On the first occasion, the sponsor took almost two months to submit a partial response to only one specific comment without addressing the other comments. On the second occasion, the sponsor failed to fully address the Exchange's comments in several areas, including the applicant's business model, tariff-related risks and the relationship between the listing applicant and a major customer, resulting in a delay in the process.

Efforts to enhance efficiency and transparency

78. We noted that the IPO Vetting department has implemented a suite of initiatives to enhance the efficiency and transparency of the IPO vetting process. For example, an internal meeting with the department's senior management is held at an earlier stage of the vetting process so that major issues identified by the case team can be escalated to senior management more promptly. In addition, the department's internal monthly progress reports have been enhanced to facilitate senior management's monitoring of the key operational metrics.

79. To enhance transparency, the Exchange has published more operational statistics in relation to the IPO vetting process on its website[49]. In addition, to facilitate the market's understanding of the Listing Rules and preparation for filing a listing application, the Exchange published the Guide for New Listing Applicants in November 2023 (with an updated version published in August 2024), which consolidated and rearranged the Exchange's various guidance letters, listing decisions and frequently asked questions (**FAQ**) on IPO-related matters.

80. Whilst improving efficiency remains a focus of the Exchange, the IPO Vetting department emphasised that it has adopted appropriate procedures and measures to control the quality of the vetting process and uphold the gatekeeping function in its daily work.

Subsequent development

81. Subsequent to the review period, the SFC and the Exchange issued a joint statement on 18 October 2024 setting out an enhanced timeframe for the New Listing application process. The enhanced timeframe provides more clarity and certainty regarding the timing and rounds of comments from both regulators, as well as enhanced transparency in the application process for New Listing applications.

[48] The Exchange indicated in these two emails that the IPO Vetting department would not review the sponsor's submission until a full submission that could satisfactorily address all of its comments was submitted.

[49] On the last trading day of each month, the Exchange updates the progress report for new listing applications on its webpage which sets out, amongst other things, the number of comment letters issued in respect of IPO applications in each month and the median of business days taken by the Exchange for issuing the first comment letter. See https://www2.hkexnews.hk/New-Listings/Progress-Report-for-New-Listing-Applications/Main-Board?sc_lang=en.

Section 3

Follow-up from the 2022 and 2021 reviews

Follow-up from the 2022 review

82. In our 2022 review, we reviewed the Exchange's performance in its regulation of listing matters during 2021. We identified a few areas for potential improvement and made recommendations for the Exchange to consider. This section discusses the steps taken by the Exchange in response to our recommendations in the 2022 review report.

The Exchange's review of business valuations in connection with major (or larger) acquisitions and disposals

83. We reviewed the Exchange's processes and procedures for reviewing business valuations in connection with major (or larger) acquisitions and disposals.

84. Our review noted that the Listing Rules do not specify how and to what extent the bases for the agreed consideration, including any business valuation, should be described. In a number of cases reviewed, there appeared to be significant variations in the types and quality of the information disclosed in the circulars. We recommended that the Exchange take steps to improve the disclosure and other practices among listed issuers in this regard.

SFC observations

85. In October 2023, the Exchange published a guidance letter[50] setting out the information that is expected to be disclosed by a listed issuer on (i) business valuations which form a primary factor in determining the consideration and (ii) the basis of the consideration regardless of whether an independent valuation is disclosed. LIR staff were provided with training, which covered the guidelines and illustrative examples to facilitate their vetting of business valuations.

86. We reviewed the circulars for a sample of major (or larger) transactions which were issued since the publication of the new guidance letter. In the majority of these transactions, issuers generally complied with the disclosure requirements set out in the guidance letter. In a small number of cases where no independent valuation was obtained, the disclosure on the basis of the transaction consideration appeared to be insufficient. We recommend that the Exchange further improve issuers' disclosures and enhance its staff training for the vetting of these transactions.

The Exchange's administration of the IPO Placing Guidelines and review of the IPO placee lists

87. We reviewed the Exchange's processes and procedures for reviewing the IPO placee lists and monitoring compliance with the Placing Guidelines for IPOs by intermediaries, as well as its criteria for granting consent for share allocations to specified persons under the Placing Guidelines, including "connected clients" and the listing applicant's directors and existing shareholders or their close associates.

[50] Disclosure of the basis of consideration and business valuations in notifiable transactions, HKEX-GL116-23 (updated in June 2024).

