Part XIV

OFFENCES RELATING TO DEALINGS IN SECURITIES AND FUTURES CONTRACTS, ETC

The reader of this Ordinance must be careful about the definitions of various terms. Schedule 1 to this Securities and Futures Ordinance (Cap.571) sets out all definitions which have general application across this Ordinance. The opening Division of a Part within the main body of the Ordinance sets out definitions of terms that are specific to that particular Part. Definitions of terms that are solely used in a single provision are found in the last subsection of each section. For example, "financial product" is defined in Schedule 1 for the purpose of this Ordinance generally. But this term is again separately defined in Schedule 9 to the Ordinance to have a different meaning in the context of insider dealing.

Long Title

An Ordinance to consolidate and amend the law relating to financial products, the securities and futures market and the securities and futures industry, the regulation of activities and other matters connected with financial products, the securities and futures market and the securities and futures industry, the protection of investors, and other matters incidental thereto or connected therewith, and for connected purposes.

[1 April 2003] *L.N. 12 of 2003*

(Enacting provision omitted—E.R. 2 of 2012)

(Originally 5 of 2002)

(*Format changes—E.R. 2 of 2012)

1. Short title

(1) This Ordinance may be cited as the Securities and Futures Ordinance.

(2) (Omitted as spent—ER 2 of 2012)

COMMENTARY

Enactment History

[1.01] As a White Bill for consultation (Special Supplement No. 5 to Government Gazette dated 7 April 2000). The Blue Bill was gazetted on 24 November 2000 and its first reading in the Legislative Council was on 29 November 2000. A Bills Committee was formed in December 2000 to study the Securities and Futures Bill and the Banking (Amendment) Bill 2000. The Securities and Futures Ordinance was passed by the Legislative Council on 13 March 2002.

2. Interpretation

(1) Schedule 1 contains interpretation provisions which apply to this Ordinance in accordance with their terms.

(2) Individual Parts and provisions of this Ordinance contain interpretation provisions which have application in accordance with their terms.

(3) The Commission may, by notice published in the Gazette, amend Parts 2, 3, 4 and 5 of Schedule 1.

COMMENTARY

Overview

The Securities and Futures Ordinance is based upon a number of important definitions. **[2.01]**

Given the volume and importance of the definitions, the interpretation provisions are primarily set out in Part 1 to Schedule 1 of the SFO. While the definitions of general application are located in Part 1 to Schedule 1 of this Ordinance, specific definitions applying to the particular Parts of the SFO are set out in the opening provision of that relevant Part. Furthermore, definitions of terms that are relevant to a single section or the sections within a Part of the Ordinance are often set out at the end of a particular section of the relevant Part of the Ordinance.

the SEHK and the SFC with the duty of acting in the public interest, it is for those bodies (and not the Court) to determine what is or is not in the public interest. In this case, the applicant applied for leave to apply for judicial review against the listing of a company with main business of casino gambling in Macau. The Court refused to grant leave.

Defining relevant terms under this section 5

[5.03] 'Function' is defined in Schedule 1 to the SFO as including "power and duty". See s.6 of the SFO below for the listed duties of the SFC.

'Securities and futures industry' is defined as the securities and futures market and participants (other than investors) therein (including recognized exchange companies, recognized clearing houses, recognized exchange controllers, recognized investor compensation companies and persons carrying on any regulated activity), and any activities related to financial products that are carried on in such securities and futures market or by such participants.

'Recognised exchange companies' refers to companies recognised as exchange companies under s.19(2) of the SFO, which currently includes the Stock Exchange of Hong Kong Limited ('SEHK'), a wholly owned subsidiary of the Hong Kong Exchanges and Clearing Limited ('HKEx'), which operates the Stock Exchange of Hong Kong.

'Recognised clearing houses' refers to companies recognised as clearing houses under subsequent s.37(1) of the SFO, which currently includes the Hong Kong Securities Clearing Company ('HKSCC') a wholly owned subsidiary of HKEx, and operates the Central Clearing and Settlement System ('CCASS').

'Recognised exchange controllers' refers to companies recognised as exchange controllers under subsequent s.59(2) of the SFO, which currently includes the HKEx.

