

Client Alert

Corporate Finance

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Hong Kong Stock Exchange proposes rule amendments to enhance the regulation of share option / award schemes

On 29 October 2021, The Stock Exchange of Hong Kong Limited (**Exchange**) published a [consultation paper](#) on its proposed amendments to the Listing Rules relating to share option schemes and share award schemes (collectively, **share schemes**) of listed issuers.

Chapter 17 of the Listing Rules¹ (**Chapter 17**) currently applies to issuers' and their subsidiaries' share option schemes, but not their share award schemes. In view of issuers' increasing adoption of share award schemes, the Exchange proposes to amend Chapter 17 to also govern share award schemes. In addition, the Exchange also proposes changes to Chapter 17 in specific areas, including, among other things, the definition of eligible participants, the requirements for scheme mandate refreshments and the disclosure requirements.

Consultation will end on **31 December 2021**.

The key proposals are summarised below.

	Current position	Proposals
Share schemes involving issuance of new shares of listed issuers		
Share award schemes	Chapter 17 currently applies to share option schemes, but not share award schemes.	To extend Chapter 17 to govern all share schemes.
Eligible participants	No restriction on the categories of eligible participants.	To define eligible participants of share schemes to include the following persons: <ul style="list-style-type: none"> ➤ "Employee Participants" – i.e. directors and employees of the issuer or any of its subsidiaries (including persons who are granted shares or options under the scheme as an inducement to enter into employment contracts with these companies); ➤ "Related Entity Participants" – i.e. directors and employees of the holding companies, fellow subsidiaries or associated companies of the issuer; and ➤ "Service Providers" – i.e. persons who provide services to the issuer group on a continuing and recurring basis in their ordinary and usual course of business which are material to the long term growth of the issuer group. They should exclude financial advisors or placing agents providing

¹ Chapter 23 of the GEM listing Rules

		<p>fundraising or M&A services, or consultants providing professional services to the issuer.</p> <p>To require grants to Related Entity Participants and Service Providers be approved by the remuneration committee with reasons for grants clearly disclosed.</p>
Scheme mandate	<p>Chapter 17 limits grants of share options from all share option schemes of an issuer to 10% of its total issued shares (10% scheme mandate limit).</p> <p>Issuers may seek approval from shareholders to refresh the scheme mandate at any time, provided that options outstanding do not exceed the 30% of the issued shares (overall limit).</p>	<p>To apply the current 10% scheme mandate limit to all share schemes.</p> <p>This mandate may be refreshed by shareholders once every three years. Refreshments within a three year period must be approved by shareholders of the issuer (other than the controlling shareholders of the issuer (or if there is no controlling shareholder, the executive directors and non-executive directors and chief executive of the issuer) and their associates).</p> <p>To require the issuer to set a sublimit in respect of grants to Service Providers and disclose the basis for determining the sublimit in circulars. This sublimit must be separately voted on by shareholders.</p> <p>To remove the overall limit.</p>
Grants to individual participants	<p>Grants of options to an individual under Chapter 17 are subject to shareholders' approval if the number of shares covered by the grants exceed 1% of the shares in issue over any 12-month period (1% individual limit).</p>	<p>To apply the current 1% individual limit to all share schemes.</p>
Grants to directors, chief executive or substantial shareholder of the issuer or an associate of any of them (connected persons)	<p>Grants of options to a connected person under Chapter 17 require approval by independent non-executive directors (INEDs) of the issuer (excluding an INED who is a grantee).</p> <p>Grants of options to an INED or a substantial shareholder of an issuer (or an associate of any of them) in excess of 0.1% of issued shares and HK\$5 million in value over a 12-month period must be approved by shareholders (excluding the grantee, his/her associates and all core connected persons of the issuer).</p> <p>Any grant of share awards to a connected person constitutes a connected transaction subject to independent shareholders' approval regardless of the size of the grant.</p>	<p>To require approval by the remuneration committee for all grants to connected persons.</p> <p><u>Grants to a director (other than an INED) or the chief executive</u> To require approval by shareholders other than the grantee, his/her associates and all core connected persons of the issuer for grants of share awards in excess of 0.1% of the issued shares of the issuer over any 12-month period.</p> <p><u>Grants to an INED or a substantial shareholder</u> To require approval by shareholders other than the grantee, his/her associates and all core connected persons of the issuer if the grants of share awards and share options in aggregate exceed 0.1% of the issued shares of the issuer over any 12-month period.</p>
Vesting period	<p>Chapter 17 currently does not have specific requirements on vesting period.</p>	<p>To require a minimum vesting period of 12 months, unless a shorter vesting period is approved by the remuneration committee in respect of grants made to Employee Participants specifically identified by the issuer.</p>
Performance targets and clawback mechanism	<p>Chapter 17 currently requires an issuer to set out in the scheme documents any performance targets attached to the grants or a negative statement.</p>	<p>To require performance targets and clawback mechanism for all grants and disclosure of the same in grant announcements. If the grants are made without performance targets and/or a clawback mechanism, the grant announcement must disclose</p>