88. We noted amongst others that:

(a) there was no systematic process for reviewing the IPO placee lists which would enable the Exchange to identify "problematic" (eg, controlled) placees in a timely manner. In some cases, the pertinent issues relating to the placee lists submitted to the Exchange were dealt with at a late stage in the vetting process, thereby requiring last-minute changes to the IPO share allocations. In addition, when processing applications for its placing consent, the Exchange mainly relied on confirmations of independence provided by relevant parties without further scrutiny; and

(b) the Exchange's written procedures and training materials did not contain sufficient guidance on the factors which should be taken into consideration when assessing the independence or genuineness of the placee or when processing applications for the Exchange's consent for placing to connected clients.

89. We recommended that the Exchange review its internal guidance on the vetting of placee lists and allotment results announcements taking into consideration the new processes and protocols under FINI to further enhance the efficiency and effectiveness of the placee vetting process. In the longer run, the Exchange should consider whether it is possible to introduce new features in FINI to help identify notable red flags such as those revealed in past cases. The Exchange should also put in place appropriate procedures for reviewing the independence confirmations received in support of applications for placing consent. In addition, the monitoring of case progress by senior personnel of the IPO Vetting department should be enhanced. The Exchange's training materials should be updated to take account of the above changes.

SFC observations

90. FINI began operation in November 2023. We were informed by the Exchange that before FINI was launched, staff training sessions were conducted to familiarise staff with the relevant process and procedures. After the launch, an additional staff training session was conducted in January 2024 on review of placee lists via FINI and post-launch observations. The training materials covered, amongst others, the practices and procedures for vetting placee lists via the FINI platform, the FINI timeline, guidelines on processing issuers' application for the Exchange's consent or waiver for placings to connected clients or existing shareholders or their close associates, and identification of red flags. In addition, the training materials included more case studies to assist the Listing Division staff in vetting the placee lists and identifying connected clients.

91. In February 2024, the Exchange's internal guidance was updated to reflect the new processes and protocols under FINI[51] and codify the Exchange's practices relating to the assessment of placee independence. The guidance includes a reminder to staff to ensure that the Exchange's consent for placings to connected clients or relevant waivers for placings to existing shareholders or their close associates should be sought in advance, and to refer to the Guide for New Listing Applicants[52] and internal training materials. The internal guidance also specifies detailed checkpoints for the IPO vetting staff to report case progress to the Co-Heads of the IPO Vetting department.

[51] The FINI platform is accessible to staff of all levels within the IPO Vetting department (ranging from junior staff to the Co-Heads), thereby enabling senior personnel to review the status of a listing application or the placee lists at any time.

[52] See paragraph 79.

92. Nevertheless, we observed that in isolated cases the Exchange's staff failed to act on red flags relating to connected placees or overly relied on the independence confirmations provided through the sponsor-overall coordinators without sufficient scrutiny. In some of these cases, significant issues were not escalated to senior personnel of the IPO Vetting department until a very late stage, thereby potentially affecting the clearance of the cases. We noted that the Exchange has enhanced its internal guidance to include a list of red flags based on past rejected consent applications and a compilation of novel issues to assist the IPO vetting staff to better identify problematic placees, and has provided additional training to its staff.

The Exchange's processes and procedures in respect of (i) the LOG Committee, (ii) the Listing Compliance function and (iii) the management of conflicts of interest on the part of Listing Committee members and Listing Division staff in handling cases

93. We reviewed the Exchange's processes and procedures in respect of (i) the LOG Committee, (ii) the Listing Compliance function and (iii) the management of conflicts of interest on the part of Listing Committee members and Listing Division staff in handling cases. Our key observations and recommendations are set out below.

Listing Operation Governance Committee

94. We noted that the LOG Committee was established to assist the HKEX Board in overseeing the management and operations of the Listing Division. The former Head of Listing and the Chairman and Deputy Chairmen of the Listing Committee were of the view that: the discussions at the LOG Committee meetings were effective; the HKEX Board through the LOG Committee has gained a better understanding of the Listing Division's operations; and the communication between the HKEX Board on the one hand and the Listing Division and the Listing Committee on the other has been enhanced.