'Recognised investor compensation companies' refers to companies recognised as investor compensation companies under subsequent s.79(1) of the SFO, which currently includes the Investor Compensation Company Limited ('ICC').

'Relevant provisions' refers to the provisions under this Ordinance and Parts II and XII of the (predecessor) Companies Ordinance (Cap.32) insofar as those Parts relate to prospectuses, the purchase by a corporation of its own shares, a corporation giving financial assistance for the acquisition of its own shares, or advertisements concerning prospectuses. It should be noted that prospectuses are not provided for in the new Companies Ordinance

(Cap.622). However, note that the prospectus provisions remain in the unrepealed parts of Cap.32, which is renamed the Companies (Winding-Up and Miscellaneous Provisions) Ordinance. Provisions on prospectuses in the Companies Ordinance will be dealt with in a separate review by the Securities and Futures Commission in due course.

'Registered institutions' means authorised financial institutions registered under subsequent s.119 of the SFO. An authorised financial institution is defined in the Banking Ordinance (Cap.155) as banks, restricted licence banks, or deposit-taking companies.

'Financial products' includes securities, futures contracts, collective investment schemes, leveraged foreign exchange contracts, and under recent amendments to this Ordinance, any structured product. These are defined extensively in s.1A, Part 1, Schedule 1 of the SFO.

'Public' refers to the public of Hong Kong.

'Performance', in relation to a function, includes the discharge of duties or exercise of power.

'Intermediaries' refers to licensed corporations or registered institutions - licensed corporations are those corporations granted a licence under subsequent sections 116 or 117 of the SFO.

'Associated entities' refer to companies which are in a controlling entity relationship with an intermediary and receives and holds client assets of the intermediary in Hong Kong. 'Controlling entity' and 'controlling entity relationship' are defined extensively in section 1, Part 1 of Schedule 1 of the SFO.

6. General duties of Commission

(1) In performing its functions, the Commission shall, so far as reasonably practicable, act in a way which –

(a) is compatible with its regulatory objectives; and

(b) it considers most appropriate for the purpose of meeting those objectives.

(2) In pursuing its regulatory objectives and performing its functions, the Commission shall have regard to –

(a) the international character of the securities and futures industry and the desirability of maintaining the status of Hong Kong as a competitive international financial centre;

(b) the desirability of facilitating innovation in connection with financial products and with activities regulated by the Commission under any of the relevant provisions;

> 33. It may often be that a committee will have to go by its "feel" in relation to a given application. But the committee must still ground such "feel" in stated reasons. It may be that the "feel" cannot be fully articulated in words or reduced to a neat numerical calculus. But the membership should at least give a "ball-park" figure or guideline of what it expects from an applicant. The strict application of that "ballpark" figure or guideline could then be left to the discretion of a committee in light of the special circumstances of a given case."

The Court therefore acknowledged and held that a recognized exchange company is indeed a self-regulating body, but certain rules, procedures, and limits must be imposed and as such, does not give it *carte blanche* to apply its rules without regard to principles of fairness.

Statutory declaration

[23.04] Subsections 23(6) to 23(9) of the SFO deal with statutory declarations which were required to be made pursuant to the rules of a recognized exchange company. They were introduced in 2004 to deal with the difficulty which arose in the matter of *R v Low Robert Eli* [1996] 4 HKC 125. With respect to that case, Sears J queried if a form required by the Listing Committee of the Stock Exchange to be executed by a director had to comply with the requirements of a statutory declaration required by the Oaths and Declarations Ordinance (Cap.11), when there is nothing in the said Ordinance relating to the Stock Exchange which required this type of formality to be given:

> "… [Mr. Robert Eli Low] practised as a partner in a firm of solicitors until his retirement in 1995. In that year, he became a director of Sincere Co Ltd which is a publicly listed company on the Hong Kong Stock Exchange. He made a return and declaration with regard to directors which was required, called Form B, to the Managing Committee of the Stock Exchange known as the Listing Committee. It is an unusual form in that it appears on its face to be a declaration made under the Oaths and Declarations Ordinance (Cap.11). It says "Every director must execute this declaration as a statutory declaration." There is no requirement, as I understand it, in the Ordinance relating to the Stock Exchange for this type of formality to be given as to a declaration by a director. If the Ordinance does not require it, I query whether the Stock Exchange is entitled to insist that it must be executed, but whatever the position, the piece of paper which Mr. Low had signed had been filled up …"

The introduction and enactment of these subsections 23(6) to 23(9) of the SFO therefore made it clear that the Stock Exchange is entitled to request that statutory declarations and is able to take into account the standards imposed on professionals by law and under professional conduct.

