



Hong Kong

March 2016

## SFC CONCLUDES ON EXPANDING SCOPE OF SHORT POSITION REPORTING

### Introduction

On 24 February 2016, the Securities and Futures Commission (SFC) published its Consultation Conclusions<sup>1</sup> on expanding the scope of short position reporting and the corresponding amendments to the Securities and Futures (Short Position Reporting) Rules (**Consultation Conclusions**).

The Consultation Conclusions are a response to feedback provided by relevant parties regarding the SFC's Consultation Paper<sup>2</sup> on the same matter published in November 2015. For more information on the Consultation Paper, please see our December 2015<sup>3</sup> newsletter.

The key changes to be implemented are:

- Short position reporting will be required for all securities, including collective investment schemes, which are determined by The Stock Exchange of Hong Kong Limited (SEHK) to be Designated Securities (i.e. securities that can be short sold under the rules of SEHK);
- The reporting threshold for Designated Securities that are stocks will remain the same - i.e. the lower of 0.02% of the stock's market capitalisation, or HK\$30 million;

- The reporting threshold for Designated Securities that are collective investment schemes will be HK\$30 million;
- To determine the value of a net short position where a Designated Security's closing price is in a foreign currency, it must first be converted into Hong Kong dollars at the specified rate for that currency; and
- Daily reporting will apply in contingency situations to those Designated Securities specified by the SFC in a public note.

The SFC intends to implement the expanded reporting regime on 15 March 2017, subject to the legislative process to adopt the revised Short Position Reporting Rules.

### Overall support for the Consultation Proposals

Most of the responses to the SFC's consultation proposals came from financial institutions and professional associations<sup>4</sup>, and a majority of these respondents were in favour of the SFC's proposals.

There were some responses which opposed the expansion, which will be discussed below. The SFC has addressed such opposition in the Consultation Conclusions.

1 <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/conclusion?refNo=15CP6>

2 <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=15CP6>

3 <http://www.charltonslaw.com/sfc-consults-on-expanding-the-scope-of-short-position-reporting/>

4 A list of the respondents, barring those who wished to remain anonymous, can be found in Appendix A of the Consultation Conclusions: <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/conclusion?refNo=15CP6>

### Expanded Scope of Reporting

The short position reporting requirement under the current Short Position Reporting Rules applies only to a subset of the securities that are eligible for short selling which are known as Designated Securities. As at 30 October 2015, the short position reporting requirement applied to 127 (14%) of the 889 Designated Securities.

Under the new regime, the reporting requirement will apply to all Designated Securities, including those which are collective investment schemes.

While receiving support for the proposal from a majority of financial institutions and professional associations, there were suggestions from individual respondents that the Short Position Reporting Rules should be scrapped. The SFC took the opportunity to reiterate that short position reporting is required in most major jurisdictions, including the US, EU, Japan and Australia. The SFC considers that Hong Kong, as an international financial centre, should have a short position reporting regime to enable the SFC to more effectively monitor short selling activities.

### Reporting Threshold

For Designated Securities that are stocks, the reporting threshold will remain unchanged. A person will have to report a net short position in Designated Securities that is equal to or exceeds 0.02% of the market capitalisation of the listed issuer concerned or HK\$30 million, whichever is lower.

The SFC set this threshold in 2012, taking into account the size of listed companies, market capitalisation, liquidity, the type of market participants and investors and their trading activities. The SFC also took the opportunity to emphasise there is no “one-size-fits-all” threshold level, when compared to other reporting thresholds globally. For Hong Kong, the SFC concluded that if the reporting threshold is set at a high level, an early build-up of large short positions would not be detected. It is best, therefore, to maintain the reporting threshold at the current level.

The reporting threshold for Designated Securities that are collective investment schemes will be HK\$30 million. This is because some collective investment schemes are open-ended and it was considered impractical to set the reporting threshold by reference to market capitalisation since this can change frequently and significantly due to the creation and redemption process. A person will have to report a short position if, at the

end of the last trading day of the week, his net short position in a collective investment scheme has a value of HK\$30 million or more.

### Designated Securities that are Traded in Foreign Currency

Designated Securities can be traded in a foreign currency (currently including US dollars and renminbi). Where the trade price is in a foreign currency, the closing price must first be converted into Hong Kong dollars (**HKD**) to determine the value of a net short position. The rate of exchange used would be the rate for the foreign currency which is the buying rate for telegraphic transfers on the reporting day, as determined by the Hong Kong Monetary Authority (HKMA). Applicable exchange rates can be obtained from the website [http://www.hkex.com.hk/eng/market/sec\\_tradinfo/stampfx/stampfx.asp](http://www.hkex.com.hk/eng/market/sec_tradinfo/stampfx/stampfx.asp).

For those Designated Securities which can be traded in multiple currencies, to determine whether a person has a reporting obligation, he will first have to convert the value of his position in the foreign currency counter into HKD, as above, and then include that in his position in the HKD counter. If the value of his net short position exceeds the relevant reporting threshold trigger, he will have to report his position to the SFC.

### Reporting in Contingency Situations

The Short Position Reporting Rules allow the SFC to require daily reporting in a contingency situation. To reduce the operational burden once the reporting requirement is extended to all Designated Securities, in contingency situations, the SFC will publish a list of Designated Securities which are subject to daily reporting. It may then stop daily reporting on one or more of the Daily Reporting Securities depending on market conditions.

### Reporting through SFC Designated Electronic System

Market participants currently report short positions using an electronic system developed by the SFC. Moving forward, in the light of technological developments, the SFC will seek to adopt more than one electronic system for reporting. The SFC will conduct a thorough study in this area. Details will be announced once the study is complete. Until then, market participants are to continue using the existing electronic channel to report short positions.

## Operational Arrangements for Short Position Reporting

Following the consultation process, the SFC is now determining the operational arrangements for short position reporting.

The current operation arrangements for short position reporting involve the SFC publishing a list of specified shares for each report date, including information on the stock code, the stock name of the specified shares in Comma Separate value (**CSV**) and PDF formats.

In view of the expanded scope of reporting, the SFC is now considering the publication of a CSV file which will cover all Designated Securities, including the following information:

- i) the security type of a Designated Security;
- ii) the currency that the Designated Security is traded in; and
- iii) if applicable, the exchange rates for currencies other than Hong Kong dollars.

The SFC will publish further information relating to the proposed CSV file in due course. The SFC encourages interested parties to subscribe to the short position email alert service.<sup>5</sup>

## Next Steps

- The SFC will now submit the amended Short Position Reporting Rules to the Legislative Council for negative vetting.
- The target for implementation of the amended Short Position Reporting Rules is 15 March 2017. Further FAQs will be provided for more clarity.

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<sup>5</sup> <https://www.sfc.hk/CampaignHelper/campaignForm.jsp?lang=EN>

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