95. The LOG Committee's terms of reference require it to provide guidance to the Listing Division and advise the HKEX Board on the discharge of HKEX's and the Exchange's obligations to act in the interest of the public in listing policy development. Given the short history of the LOG Committee, its track record had yet to be developed. We recommended that the minutes of the LOG Committee meetings be more detailed to provide a fair and accurate summary of the public interest considerations and issues presented to the LOG Committee by the Listing Division as well as the analysis considered and discussed and any conclusions reached.

SFC observations

96. We noted that with respect to listing policy initiatives, the minutes of the LOG Committee meetings have been enhanced to include the analysis presented by the Listing Division on public interest considerations and comments provided by the LOG Committee.

The management of conflicts of interest on the part of Listing Committee members and Listing Division staff in handling cases

97. We recommended that, amongst others:

(a) the Listing Committee Handbook should be enhanced to provide more detailed guidance on potential conflict situations, in particular to include common

examples of relationships which are not directly related to the specific matter being considered by the committee but may nonetheless be perceived as affecting the impartiality of a member;

(b) in respect of the amendment to the procedures which require members to update the Listing Committee on new conflicts that arise throughout the process of a case, the guidance should clarify that, in the context of IPO applications, a member should be excluded from receiving relevant papers or participating in committee discussions once his or her firm has commenced cornerstone investment discussions with the listing applicant. The member should also confirm to the Exchange that the investment (if entered into after the member receives the relevant papers or participates in any committee discussion of the listing application) was not based on non-public information obtained by virtue of his or her participation in the matter as a committee member;

(c) to address perception issues, declarations of potential conflicts by the Head of Listing should be routinely referred to HKEX Group Compliance; and

(d) Listing Compliance should continue to monitor and test the effectiveness of the conflict management controls, processes and procedures of the Listing Division and the operational departments after the migration to OPAS.

SFC observations

98. The Listing Committee Handbook has been amended to include more detailed guidance on potential conflict situations. The Listing Division's conflicts management procedures have also been revised to provide that declarations of potential conflicts of interest by the Head of Listing will be assessed by HKEX Group Compliance.

99. Listing Compliance (renamed as Listing Operational Risk & Control) has conducted testing and review of the conflicts management processes of the Listing Division after the migration to OPAS and recommended certain enhancements.

Further follow-up from the 2021 review

100. In the 2021 report, we reviewed the Exchange's handling of review hearings for non-disciplinary listing matters. In the 2022 report, we noted that the Exchange had implemented new processes, procedures and practices for the review of non-disciplinary matters to address our recommendations from the 2021 review. We recommended further enhancements in the following areas:

(a) the Exchange should further shorten the time period for holding the rehearing after the Listing Review Committee (**LRC**) remits a case to the Listing Committee and improve the efficiency of the review hearing process in general;

(b) the LRC should ensure that when it overturns a Listing Committee decision, the key elements of the overturned decision are adequately addressed in the LRC's decision; and

(c) the Exchange should take action to ensure that the LRC adheres to the Exchange's published listing guidance.

SFC observations

101. We were informed by the Exchange that the processes and procedures for rehearings by the Listing Committee of remitted cases have been adjusted. Unlike the previous practice where the review parties were invited to make new submissions to the Listing Committee for the rehearing, under the new procedures, rehearings would be conducted on the basis of the same submissions presented to the LRC together with the LRC decision[53]. Rehearings are generally expected to be scheduled around four weeks after the LRC decision[54].

102. In addition, since April 2024 the Exchange has streamlined the processes for making review submissions to the LRC and preparing hearing bundles. The average time lapse between the receipt of the review application and the LRC hearing has been shortened from 80 days in 2023 to 45 days since April 2024.

103. The Exchange informed us that it has strengthened the training provided to LRC members. The LRC Secretary has assumed an active role to ensure the LRC is aware of and considers all relevant Listing Rules and guidance when exercising its discretion in deciding a case. Senior members of the Listing Division are available to provide explanation and advice to the LRC for more complex or nuanced legal, Listing Rule or procedural issues.

104. We noted that following our 2022 review, when the LRC overturned the Listing Committee's decisions, in most cases, the LRC included adequate explanations for the difference between its decisions and those of the Listing Committee and followed the Exchange's published guidance.

[53] In the unusual circumstances that any of the parties considers a further submission is necessary and appropriate, such further submissions must be filed within 14 days from the notification of the rehearing date to the parties.

[54] Since the publication of our 2022 review report, no case has been remitted by the LRC to the Listing Committee.