24. Approval of rules or amendments to rules of recognized exchange company

(1) Subject to subsection (7), no rule (whether or not made under section 23) of a recognized exchange company or any amendment thereto shall have effect unless it has the approval in writing of the Commission.

(2) A recognized exchange company shall submit or cause to be submitted to the Commission –

(a) for its approval the rules and every amendment thereto that require approval under subsection (1), together with explanations of their purpose and likely effect, including their effect on the investing public, in sufficient detail to enable the Commission to decide whether to approve them or refuse to approve them; and

(b) for its information the rules which belong to a class the subject of a declaration under subsection (7) and every amendment to the rules, as soon as reasonably practicable after they have been made.

(3) The Commission shall, not later than 6 weeks after the receipt of a submission under subsection (2)(a) from a recognized exchange company, by notice in writing served on the company, give its approval or refuse to give its approval (together with its reasons for the refusal) to the rules or amendment of the rules (as the case may be) or any part thereof, the subject of the submission.

(4) The Commission may give its approval under subsection (3) subject to requirements which shall be satisfied before the rules or amendment of the rules or any part thereof take effect.

(5) The Commission may in a particular case, with the agreement of the recognized exchange company concerned, extend the time prescribed in subsection (3).

(6) The Financial Secretary may, after consultation with the Commission and the recognized exchange company concerned, extend the time prescribed in subsection (3).

(7) The Commission may, by notice published in the Gazette, declare any class of rules of a recognized exchange company to be a class of rules which are not required to be approved under subsection (1) and, accordingly, any rules of the company which belong to that class (including any amendment thereto) shall have effect notwithstanding that they have not been so approved.

(8) Neither the rules under section 23 nor a notice under subsection (7) is subsidiary legislation.

COMMENTARY

Predecessor provisions

[42.01] Section 42 was based upon s.103 of the repealed Commodities Trading Ordinance (Cap.250). This section came into effect on 1 April 2003.

Commission's power to request documents, records, etc. from a recognized clearing house

[42.02] In the same fashion as of previous section 27 of the SFO, this 42 section continues to facilitate the overall check and balance system between the Commission and the recognized clearing house. Simply put, this provision empowers the Commission to request from a recognized clearing house any and all books, records, and other sources/mediums of information relating to that clearing house's business, clearings, or other settlement arrangements in regards to any transaction in securities and futures contracts as the Commission sees fit and may be required to be produced.

43. Withdrawal of recognition of clearing house and direction to cease to provide facilities

(1) Subject to subsections (3), (4) and (5), the Commission may, after consultation with the Financial Secretary, by notice in writing served on a recognized clearing house –

(a) withdraw the company's recognition as a clearing house with effect from a date specified in the notice for the purpose; or

(b) direct the clearing house to cease to provide or operate with effect from a date specified in the notice for the purpose such clearing or settlement facilities as are specified therein.

(2) The Commission may by the notice served under subsection (1) permit the recognized clearing house to continue, on or after the date on which the withdrawal or direction is to take effect, to carry on such activities affected by the withdrawal or direction as the Commission may specify in the notice for the purpose of –

(a) closing down the operations of the clearing house; or

(b) protecting the interest of the investing public or the public interest.

(3) The Commission may only serve a notice under subsection (1) in relation to a recognized clearing house that –

(a) fails to comply with any requirement of this Ordinance or with a condition imposed under section 37;

(b) is being wound up;

(c) ceases to operate as a clearing house; or

(d) requests the Commission to do so.

