CSRC issued new rules to restrict the sale of shares

CSRC has just issued the *Rules on the Sale of Shares by Major Shareholders, Directors, Supervisors and Senior Management of Listed Companies* ("**Rules**"), which will become effective as from 9 January 2016. This initiative is an important confirmation of CSRC's continued determination to stabilize the Chinese stock markets.

CSRC's Notice No. 18 issued on 8 July 2015 was one of the most note-worthy "bail-out" measures taken by the PRC regulator to stabilize the volatile A Share market last summer. It prohibited any controlling shareholder or shareholder of over 5% shareholding (jointly referred to as a "**Major Shareholder**"), director, supervisor or senior management of a listed company (collectively the "**Covered Shareholders**") from reducing its shareholding through trading on the secondary market for six months as from 8 July 2015.

This period has passed and the effect of Notice No. 18 would expire by 8 January 2016. As a result, the market has been increasingly concerned about the systematic risks which might arise if there were to be sale of shares by Covered Shareholders in large volumes.

Focus of the Rules

In order to continuously stabilize the stock market, the CSRC issued the Rules on 7 January 2016 to immediately succeed Notice No. 18 upon its expiry. Different from Notice No. 18, the Rules focus more on the sale of shares by Major Shareholders rather than all the Covered Shareholders (which also include directors, supervisors and senior management of listed companies). In addition, the Rules put more restrictions on the sale of shares by mandating trading through centralized bidding on the exchanges rather than other means such as transfer by agreement or block trading.

While not expressly stated, the Rules should only apply to the sale of A Shares according to the regulatory intention of the CSRC.

General exception

It is important to note that the sale of shares purchased by the Major Shareholders through the secondary market is not subject to the restrictions under the Rules.

Ongoing limitations

In addition, the sale of shares by a Major Shareholder through centralized bidding on the exchanges is subject to the following ongoing limitations:

- the shareholding reduced by a Major Shareholder within three months must not exceed 1% of the listed company's total shares; and
- a Major Shareholder must disclose its shares sale plan 15 trading days prior to its first sale on the exchange.

It is worth noting that both the Shanghai and Shenzhen Stock Exchanges have respectively issued their standard forms of shares sale plan to meet the above disclosure requirement. Both exchanges have clarified that a listed company's total shares should include shares issued domestically and overseas, where applicable.

The Rules also clarified that its restrictions would extend to judicial enforcement and involuntary sale for the purpose of enforcing a share pledge.

Penalties

A Covered Shareholder that does not comply with the Rules will be subject to administrative measures or penalties imposed by the stock exchange and/or CSRC. These penalties range from a written warning, public censure, trading restriction to a ban on securities market entry, depending on the seriousness of the misconduct in issue.

We will continue to monitor the progress of this regulatory development closely and provide updates accordingly.

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