Section 4

Review of the operations of the Listing Division in 2022 and 2023

Overview

105. The following table summarises the operational activity reported by the Exchange in its listing regulation for 2019, 2020, 2021, 2022 and 2023[55].

	2019	2020	2021	2022	2023
Number of listing applications accepted for vetting by the IPO Vetting department	300	231	316	187	136
Number of listing applications processed by the IPO Vetting department[56]	N/A	N/A	N/A	361	249
Number of listing applications approved by Listing Committee	179	148	118	126	72
Number of compliance and monitoring actions handled by the LIR department[57]	73,704	82,228	82,227	67,279	72,036
Number of investigations handled by the Enforcement department	112	128	164	141	123
Number of Listing Decisions published	3	6	2	7	0
Number of Guidance Letters published	7	3	1	4	4
Number of FAQs published	7 series	2 series	2 series	5 series	3 series
Number of other guidance materials published	2	7	6	3	5
Number of listing applications processed by the Structured Products and Fixed Income department[58]	33,671	50,167	59,491	46,891	30,818
- Derivative warrants	8,939	12,128	16,684	11,874	7,967
- Callable Bull/Bear Contracts (more commonly known as CBBCs)	24,732	38,039	42,807	35,017	22,851

[55] Sources: HKEX 2022 and 2023 Annual Reports and Listing Committee reports 2019-2023.

[56] The number comprises new listing applications accepted in the current year, listing applications brought forward from the previous year, and renewal applications accepted within three months following a lapsed application by the same applicant. The information for the "number of listing applications processed by the IPO Vetting department" is only available for 2023 and 2022 due to a change in the disclosure details in HKEX's 2023 Annual Report.

[57] Compliance and monitoring actions include announcements and circulars vetted, share price and trading volume monitoring actions undertaken and complaints handled.

[58] The figures refer to issues of new structured products and do not include further issues.

IPOs

106. The number of listing applications accepted for vetting by the Exchange in 2023 was 136, representing a decrease of 51 (or 27.3%) from 187 in 2022.

107. The number of listing applications processed by the Exchange in 2023 was 249, down by 112 (or 31%) from 361 in 2022. Please refer to Section 2 for the relevant statistics on the processing time of IPO cases.

108. In 2023, the IPO Vetting department published two guidance letters (2022: three) and did not publish any listing decisions (2022: five)[59]. In November 2023, the Listing Division published a Guide for New Listing Applicants (with an updated version published in August 2024), which consolidated and rearranged all existing guidance letters, listing decisions and FAQs on IPO-related matters.

Listed issuer regulation

109. The number of LIR actions handled by the Exchange was 72,036 in 2023 (2022: 67,279), representing an increase of 4,757 (or 7.1%) in 2023. The following is a breakdown of the announcements handled by the LIR department in 2022 and 2023.

	Post-vetted	% of total	Pre-vetted	% of total	Total
2022	55,874	99.86	80	0.14	55,954
2023	62,517	99.90	61	0.10	62,578

110. The LIR department referred 39 cases to Listing Enforcement in 2023, down 45% from 71 referral cases in 2022. Referrals to external regulatory bodies[60] decreased by 13% from 46 cases in 2022 to 40 cases in 2023.

111. In terms of turnaround time, the Exchange:

(a) post-vetted results announcements within three business days of publication in 97% of the cases in 2023 (2022: 99%);

(b) post-vetted other announcements within one business day of publication in 96% of the cases in 2023 (2022: 99%); and

(c) pre-vetted announcements[61] within the same day in 95% of the cases in 2023 (2022: 95%).

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[59] Guidance Letters: "Guidance for Overseas Issuers" (January 2022), "Guidance on Special Purpose Acquisition Companies" (January 2022), "Guidance on the qualifications and obligations of a trustee / custodian regarding the operation of the escrow account of a SPAC" (March 2022), "Guidance on Specialist Technology Companies" (March 2023) and "Guidance on the electronic submission of prospectus and accompanying documents to the Exchange and the Companies Registry for authorisation and registration" (December 2023). Three of these guidance letters (the first, second and the last) were published jointly by the IPO Vetting department and the LIR department.