(4) Except where responding to a request under subsection (3)(d), the Commission shall not exercise its power under subsection (1) in relation to a recognized clearing house unless it has given the clearing house a reasonable opportunity of being heard.

(5) Except where responding to a request under subsection (3)(d), the Commission shall give the recognized clearing house not less than 14 days' notice in writing of its intention to serve a notice under subsection (1) and the grounds for doing so.

(6) Where the Commission withdraws a company's recognition as a clearing house under subsection (1)(a), it shall cause notice of that fact to be published in the Gazette.

(7) Where the Commission directs under subsection (1)(b) a recognized clearing house to cease to provide or operate any clearing or settlement facilities, it shall cause notice of the particulars of the direction to be published in the Gazette.

(8) A notice served under subsection (1)(a) shall not take effect –

(a) subject to paragraph (b), until the expiration of the period within which an appeal against the notice may be made under section 44; or

(b) if an appeal against the notice is made under section 44, until the appeal is withdrawn, abandoned or determined.

(9) A notice served under subsection (1)(b) shall take effect immediately.

COMMENTARY

Predecessor provisions

[43.01] The wording of this section 43 of the SFO was modelled on the previous section 28 of this Ordinance as there is no predecessor equivalent Hong Kong legislation. This section came into effect on 1 April 2003.

Sanction against recognised exchange company

[43.02] Similiar to the corollary section 28, this section 43 of the SFO provides and lists those instances and circumstances where the Commission may withdraw and terminate the recognition of a clearing house which includes directing the company to cease the provision of facilities and/or services. Subsection 43(1) of the SFO specifically words that the Commission is so empowered to withdraw and terminate a company's recognition as an exchange company and order it to cease all operations upon consultation with the Financial Secretary.

Accordingly, a recognized clearing house's failure to discharge its statutory duties properly may subject the company to sanctions posted and implemented

Overview

[62.02] Section 62 of the SFO gives the Financial Secretary the "exemption" power from those qualifications as prescribed in previous section 59(1) of this Ordinance when he is satisfied it is appropriate: (i) to do so in the interest of the investing public or in the public interest; or (ii) for the proper regulation of markets in securities or futures contracts.

Note that the Financial Secretary, in turn, may also revoke such an exemption on the same above mentioned grounds that a company may be recognized as a recognized exchange controller.

63. Duties of recognized exchange controller

(1) It shall be the duty of a recognized exchange controller which is a controller of a recognized exchange company or recognized clearing house to ensure so far as reasonably practicable –

(a) an orderly, informed and fair market in securities or futures contracts traded on the stock market or futures market operated by the recognized exchange company or through the facilities of the company;

(ab) an orderly, informed and fair market in OTC derivative products traded through the facilities of the recognized exchange company; (Added 6 of 2014 s. 7)**

(b) that there are orderly, fair and expeditious clearing and settlement arrangements for any transactions in securities, futures contracts or OTC derivative products cleared or settled through the facilities of the recognized clearing house; (Amended 6 of 2014 s. 7)**

(c) that risks associated with its business and operations are managed prudently;

(d) that the recognized exchange company or recognized clearing house (as the case may be) complies with any lawful requirement placed on it under any enactment or rule of law and with any other legal requirement placed on it.

(2) In discharging its duty under subsection (1)(a), (b) or (c), a recognized exchange controller shall –

(a) act in the interest of the public, having particular regard to the interest of the investing public; and

(b) ensure that the interest of the public prevails where it conflicts with the interest of the recognized exchange controller.

** *Amended as 6 of 2014 as these terms just came into effect this past 10 July 2015.*

COMMENTARY

Predecessor provisions

Section 63 was based upon s.8 of the repealed Exchanges and Clearing Houses (Merger) Ordinance (Cap.555). This section came into effect on 1 April 2003. [63.01]

Duties imposed on an exchange controller

[63.02] In furtherance of the Commission's regulatory objectives and functions, the Commission is tasked with supervising, monitoring and regulating the activities carried out by the recognized exchange controller. Subsection 63(1) stipulate the specific duties of a recognized exchange controller, including: (i) the duty to ensure orderly, fair and informed market place; (ii) that there is an expeditious clearing and settlement arrangements; (iii) that risks associated with its business and operations are managed prudently; and (iv) all participants and associates are acting within compliance of the law.

