




Stock Exchange Consults on Listing Rules for Share Schemes


The Stock Exchange of Hong Kong Limited (the Exchange) has published a consultation paper on the Proposed Amendments to Listing Rules relating to Share Schemes of Listed Issuers.


There are significant changes proposed that will impact the design, governance and administration for share schemes of companies listed on the Exchange.


This is proposed to apply to new share schemes adopted on or after the effective date of the amendments, with transitional arrangements for existing share schemes that are valid at the effective date.

Who will be impacted


 Listed companies that have implemented share award or share option schemes


 Companies considering IPOs which include share incentive plans


 Start up and early-stage companies that might want to list in future


 Listed companies/applicants with relatively informal or relaxed incentive arrangements

Key Stakeholders

 HK listed companies and listing applicants

 Remuneration committees of listed companies

 Participants of share incentive schemes of listed companies or their subsidiaries

 Trustees holding unvested shares of share incentive schemes



Implications on scheme design and management

Under the proposal, the requirements of Chapter 17 of The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the Listing Rules), which currently only apply to share options, will extend to share awards. Many listed issuers have already adopted equity remuneration arrangements. These companies and those planning to implement share schemes should consider how these changes might impact their share schemes and whether the plan documentation and procedures around them need to be updated. We highlight below some of the key proposals along with our initial takeaways.



Limit on newly issued shares to settle grants

The number of new shares that can be granted under all share schemes (i.e., share options and share awards) will be capped at 10% of the listed issuer's issued shares. The cap can be refreshed once every three years, with any more frequent refreshments being subject to approval by independent shareholders. This cap does not apply to grants settled with shares purchased from the market. The rationale behind such changes is to safeguard against excessive dilution of shareholders due to new issues of shares.

Companies with significant share and option awards should consider the impact of this proposal and, if necessary, consider the implications of limiting the grants or settling grants with shares purchased from the market.



Minimum 12-month vesting period

Share options and share awards that are to be settled by issuing new shares will generally become subject to a minimum vesting period of 12 months. A shorter vesting period for specifically identified employee participants can be approved by the remuneration committee, in which case the company's grant announcement would need to disclose additional information related to the rationale for this shorter vesting period.

It is common for companies to grant share options and share awards subject to vesting of more than 12 months, e.g., vesting in tranches over multiple years. Companies should review and make sure that the first tranche vests at least 12 months from the date of grant.

This proposal could impact companies intending to grant restricted shares that vest immediately but which are subject to sale restrictions, such as those granted to attract new talent as a sign-on bonus and/or compensate new employees for benefits forfeited on resignation of their previous role. Vesting periods may come into sharper focus with the recent decision of the Court of First Instance in the *Forlee*¹ case, which drew a clear distinction between vesting conditions and future forfeiture events, when considering the tax outcomes.



Performance targets and clawback mechanism

Grants of share awards and share options to acquire new shares of a listed issuer (or grants of share awards and/or share options to acquire new or existing shares of a listed issuer's subsidiary), are expected to have performance targets and a clawback mechanism and should be disclosed in grant announcements.

If there is a grant of such incentives without performance targets and/or a clawback mechanism, the remuneration committee's views on why performance targets and/or a clawback mechanism are not required and how the grant serves the purpose of the scheme must be disclosed in the grant announcement.

¹ *Richard Paul Forlee v Commissioner of Inland Revenue* [2020]HKCFI868



Disclosure requirements

There will be various enhanced disclosure requirements all types of grants, irrespective of whether the grants will be settled with newly issued shares or shares purchased from the market. These requirements include:

- ❖ disclosure of all types of grants for participants within certain categories, or on an individual named basis where applicable. Examples as follows:
 - a. Grants to Connected Persons²
 - b. Grants to related entities and service providers of over 0.1% of the issuer's issued shares in any 12-month period
 - c. Grants to any participant of over 1% of the issuer's issued shares in any 12-month period

- ❖ disclosure of work performed by the remuneration committee in relation to share scheme matters, such as matters reviewed and/or approved by the committee, explanations for approvals given, and factors that it took into account.



Other considerations

Grants to participants exceeding certain thresholds or who are Connected Persons will require approval by the remuneration committee, shareholders and/or independent shareholders, depending on the circumstances.

Participants eligible for grants which will be settled by issuing new shares will be restricted to (i) directors and employees of the listed company or its subsidiaries, (ii) directors and employees of related entities of the issuer group (i.e. holding companies, fellow subsidiaries and associated companies of the issuer), and (iii) material service providers that provide continual and recurring service to the issuer group. Issuers must also set a sublimit, to be separately voted on by shareholders, on the grants that can be made to service providers. These eligibility restrictions are new and aim to reward and incentivise participants that contribute to the long-term growth of the issuer.

The new proposals also generally apply, with some relaxation for issues that are not significant to the group as a whole, to share schemes operated by subsidiaries. Therefore, when planning or reviewing their share incentive framework, companies should take a holistic view of the share schemes across the whole group.

Trustees holding shares for the purpose of settling grants which have yet to vest shall abstain from voting in respect of such shares on matters that require shareholders' approval under the Listing Rules, and the number of unvested shares held by such trustees should be disclosed by the issuer in its monthly returns. If a company is using such a trustee, it will need to review the relevant documents and arrangements to ensure that these requirements can be met.

² A connected person in this case means a director, chief executive or substantial shareholder of the listed issuer or an associate of any of them (Connected Person(s)).



Next steps

The Exchange is seeking market views on the proposed amendments to Chapter 17 of the Listing Rules, and interested parties are encouraged to submit a response to the consultation paper by 31 December 2021.

The effective date of the Listing Rules amendments would only be known after the consultation conclusions are published. If the proposals in the consultation are adopted, then certain transitional arrangements for existing share schemes that are valid at the effective date will apply, such as complying with the new disclosure requirements after the effective date, and amending the terms of existing share schemes to comply with the amended Chapter 17 of the Listing Rules before certain time limits. Issuers should take note of which transitional arrangements might apply to them and be ready in advance to comply once the effective date is confirmed.

Hong Kong listed companies and aspiring listing applicants that already have or are planning to operate share schemes should review the proposed changes and consider the implications to their share scheme arrangements and any additional approval or disclosure requirements. We suggest companies should review the requirements and keep updated on developments after the consultation concludes and the conclusions are subsequently published.

If you have any questions, please contact your usual KPMG or SF Lawyers contact, or the authors, for a confidential discussion.

Contact us

The team of commercial, tax and legal advisors at KPMG and SF Lawyers are ready to assist you. Please contact us to discuss how we can help you resolve current issues facing your business and deliver future growth.



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