Listing Decisions: "To provide guidance on why the Exchange considered certain proposed applicants have not demonstrated their suitability to list with a WVR structure" (September 2022), "Whether Product X (being one of Company A's Core Products) which completed the Phase 1 clinical trials under the Therapeutic Goods Administration in Australia and subsequently obtained approval from both the European Medicines Agency and the National Medical Products Administration to commence the global pivotal Phase 2/3 clinical trial satisfies the relevant core product eligibility requirements under GL92-18 and Chapter 18A of the Main Board Rules" (May 2022), "Whether Company X is suitable for listing in light of (a) the prolonged deterioration of financial performance of its Core Businesses; (b) the limited track record of its new services and temporary business improvement; and (c) the failure to prove its business improvement plans" (May 2022), "Whether Company X is suitable for listing in light of the material reliance on Dr. A" (May 2022) and "Whether each of Mr. A and Mr. B is suitable to act as a director of an issuer in light of bribery incidents" (May 2022).

[60] The SFC, the Accounting and Financial Reporting Council and other regulatory bodies.

[61] These primarily comprised announcements made in relation to very substantial acquisitions, very substantial disposals, reverse takeovers and cash companies, which are required to be pre-vetted by the Exchange under the Listing Rules.

112. In 2023, the LIR department issued three guidance letters (2022: three) but did not issue any listing decision (2022: two)[62].

113. The Exchange reported that, in 2023, it continued its initiative to promote self-compliance by listed issuers with the Listing Rules. This initiative was pursued primarily through issuing guidance letters, information paper, Listed Issuer Regulation Newsletters, Enforcement Bulletins and publishing corporate governance materials as well as launching e-training module.

SFC observations

114. As noted above, the caseload of the IPO Vetting department decreased by 31% in 2023 (see paragraph 107) while the number of LIR actions handled by the LIR department increased by 7.1% (see paragraph 109).

115. During the review period:

(a) the time taken to issue first-round comments on IPO applications was shortened (see paragraph 73), and the median time taken from the receipt of application to the date of Listing Committee hearing remained at a similar level (see paragraph 74); and

(b) the proportion of results announcements post-vetted within three business days and the proportion of other announcements post-vetted within one business day fell slightly in 2023, and the proportion of announcements pre-vetted within the same day remained the same in 2023 (see paragraph 111).

116. During 2023, the IPO Vetting department issued two guidance letters but did not issue any listing decision (see paragraph 108), while the LIR department issued three guidance letters but did not issue any listing decision (see paragraph 112).

117. Referrals from the LIR department to Listing Enforcement decreased by 45% from 71 cases in 2022 to 39 cases in 2023. The Exchange explained that, during the review period, breaches of the connected transaction rules were handled mainly by issuing guidance letters. In addition, there was a decrease in referral cases relating to breaches of directors' fiduciary duties involving audit issues or problematic transactions as the market is better informed of a director's role in a transaction.

Investigation and enforcement

118. In 2023, the Exchange published two Enforcement Bulletins (2022: two)[63] and a new guide to highlight the key responsibilities and obligations of INEDs.

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[62] Guidance Letters: "Guidance on special purpose acquisition companies" (January 2022), "Change of listing status from secondary listing to dual-primary or primary listing on the Main Board" (January 2022), "Guidance for overseas issuers" (January 2022), "Disclosure of the basis of consideration and business valuations in notifiable transactions" (October 2023), "Guidance on automatic share buy-back programs conducted on behalf of listed issuers" (October 2023) and "Guidance on the electronic submission of prospectus and accompanying documents to the Exchange and the Companies Registry for authorisation and registration" (December 2023). Three of these guidance letters (the first, third and the last) were published jointly by the IPO Vetting department and the LIR department.

Listing Decisions: "Whether there were exceptional circumstances for a listed issuer to conduct a highly dilutive issuance of shares" (June 2022) and "Whether Company A's proposed acquisition which constituted a disclosable transaction was a reverse takeover" (June 2022).

[63] Enforcement Bulletins in relation to, amongst others, listed issuers' internal controls (February 2022), record-keeping by issuers and directors (August 2022), accurate and meaningful disclosures of information (March 2023) and directors' duties towards conflicts of interests (September 2023).

119. The Exchange reported that it handled 123 investigations in 2023, down 12.8% from 141 in 2022.

120. The Exchange completed 33 disciplinary cases in 2023 (2022: 29), 32 of which were concluded with public sanctions imposed by the Exchange (2022: 29). In respect of these disciplinary cases, the Exchange issued in 2023:

(a) 19 sanctions against listed issuers (2022: 23) and 124 sanctions against individuals (2022: 167[64]). These included, amongst others, unsuitability statements (**DUS**)[65] against 29 individuals (2022: 13) and prejudice statements (**PII**)[66] against 22 individuals (2022: 29);

(b) directions in 27 cases[67] (2022: 26); and

(c) regulatory letters in 18 cases (2022: 19).

