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# Amended Hong Kong listing rules on share schemes

Rossana Chu
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**The amended listing rules will become effective on 1 January 2023.**

Issued in July 2022, Hong Kong Stock Exchange's conclusions to the earlier consultation on the amended listing rules regarding share schemes have been issued by the exchange following consultation. This article summarises the amendments that become effective on 1 January 2023.

## TYPES OF SCHEMES

Listed companies often incentivise employees and other eligible participants by non-cash means, including being linked to the value of company shares. Common types of share-based incentive schemes include:

1. The company may grant options to participants for subscribing for new shares at a conversion price. If the market price of the shares rises above the conversion price, the participants may exercise those share options by paying the conversion price, and profit from the share price appreciation. The existing listing rules have a specific chapter governing share option schemes, including the conversion price – which has to be fixed at the market price level of the grant time – and the maximum amount of options subject to the scheme.
2. Another type is a share award scheme, where the listed company purchases existing shares from the open market with its own money, and makes grants to participants who may or may not be required to pay for the shares.
3. In recent years, more companies have set up share award schemes issuing new shares to participants.

The stock exchange realises the increasing popularity of types (2) and (3) of share schemes, and has decided to include them in the amended listing rules.

## SCHEME MANDATE

The mandate limit for all schemes together must not exceed 10% of the shares in issue. The limit can be refreshed after three years from shareholders' approval of the scheme, or the last refreshment. The purpose is to control the dilutive effect of the schemes. Nevertheless, the stock exchange may grant a waiver to this 10% limit on a case-by-case basis, such as the listed company having a strategy to make large share grants to recruit or incentivise talent.

## ELIGIBLE PARTICIPANTS

Share option schemes were supposed to reward officers and employees, but many listed companies have made grants to others including officers of their controlling shareholders and certain service providers. This wide diversity of participation aroused concerns of unjustified dilution to shareholders and conflicts of interest.

The amended listing rules require share schemes to have only three types of eligible participants, namely:

1. Employee participants, being directors and employees of the listed company and its subsidiaries;

2. Related entity participants, being directors and employees of the listed company's holding companies, fellow subsidiaries and associated companies; and

3. Service providers who provide services to the listed group on a continuing or recurring basis. They may be independent contracts where the continuity and frequency of their services are akin to those of employees. Placing agents and financial advisers providing advisory services for fundraising or mergers and acquisitions are ineligible, and so are auditors and valuers who provide assurance or services with impartiality and objectivity.

## MINIMUM VESTING PERIOD

The listing rules will expect that each participant may only fully exercise the share options or obtain the shares after at least 12 months following the grants. However, grants to employee participants may be made with a shorter vesting period under specific circumstances set out in the scheme rules. This exception is not allowed for related entity participants or service providers,

## PERFORMANCE AND CLAWBACK

Scheme rules will be required to describe the performance targets (if any) attached to options or awards, and to disclose the clawback mechanism (if any) to recover or withhold any awards or options granted. Where grants are made without performance targets and/or clawback mechanism, the board of directors or its remuneration committee must provide their views on the reasons for making such grants,

## OTHER AMENDMENTS

Shareholders' approval is required if a grant is made to:

1. An individual participant in excess of 1% of the shares in issue;

2. A director (other than an independent non-executive director) or the chief executive of the listed company of awards which will result in shares issued (and to be issued) in all awards granted in the 12-month period representing more than 0.1% of the shares in issue; or

3. An independent non-executive director, or a substantial shareholder of the listed company of awards or options, which will result in the shares issued (and to be issued) in all awards and options granted in the 12-month period representing more than 0.1% of the shares in issue.

When a grant is made, the listed company must make an announcement. Disclosure must be made on an individual basis for:

1. A connected person;

2. A participant with grants in excess of the 1% individual Limit; and

3. A related entity participant or service provider with grants in excess of the above-mentioned 0.1% threshold.

The amendments include disclosure requirements in the listed company's annual and interim reports, and the work performed by the remuneration committee in the corporate governance report.

## IMPLEMENTATION

The amended listing rules will become effective on 1 January 2023. Any share scheme to be adopted from this effective day onward must comply with the new rules. Grants may be made from that day under the pre-existing schemes, but only to the three types of eligible participants,

# KEY CONTACT

**Rossana Chu**
**Managing partner**
Rossana.Chu@eylaw.com.hk
+852 2629 1768

## Contact us

**LC Lawyers LLP**
Suite 3106,
31/F One Taikoo Place,
979 King's Road,
Quarry Bay, Hong Kong
Tel: (852) 2629 3200
Fax: (852) 2956 1980
https://www.eylaw.com.hk/en_hk

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