	There is no specific disclosure requirement relating to a clawback mechanism where an issuer may recover or withhold any shares or options granted to a participant in the event of serious misconduct, a material misstatement in the issuer's financial statements or other special circumstances.	the remuneration committee's views as to why performance targets and/or a clawback mechanism is/are not required and how the grants serve the purpose of the scheme.
Disclosure of details of grants to certain categories of participants on an individual basis	Under Chapter 17, an issuer must disclose details of option grants by way of announcement, and disclosure of grants to a connected person must be made on an individual basis.	To require disclosure of details of grants to the following participants to be made on an individual basis: <ul style="list-style-type: none"> ➤ a connected person; ➤ a participant with grants in excess of the 1% individual limit; and ➤ a Related Entity Participant or Service Provider with grants in excess of 0.1% of the issuer's issued shares over any 12-month period. Grants to other participants can be disclosed in aggregate by category, but the Exchange may require the issuer to submit a list of grantees.
Disclosure of work performed by the remuneration committee	An issuer is required to disclose in its Corporate Governance Report a summary of the work performed by the remuneration committee during the year, including the committee's work on determining the remuneration policy for executive directors, assessing their performance and approving the terms of their service contracts.	To require disclosure in the Corporate Governance Report of matters relating to share schemes reviewed and/or approved by the remuneration committee during the financial year.
Approval for changes to terms of grant	Chapter 17 requires an issuer to seek shareholders' approval for any changes to the terms of option granted.	To modify the current requirement such that changes to the terms of share award or option granted must be approved by the remuneration committee and/or shareholders of the issuer if the initial grant of the share award or option requires such approval (as the case may be).
Transfer of share awards / options to a trust or a private company	Share options may not be transferred by the grantee to other persons.	To provide a waiver to allow a transfer of share awards or options to a vehicle (including a trust or a private company) for the benefit of the grantee and his/her family members (e.g. for estate planning or tax planning purposes), provided that such transfer would continue to meet the purpose of the scheme and other requirements of Chapter 17.
Voting rights of unvested shares held by trustee	No specific requirement.	To clarify that the trustee holding unvested shares of a share scheme shall abstain from voting on matters that require shareholders' approval under the Listing Rules. To require disclosure of the number of unvested shares held by the trustee in monthly returns.
Share schemes funded by existing shares		
Disclosure in grant announcements	No specific requirement.	To require disclosure of the terms of the scheme and details of the grants of existing shares consistent with

and financial reports		that applicable to share schemes funded by issuance of new shares.
Voting rights of unvested shares held by trustee	No specific requirement.	To clarify that the trustee holding unvested shares of a share scheme shall abstain from voting on matters that require shareholders' approval under the Rules. To require disclosure of the number of unvested shares held by the trustee in monthly returns.
Share schemes of subsidiaries		
Share award schemes	Chapter 17 currently applies to share option schemes of issuer's subsidiaries, but not their share award schemes.	To extend Chapter 17 to govern subsidiaries' share award schemes that are funded by new or existing shares of the subsidiaries.
Share schemes of insignificant subsidiaries		For a share scheme of an insignificant subsidiary (as defined under Chapter 14A of the Listing Rules), to exempt the adoption of the scheme and refreshment of scheme mandate from the shareholders' approval requirement under Chapter 17, if: <ul style="list-style-type: none"> ➤ they are approved by the remuneration committee of the issuer; ➤ the scheme complies with other requirements of Chapter 17; and ➤ the subsidiary is, and remains to be, an insignificant subsidiary.

Transitional arrangements

If the proposals are adopted, the new rules would apply to new share schemes adopted on or after the effective date of the Listing Rule amendments (**Effective Date**).

The Exchange proposes the following transitional arrangements for existing share schemes:

- issuers would be required to comply with the new disclosure requirements from the Effective Date, including announcements of grants of share awards or share options under these schemes and disclosures in interim or annual reports published on or after the Effective Date;
- issuers may continue to grant share awards or share options only to eligible participants under the amended Chapter 17 after the Effective Date;
- for share option schemes, when the issuer refreshes the scheme mandate of its existing schemes, it must follow the amended Chapter 17 and where appropriate, amend the terms of its existing schemes;
- for share award schemes with an advanced specific mandates approved by shareholders, no further refreshment of the scheme mandate is allowed; and
- for share award schemes involving grants of new shares under general mandate, the issuer may continue to grant share awards to eligible participants under the amended Chapter 17 up to the date of the first annual general meeting after the Effective Date. Thereafter, the issuer should amend the terms of the schemes to comply with the amended Chapter 17.

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