121. In 2023, the Exchange imposed sanctions against 124 directors[68], representing a 23% decrease from 2022 (160 directors). These sanctions included, amongst others, DUSs against 29 directors (2022: 13), PIIs against 22 directors (2022: 29) and public censure against 42 directors (2022: 38).

		DUS	PII	Public censure*	Total
2023	Executive directors	18	17	30	**65**
	Non-executive directors	4	-	-	**4**
	INEDs	7	5	12	**24**
	Total	**29**	**22**	**42**	**93**
2022	Executive directors	7	21	25	**53**
	Non-executive directors	1	4	6	**11**
	INEDs	5	4	7	**16**
	Total	**13**	**29**	**38**	**80**
*The figures for "public censure" exclude those individuals subject to both (i) a public censure and (ii) a DUS or a PII.					

122. Following the adoption of the revised sanctions framework in July 2021[69], the DUS is now the most severe sanction against directors. Where a director fails to cooperate with the Exchange's investigation, the Exchange considers that reflects a highly concerning attitude towards regulation and compliance, and a DUS would be recommended by Listing Enforcement.

[64] The number of sanctions against individuals in 2022 included sanctions against 160 directors and seven non-directors (such as supervisors).

[65] Director unsuitability statement pursuant to rule 2A.10(5).

[66] A statement of opinion made by the Exchange pursuant to rule 2A.10(4) that the retention of office by the director or senior management may cause prejudice to the interests of investors.

[67] These represented directions requiring listed issuers and directors to take proactive remedial actions to rectify breaches, improve internal controls and overall corporate governance. In 2023, the Exchange issued internal control review directions in four cases (2022: four), retention of compliance adviser directions in two cases (2022: one) and training of directors directions in 21 cases (2022: 21).

[68] Directors are personally required both to comply with the Listing Rules and to procure Listing Rule compliance by listed issuers.

[69] See Consultation Conclusions on Review of Listing Rules Relating to Disciplinary Powers and Sanctions (May 2021).

123. In 2022 and 2023, two INEDs received PIIs for their persistent failure to address the issuer's internal control deficiencies. All DUSs and PIIs against other INEDs were imposed on those who failed to cooperate with the Exchange's investigation.

124. Below is a summary of the number of investigations handled by the Exchange and the enforcement outcomes from 2019 to 2023:

	Investigations*	**No. of cases involving issuance of regulatory letters (eg, warning letters)**	**Cases closed by way of "no further action"**	**Disciplinary cases**
2019	112	15	21	13
2020	128	9	6	13
2021	164	12	10	36
2022	141	19	11	29
2023	123	18	7	33

*The numbers represent cases handled by Listing Enforcement during the year, including those carried over to the relevant period and those not concluded at the end of the year. At the end of 2023, the number of outstanding investigations was 38 (2022: 37) and the number of cases pending disposal or disciplinary action was 27 (2022: 43).

125. The average time taken to complete an investigation was 12.4 months in 2023 and 11.8 months in 2022.

SFC observations

126. The number of listed issuers increased 0.5% from 2022 to 2023[70] but the number of investigations of Listing Rule breaches handled by the Exchange decreased[71]. The number of outstanding investigations slightly increased from 37 in 2022 to 38 in 2023.

127. In recent years, Listing Enforcement continued to pursue more cases to maintain market integrity. In 2021, there began to be a notable increase in the number of disciplinary cases concluded, with a focus on how directors discharged their duties. Following the adoption of the revised sanctions framework, 42 DUSs were imposed on directors in 2022 and 2023. In a case in 2023, two INEDs of a listed issuer received PIIs for serious failures to address the issuer's internal control deficiencies for an extended period of time. The decision sent an important message to the market about INEDs' duties to oversee listed issuers' Listing Rule compliance and corporate governance.

Debts and derivatives

128. The total number of derivative warrants and CBBCs listing applications processed by the Structured Products and Fixed Income department in 2023 (30,818) decreased 34.3% from 2022 (46,891).

[70] The number of listed issuers increased from 2,597 in 2022 to 2,609 in 2023, representing an increase of 12 (or 0.5%).

[71] See paragraphs 119 and 124.