Furthermore, subsection 63(2) prescribes that in discharging its duties, a recognized exchange controller house has to: (i) act in the interest of the public, having particular regard to the interest of the investing public; and (ii) ensure that the interest of the public prevails where it conflicts with its own interest.

While the SFO does not set out detailed regulatory requirements in respect of recognized exchange controllers, the Commission has always made reference to international best practices and standards for the purposes of carrying out its functions in relation to recognized clearing houses. The Commission further notes that the main policy objectives behind the Principles for Financial Market Infrastructures (PFMIs) are consistent with the regulatory objectives of the Commission under the Ordinance. In addition, the specific duties of recognized exchange controller, as prescribed in this s.63 of the SFO, are also in line with the PFMIs.

The Commission considers that all recognized exchange controllers are systemically important financial market infrastructures in Hong Kong. Therefore, the Commission has adopted these PFMIs as benchmarks against which to assess recognized exchange controllers in the course of carrying out its function to supervise, monitor and regulate them.

As listed, the duties imposed on a recognized exchange controllers include:

1. to ensure an orderly, fair and informed market structure;
2. to ensure the efficient and expeditious clearing and settlement arrangement;
3. to ensure careful and prudent management of risks; and

established pursuant to the Deposit Protection Scheme Ordinance (Cap.581). This Deposit Protection Scheme Ordinance was devised to provide compensation to those depositors in the event of the insolvency of that licensed bank. As such, where the compensation is provided to the claimant under the scheme created by the Hong Kong Deposit Protection Board, it is the Board that is *entitled* to the right of subrogation against the defaulting/insolvent party. See Deposit Protection Scheme Ordinance (Cap.581), s.38.

Extent of subrogation when the claimant is partially compensated

[87.04] Subsection 87(1)(a) of the Ordinance spells out that in those instances where the claimant has received payment which partially compensates the claimant's loss, the investor compensation company is able to exercise its subrogation right only to the extent of the monies still owed to the claimant. See *Re Forluxe Securities (In Liquidation)* (unrep., HCCW 310 and 311, 20 December 2000); see also *Re Law Siu Kong Christopher* (unrep., HCMP 2477/2002). This equates to the fact that the claimant would accordingly be entitled to exercise its right to commence an action against the defaulting party with respect to the uncompensated amount still owed. However, note that the amount recoverable by the investor compensation company on the basis of its subrogated rights *cannot exceed* the amount of compensation that the company actually paid to the claimant which made up the difference that was still owed to the claimant after the partial payment by the defaulting party. See *Re Tiffit Securities (Hong Kong) Ltd* [2007] 1 HKLRD 267.

88. Financial statements of a recognized investor compensation company

(1) Subject to subsection (3), a recognized investor compensation company shall –

(a) prepare such financial statements and other documents, for such periods, as are prescribed by rulescmade under section 397 for the purposes of this section; and

(b) submit the financial statements and other documents, together with an auditor's report, to the Commission not later than 4 months after the end of the financial year to which they relate.

(2) Without limiting the generality of subsection (1), the requirements under that subsection relating to the financial statements and other documents, and the auditor's report, referred to in that subsection include the requirements that –

(a) the financial statements and other documents are to relate to such matters and contain such particulars as are prescribed by rules made under section 397 for the purposes of this section;

(b) the auditor's report is to contain such particulars, including such statement of opinion, as are prescribed by the rules;

(c) the financial statements and other documents, and the auditor's report, are to be prepared in accordance with such principles or bases as are prescribed by the rules; and

(d) without limiting the generality of section 387 of the Companies Ordinance (Cap.622), the financial statements and other documents are to be signed by the chief executive officer of the recognized investor compensation company, by which they are prepared. (Amended 28 of 2012 ss.912 & 920)

(3) On an application in writing by the recognized investor compensation company by which any financial statements and other documents, and any auditor's report, are required under subsection (1) to be submitted, the Commission may, where it is satisfied that there are special reasons for so doing, extend the period within which the financial statements and other documents, and the auditor's report, are required to be submitted, for such period and subject to such conditions as the Commission considers appropriate, and upon the Commission granting the extension, subsection (1) shall apply subject to the extension accordingly.

