To: Hong Kong Exchanges and Clearing Limited

Re: Consultation Paper – Review of Listing Rules relating to Disciplinary Powers and Sanctions

Abuse or Amuse - Disciplinary Powers and Sanctions on Professional Advisers?

Earlier this year, The Stock Exchange of Hong Kong Limited ("**Exchange**") issued a Consultation Paper on proposed changes with regards to the Exchange's disciplinary regime. We are responding to Q10, Q12, Q15, Q19 and Q20 of the Consultation Paper only.

For the purpose of this submission, references made to "professional adviser" in the consultation questions are taken to mean legal advisers (as defined under Rule 2A.10) and the following arguments shall focus on the said meaning.

We propose to include express obligations on professional advisers when acting in connection with Rule matters (Q20)

Recognizing the important role professional advisers play in the discharge of rule obligations by listed issuers, the Exchange has proposed to impose express obligations for such advisers to (i) use all reasonable efforts to ensure that their clients understand and are advised as to the scope of and their obligations under the Rules; and (ii) not knowingly provide information to the Exchange which is false or misleading in a material particular.

(i) Use all reasonable efforts to ensure client understand the scope and obligations

The assumption under the existing Rule 2A.10 that professional advisers are subject to an obligation to use all reasonable efforts to ensure that their clients understand and are advised as to the scope of the Rules is correct. Such obligations are inherent under The Hong Kong Solicitors' Guide to Professional Conduct (the "**Solicitors' Guide**") and Solicitors' Practice Rules (Cap. 159H) (the "**Practice Rules**").

Using all reasonable efforts to ensure that clients understand and are advised as to the scope of Rules fall under a duty to act in the best interest of his client, and to maintain a proper standard of work under Rule 2 of the Practice Rules, a non-compliance of which leads to possible disciplinary proceedings by the Council of the Law Society. Further, Principle 6.01 of the Solicitors' Guide imposes a duty onto solicitors, as part of his duty to act competently, to serve his client in a conscientious, diligent, prompt and efficient manner. Reading the aforementioned duties jointly entails that when advising an issuer, a legal adviser is obliged to ensure that the client understands and are advised as to the scope of the rules.

The proposed new express obligations, therefore, will be an ineffectual attempt to produce additional hurdles for legal advises on top of the existing provisions governing their professional conduct.

We refer to the Exchange's recognition in the Consultation Paper that the primary responsibility for compliance remains with the listed issuer, and in particular, its directors. Thus, if the ultimate rationale of this proposed obligation is for the smooth discharging of rule obligations by listed issuers as suggested in the Consultation Paper, it should be noted that the Director's Declaration and Undertaking under Form B, as prescribed in Appendix 5 to the Listing Rules, serves the same purpose.

(ii) Not knowingly provide false or misleading information

We consider this proposed express obligation to have little additional value to the existing provisions which already create potential civil and criminal liabilities for professional advisers for false or misleading information illustrated below.

Section 277 of the SFO imposes civil liability where a person discloses, circulates or disseminates, or authorizes or is concerned in the disclosure, circulation or dissemination of, information that is likely inter alia to: (a) induce another person to subscribe for securities in Hong Kong; (b) induce the sale or purchase in Hong Kong of securities by another person; or (c) to maintain, increase, reduce or stabilise the price of securities, in Hong Kong, if: (i) the information is false or misleading as to a material fact or through the omission of a material fact ("**False Information**"); (ii) and the person knows that, or is reckless or, negligent as to whether, the information is False Information. Similarly, Section 298 of the SFO imposes criminal liability in virtually the same circumstances as Section 277 of the SFO except that negligence will not suffice to establish criminal liability. Any person who contravenes Section 298 of the SFO is liable to maximum fines of HK$10 million and 10 years imprisonment.

The scope of the above is broad, covering information that is likely to induce a dealing in securities or have an effect on the price of securities such as prospectus and announcements published on the Exchange website.

Further, Section 384 of the SFO imposes criminal liability on any person who intentionally or recklessly provides any information which is false or misleading in a material particular in filing with the SFC or the Exchange a prospectus, other listing document or any public disclosure materials disseminated under the Hong Kong Listing Rules. The provision of false or misleading information caught by this section, namely "intentionally or recklessly" is wider than just "knowingly" under the proposed new obligation. As such, a more stringent standard is already in place for professional advisers, rendering the second part of the proposal redundant.

The combination of the above legislation safeguards the accuracy of the information submitted to the Exchange. The rationale of the proposed express obligation is for the same purpose the above statutory provisions set out to achieve. It is therefore of minimal value and, in our view, unnecessary.

We propose to include employees of professional advisers of listed issuers and their subsidiaries as a Relevant Party under the Rules (Q15)

The Listing Committee can, under the existing Rule 2A.09(5), ban a named individual employed by a professional adviser from representing a specified party in relation to a stipulated matter or matters coming before the Listing Division or the Listing Committee for a stated period.

