

SFC's Guidelines for Market Soundings

The Securities and Futures Commission (the **SFC**) has finalised its Guidelines for Market Soundings (the **Guidelines**). The Guidelines will come into effect on 2 May 2025 and Market Sounding Intermediaries (see definition below) are expected to have completed the corresponding enhancements to their systems, policies and procedures by then.

The Guidelines are anchored on “*confidential information that is entrusted to [a licensed/registered person] by a client, an issuer or an existing shareholder selling or buying in the secondary market*” (defined as **Market Sounding Information**), and a core expectation is for licensed/registered persons to “*protect such information and safeguard its confidentiality*”, the purpose of which goes towards assessing such person’s fitness and propriety.

In our view, the revised proposals set out in the Guidelines are vastly improved from the SFC’s original proposals, and provide much needed clarity to the market. Compared to the SFC’s original proposals, the key changes are that: (i) the scope of application has been narrowed from “non-public information” to certain confidential information (defined as Market Sounding Information); (ii) the restrictions on trading or use of “non-public information” have been dropped; (iii) the Guidelines no longer apply to transactions in debt capital markets and unlisted securities (unless the underlying transaction is price sensitive); (iv) the cleansing requirement for Disclosing Person and the record keeping requirement for Recipient Persons (see definition below) have been dropped; and (v) the required record retention period for Disclosing Persons has been shortened from seven years to two years.

On reflection – noting our year-long conversations with the market in between the SFC’s consultation and its conclusion – we ask ourselves the extent to which the Guidelines are in furtherance of the underpinning of the SFC’s regulatory aims when compared to the state of play before the SFC’s original proposals.

Notwithstanding our reflections, and the SFC’s clarification that the Guidelines are –

“*aimed at assisting intermediaries in their compliance with the Code of Conduct*”;

“*not intended to change, expand or replace the existing insider dealing regime*”; and

“*principles-based, as such when assessing an intermediary’s compliance with the Guidelines, the SFC will adopt a pragmatic approach, taking into account all relevant circumstances, including the size of the intermediary, and any compensatory measures implemented by its senior management*”;

it was our recommendation (when the consultation first came out¹) and remains our recommendation that regulated intermediaries should conduct a review of their existing controls, policies, and procedures against the Guidelines.

On this note, we have summarised the requirements in the Guidelines in a two-pages fact sheet attached to this briefing.

¹ See our 16 November 2023 client briefing: <https://riskandcompliance.freshfields.com/post/102isnh/hong-kong-sfcs-new-conduct-standards-on-market-sounding>.

Scope of the Guidelines

<p>What does “market sounding” mean? A “market sounding” refers to the communication of information with potential investors, prior to the announcement (if any) of a transaction, to gauge their interest in a possible transaction and assist in determining the terms and specifications related to it, such as its potential timing, size, pricing, structure and trading method.</p> <p>What is Market Sounding Information? Confidential information that is entrusted to a Disclosing Person by a client, an issuer, or an existing shareholder selling or buying in the secondary market (a Market Sounding Beneficiary).²</p>	<p>Who are subject to the Guidelines? A licensed/registered person who:</p> <ul style="list-style-type: none"> discloses Market Sounding Information (a Disclosing Person); and receives Market Sounding Information (a Recipient Person), during the course of a market sounding. <p>Disclosing Persons and Recipient Persons are collectively referred to as Market Sounding Intermediaries.</p>	<p>When are the Guidelines relevant? Market soundings conducted “in Hong Kong” in connection with a possible transaction in:</p> <ul style="list-style-type: none"> shares that are listed on an exchange; and any other securities which are likely to materially affect the price of shares that are listed on an exchange. <p>Guidelines are not limited to Hong Kong-listed issuers, ie irrespective of the listing venue; not generally extended to market soundings conducted out of Hong Kong, with exceptions³.</p>	<p>What is the legal and regulatory standing of the Guidelines?</p> <ul style="list-style-type: none"> Do not have the force of law Do not override the provision of any law Set down expected standards of conduct applicable to Market Sounding Intermediaries Failure to comply may cause the SFC to consider the person’s fitness and propriety to remain licensed or registered
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What are the conduct expectations on a Market Sounding Intermediary when handling Market Sounding Information?
A Market Sounding Intermediary should:

- protect Market Sounding Information and safeguard its confidentiality; and
- ensure there is an effective system of functional barriers to prevent inappropriate disclosure, misuse and leakage of Market Sounding Information (the **Core Obligations**).

The Core Obligations end when the Market Sounding Intermediary no longer has a duty of confidentiality towards the handling, safeguarding, or sharing of the subject Market Sounding Information.

What are the governance and oversight requirements on a Market Sounding Intermediary?
A Market Sounding Intermediary must:

- designate a committee or person(s) with adequate knowledge of its internal policies and procedures governing market soundings to monitor market soundings in support of senior management’s oversight; and
- develop and implement appropriate managerial and supervisory processes, procedures and control measures to ensure that matters related to market soundings are promptly brought to the attention of senior management and designated committee or person(s) for review and follow-up actions to be taken, where necessary.

Specific requirements for Disclosing Persons

<p>Prior to a market sounding</p> <ul style="list-style-type: none"> Obtain agreement or consent from Market Sounding Beneficiary to engage in market soundings <p>Determine in advance:</p> <ul style="list-style-type: none"> a standard set of information to be disclosed in each market sounding an appropriate timing to conduct market soundings a suitable number of Recipient Persons or other potential investors to contact 	<p>Information to obtain from Recipient Persons, or other potential investors, before proceeding with the market sounding</p> <p>Confirmation that the individual receiving the communication was the person authorised to receive market soundings.</p> <p>Consent from the Recipient Person, or other potential investors, to safeguard confidentiality and prevent inappropriate disclosure, misuse or leakage of Market Sounding Information.</p> <p>Any preliminary information provided prior to receiving the consent should be:</p> <ul style="list-style-type: none"> on a “no-name” basis; and sufficiently broad, limited, vague and anonymised. 	<p>What can be said during a market sounding?</p> <p>A Disclosing Person must adopt the use of a standardised script which contains the minimum required content set out in the Guidelines.</p> <p>The script must be pre-approved and regularly reviewed by senior management or independent functions, such as Legal and Compliance.</p>	<p>Requirements on communication channels and record keeping</p> <p>A Disclosing Person must only use communication channels that are authorised by senior management or independent functions, such as Legal and Compliance, to conduct market soundings.</p> <p>Market soundings conducted by telephone or through other recorded communication channels (eg, audio, video, or text) should be recorded.</p> <p>A Disclosing Person must keep records for a period of not less than two years.</p>
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Specific requirements for Recipient Persons: A Recipient Person should (a) **authorise** a person to receive market soundings, and **inform** Disclosing Persons of such upon being contacted for market soundings; (b) **inform** Disclosing Persons whether it wishes to receive market soundings; and (c) when a Disclosing Person does not specify whether the communication is a market sounding, use reasonable effort to **verify** whether it is in possession of Market Sounding Information.

² One of the key factors would be establishing whether the Market Sounding Intermediary has a duty of confidentiality, trust or care towards the handling and sharing of that information. Some examples include (a) name of the subject security (or specific information that would allow the name of the subject security to be deduced); (b) identity of the Market Sounding Beneficiary; (c) the Market Sounding Beneficiary’s intent to pursue a possible transaction; and (d) the terms of or specifications related to the possible transaction such as its potential timing, size, pricing, structure and trading method.

³ For example, where an overseas affiliate conducts market soundings for a Hong Kong licensed intermediary, that Hong Kong licensed intermediary will still be held responsible for compliance with the Guidelines.