(4) A recognized investor compensation company shall cause a copy of each of the financial statements and other documents and the auditor's report that are required under subsection (1) to be submitted by it to be sent to the Financial Secretary and to be published in the Gazette.

(5) A reference in this section to financial statements shall not be construed as including a reference to financial statements of the compensation fund.

COMMENTARY

Predecessor provisions

[88.01] This section came into effect on 1 April 2003 as it has no equivalent predecessor legislation.

Requirement of an investor compensation company to submit financial statements and documents

[88.02] Section 88 of the Ordinance, working in conjunction with the Commission's rule-making power granted to it under subsequent section 397 of the Ordinance, empowers the Commission to require a recognized investor

(b) for the payment of different fees by or in relation to persons or cases of different classes or descriptions;
(c) for the time and manner of payment of the fees;
(d) that the payment of any fees may, either generally or in a particular case, be reduced, waived or refunded;
(e) that the Monetary Authority may recover any outstanding amount of the fees as a civil debt due to the Monetary Authority; and
(f) for any other matters relating or incidental to a matter mentioned in paragraph (a), (b), (c), (d) or (e).

(3) This section is in addition to and not in derogation of sections 29 and 29A of the Interpretation and General Clauses Ordinance (Cap.1).

COMMENTARY

Summary

[101M.01] This new provision empowers the Securities and Futures Commission to charge any fees that it deems necessary in regards to these mandatory reporting, clearing, trading and record keeping obligations in respect of OTC derivative transactions as related to the Hong Kong Money Authority.

101N. Rule making power—clearing obligation

Remarks: Not yet in operation

(1) The Commission may, with the consent of the Monetary Authority and after consultation with the Financial Secretary, make rules—
(a) generally for the purposes of the clearing obligation; and
(b) without limiting paragraph (a), to prescribe the particular matters set out in this section.

(2) Rules made under this section—
(a) may specify for the purposes of paragraph (b)(iv) of the definition of ***prescribed person*** in section 101A, a class or description of persons; and
(b) must provide in relation to a person of such a class or description that the person is subject to the clearing obligation only if the person is a counterparty to a specified OTC derivative transaction.

(3) Rules made under this section—
(a) may specify generally, or with reference to a class or description of transactions, the OTC derivative transactions that are subject to the clearing obligation; and

(b) without limiting paragraph (a), may provide that an OTC derivative transaction is subject to the clearing obligation—
(i) even if a counterparty or more than one counterparty is a person outside Hong Kong;
(ii) except in relation to a person of a class or description specified under subsection (2), even if a prescribed person is not a counterparty to the transaction; or
(iii) even if the transaction is entered into or conducted wholly or partially outside Hong Kong.

(4) Without limiting subsection (3), OTC derivative transactions may be specified under that subsection with reference to any factor relating to an OTC derivative transaction, including—
(a) the underlying subject matter of the transaction;
(b) the features or characteristics of the transaction; and
(c) the persons involved in the transaction.

(5) Rules made under this section may specify—
(a) the circumstances relating to a specified OTC derivative transaction in which the clearing obligation—
(i) applies;
(ii) does not apply; or
(iii) is taken to have been complied with;
(b) the criteria (including thresholds) for the application of the clearing obligation; and
(c) different circumstances and criteria for different prescribed persons or different OTC derivative transactions.

(6) Rules made under this section may specify—
(a) the manner in which a specified OTC derivative transaction is to be cleared with a designated CCP;
(b) the period within which the clearing obligation must be complied with;
(c) the circumstances in which a specified OTC derivative transaction that is cleared otherwise than with a designated CCP is treated, for the purposes of the clearing obligation, as having been cleared with a designated CCP;
(d) that a prescribed person may clear a specified OTC derivative transaction with a designated CCP directly or through a third party; and
(e) that a subsidiary specified under section 101C(5) that is a counterparty to a specified OTC derivative transaction may clear the transaction with a designated CCP directly or through a third party.