It is the Exchange's position that such disciplinary actions cannot be imposed without including the employees of professional advisers as a Relevant Party. We, however, believe that there are existing provisions available for disciplinary purposes to the same effect as the above, if not harsher, that warrants the dispensing of this proposal.

Under Section 23(8) of the SFO, the Exchange can refer breaches of Rules allegedly to be committed by a solicitor or a professional accountant and which may also constitute a breach of duty imposed by law or under rules of professional conduct to the Law Society or the Hong Kong Institute of Certified Public Accountants (the "HKICPA"). Upon taking effect of the Financial Reporting Council (Amendment) Ordinance (Cap. 588 of the Laws of Hong Kong) on 1 October 2019 (the "FRCO"), the Financial Reporting Council (the "FRC") has taken over the regulatory

function on auditors from HKICPA. FRC has become an independent auditor oversight body and is now vested, in addition to investigation powers, with inspection and disciplinary powers with regard to auditors of listed companies. Under the Memorandum of Understanding between the Exchange and the FRC dated 27 December 2007 (the "MOU"), both parties recognized the importance of ensuring proper standards by auditors and reporting accountants. The MOU sets out the working arrangements between them in order to reduce any duplication of efforts and ensure efficient and effective cooperation. In particular, the Exchange acknowledged that if it comes to the knowledge of any auditing or financial reporting irregularities or non-compliance, the Exchange will make a complaint to the FRC. Under the jurisdiction of FRC, it can imposed sanctions under Section 37D of the FRCO that are even more severe than those available under the proposed Rule 2A.10 so far as auditors are concerned.

On a similar note, when a breach of the Listing Rules by a legal adviseris likely to trigger the breaching of the professional duty to act competently and with integrity, the solicitor faces inquiry and investigation under its own regulatory body, whose Disciplinary Tribunal can, amongst all other sanctions, suspend the solicitor from practice for such period as the Solicitors Disciplinary Tribunal thinks fit (Section 10(2)(b) of the Legal Practitioners Ordinance (the **"LPO"**)). This order, which will be publicly available, seems to cover completely the banning of representation the Exchanges wishes to be able to enforce, and offers a bigger deterrent impact for misconduct.

While it may be argued that Section 23(8) of the SFO only applies when the employee is a solicitor, we note that the Exchange can also, under Section 3 of Solicitors Disciplinary Tribunal Proceedings Rules (Cap. 195C), make an application to the Law Society to consider a complaint regarding the conduct of a solicitor's employees and trainee solicitors. The possible sanctions for the above-named respondents include the cancellation or suspension of the training contract (Section 10(2)(f)) LPO) and the prohibition of employment of the employee for such as period as the Solicitors Disciplinary Tribunal may decide (Section 10(2)(g) of the LPO). Again, the available orders seem to include sanctions to the same effect of, if not more severe than, a banning of representation.

We propose to impose secondary liability on Relevant Parties if they have 'caused by action or omission or knowingly participated in a contravention of the Listing Rules' (Q10)

The Exchange stated that the current framework does not include a prescribed standard of compliance for members of senior management, substantial shareholders, professional advisers, authorized representatives and significant shareholders. As such, disciplinary actions may not be possible even if the conduct was a significant factor in the commission of a Rule Breach.

A lack of standard of compliance?

We agree with the Exchange's position to the extent that members of senior management (e.g. CEO, CFO, board secretary, etc.), substantial shareholders and significant shareholders may not be governed by a prescribed standard of compliance, and that this can serve as a good incentive to impose secondary liability onto these parties for rule breaches. We, however, do not believe that the imposing of secondary liability should include professional advisers that are already subject to existing standards of compliance prescribed by the law and their respective professional regulatory bodies.

Section 213 of the SFO grants the SFC the power to apply to the Court of First Instance for a broad range of declaratory orders and injunctions for contraventions of any provisions of the SFO, any terms and conditions of any license or registration under the SFO, or any other condition imposed under or pursuant to any provision of the SFO. Contravention is taken to mean aiding,

abetting or otherwise assisting, counseling or procuring a person to commit any such contravention; inducing, whether by threats, promises or otherwise, a person to commit any contravention; directly or indirectly being knowingly involved in, or a party to, any such contravention; attempting, or conspiring with others, to commit any such contravention.

As such, a direct or indirect contravention of the listing rules (as made under the SFO), already attracts possible court sanctions.

Further, a contravention of the Listing Rules, whether caused by action, omission or knowingly participated in, seems to breach the Solicitor's Guide and Practice Rules and can attract sanctions made available under Section 10 of the LPO that reciprocate those for professional advisers in Rule 2A.09. To name a few when the solicitor is retained by the issuer, causing by action a contravention of the Listing Rules is likely to breach a solicitor's duty to act in the best interest of his client (Rule 2 of the Practice Rules); a contravention by omission is likely to breach his duty to carry out the instructions with diligence and must exercise reasonable care and skill (Principle 5.12 of the Solicitors' Guide); and knowingly participating in a contravention of the listing rules is likely a breach of his duty to not do anything that is likely to compromise his integrity (Rule 2 of the Practice Rules).

There are obligations prescribed by law and by the professional regulatory body, which indirectly prevent a legal adviser's from contravening the Listing Rules, whether directly himself or procuring the client to commit such contraventions. The incentive to impose a secondary liability onto professional advisers because there is a lack of prescribed standard of compliance is mistaken. The existing framework deemed the imposing of the proposed secondary liability redundant, and may create a negative deterrent effect when professional advisors are burdened with unnecessary extra responsibilities for the same purpose the existing framework sets to accomplish.

Deprivation of Legal Representation

Under the proposed regime, legal advisers may be more reluctant to act for listed companies under the GEM Board due to a heightened risk of their firms' or personal liability attached to their legal work. This freedom to not accept instructions from a prospective client is set out under Principle 5.01 of the Solicitors' Guide. The introduction of a secondary liability may, inadvertently, affect the right to a choice of lawyers for lawful rights and interests of related parties under Article 35 of the Basic Law.

Existing Referral Scheme

As correctly recognized by the Exchange's Enforcement Policy Statement (revised on 17 February 2017), referrals are made to other law enforcement or regulatory bodies for conduct which falls within their jurisdiction. An indirect contravention of the Listing Rules that falls under the abovementioned standards of compliance prescribed by the law and the professional regulatory bodies, should be referred to the respective bodies and not attempted to be resolved by the Exchange through an expansion of unjustifiable disciplinary powers.

No undertakings given to the Exchange

We recognize that the collective responsibility of directors for compliance is a cornerstone of the Exchange's enforcement regime and is clearly established by the Listing Rules. This obligation is refined and reinforced by the personal undertaking given by the directors to the Exchange to use their best endeavours to procure Listing Rule compliance by listed companies. We do not contest the imposing of secondary liability onto parties such as directors that have made a compliance

(7)

related undertaking to the Exchange, but such undertakings are not made by professional advisers. The imposing of a secondary liability onto a party that did not enter into a contract with, nor give an undertaking to the Exchange cannot be justified.

We propose that sanctions may be imposed on all Relevant Parties through secondary liability where a party has failed to comply with a requirement imposed by the Listing Division, the Listing Committee or the Listing Review Committee (Q12)

The scope is ambiguous and further clarifications are needed as to whether "all Relevant Parties" to which the proposed secondary liability relates is taken to mean all Relevant Parties that have caused by action or omission or knowingly participated in a contravention of the requirement, or all Relevant Parties listed under the existing Rule 2A.10. The scope of the latter is too wide, suggesting a secondary liability even for property valuers (as included in the definition of "professional adviser"), for example, if the director fails to attend training as directed by the Listing Committee. We are of the view that the sanctions should be restricted to and focused on who the requirements are directed to, as currently practiced, for the optimal disciplinary and deterrent effect.

In addition, the Exchange is a public body and the decisions of Listing Committee or the Listing Review Committee are amendable to judicial review. Based on our observation, over the past 20 years, there were only five judicial review proceedings against the decisions of the Exchange in disciplinary and no-disciplinary review hearings. Imposing secondary liability on professional advisers is likely to attract more judiciary reviews which creates risk of the committees' decisions being challenged. The Exchange needs to bear in mind that responding to a judicial review is a time-consuming and expensive process which may not be in the interests of the investors and the market as a whole.

We propose to extend the ban on professional advisers to cover banning of representation of any or a specified party (Q19)

Under the existing Rule 2A.09 (5), the Listing Committee can ban a professional adviser or a named individual employed by a professional adviser from representing a specified party in relation to a stipulated matter or matters coming before the Listing Division or the Listing Committee for a stated period. The Exchange proposed to extend the scope of the ban to cover the banning of representation of any party.

Based on the publicly available listing enforcement notices and announcements as of today, It is our observation that 2A.09 (5) is rarely utilized (if there is any). If it is indeed an "effective practical disciplinary tool" that calls for enhancements as stipulated in the Consultation Paper, we should see more published enforcement news or announcements relating to such bans. Thus, given the low utilization rate of such provisions by the Exchange, the need to extend the coverage of the ban is questionable.

Reiterating the arguments above, the Exchange's Enforcement Policy Statement recognizes that referrals are made to other law enforcement or regulatory bodies for conduct which falls within their jurisdiction. Upon referrals and investigations, the Disciplinary Tribunal under the Law Society can, amongst all other sanctions, suspend the solicitor from practice for such period as the Solicitors Disciplinary Tribunal thinks fit. Further, Section 213(2)(f) of the SFO provides that SFC can apply to the Court of First Instance on contraventions to the Listing Rules, which are requirements made under the SFO, for a possible order directing a person to refrain from doing any act specified in the order. The Exchange's existing referral regime together with the SFC's

powers provide readily available sanctions that this proposal wishes to achieve, and thus giving little reason for why the scope of the ban in question should be expanded.

Yours faithfully

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Withers

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