"Approved person" in relation to the issue of an advertisement, invitation or document, means an individual approved by the SFC under s.105(3) for the purpose of being served by the SFC with notices and decisions for the issue. See [105.02].

"Document"

[102.04] "Document" means any publication (including a newspaper, magazine or journal, a poster or notice, a circular, brochure, pamphlet or handbill, or a prospectus), whether produced mechanically, electronically, magnetically, optically, manually or by any other means; and directed at, or the contents of which are likely to be accessed or read (whether concurrently or otherwise) by, the public.

"Exempted body"

[102.05] "Exempted body" means a body specified in Part 3 of Sch.4, namely: (1) the Government; (2) Hong Kong Housing Authority; (3) Airport Authority; (4) Kowloon-Canton Railway Corporation; (5) Urban Renewal Authority; (6) Hong Kong Export Credit Insurance Corporation; (7) Hong Kong Science and Technology Parks Corporation; (8) Hong Kong Productivity Council; (9) Hong Kong Tourism Board; (10) Hong Kong Trade Development Council; and (11) any other corporation which has any of its shares listed and any wholly owned subsidiary of such a corporation, whether incorporated in Hong Kong or elsewhere.

"Invitation"

[102.06] "Invitation" includes an offer and an invitation, whether made orally or produced mechanically, electronically, magnetically, optically, manually or by any other means.

"Issue"

[102.07] "Issue" has a very broad coverage. "Issue" in relation to any material (including any advertisement (See [102.02]), invitation (See [102.06]) or document (See [102.04])), includes publishing, circulating, distributing or otherwise disseminating the material or the contents thereof, virtually by any means and any medium. It also includes causing or authorising the material to be issued.

An advertisement, invitation or document issued by a person shall be regarded as being issued by him on every day on which he causes or authorises it to be so issued and if issued by one person on behalf of another shall be regarded as issued by both persons, e.g., both the agent and the principal or co-principals. See s.102(2) of the SFO.

"Relevant authority"

"Relevant authority" in relation to a place outside Hong Kong, means an authority which the Hong Kong Monetary Authority (HKMA) is satisfied, is a recognised banking supervisory authority of that place. [102.08]

"Representative"

"Representative" means, in general, the individual who is licensed to carry on a regulated activity in relation to a licensed corporation or a registered institution. [102.09]

"Securities"

The definition for "securities" was added pursuant to s.2(5) of the SPAO. [102.10]

"Securities" within Part IV of the SFO (for convenience, "Part IV Securities") means "securities" in s.1 of Part 1 of Sch.1 to the SFO (for convenience, "Sch.1 Securities") except that it does not include structured products that are securities only because of para.(g) of that definition, i.e., excluding a structured product which is offered to the public. In other words, *Part IV Securities means Sch.1 Securities take away para.(g).* Paragraph (g) of Sch.1 Securities provides that "a structured product that does not come within (a) to (f) but in respect of which the issue of any advertisement, invitation or document that is or contains an invitation to the public to do any act referred to in section 103(1)(a) of this Ordinance is authorized, or required to be authorized under section 105(1) of this Ordinance."

The reason for this carve-out appears to be that whether a structured product falls within para.(g) of Sch.1 Securities is determined by reference to s.103(1)(a) or s.105(1) of Part IV, thus the meaning of "securities" within Part IV (Part IV Securities) does not need to include para.(g).

Division 2 – Regulation of Offers of Investments, etc.

103. Offence to issue advertisements, invitations or documents relating to investments in certain cases

(1) Subject to subsections (2), (3) and (5) to (9), a person commits an offence if he issues, or has in his possession for the purposes of issue, whether in Hong Kong or elsewhere, an advertisement, invitation or document which to his knowledge is or contains an invitation to the public –

(a) to enter into or offer to enter into –

(i) an agreement to acquire, dispose of, subscribe for or underwrite securities; or

or (2) where the potential grower contacted a salesman directly (usually on the recommendation of an existing grower); or (3) where the salesman called the potential grower at the request of an existing grower to whom a request had previously been made by the potential grower that the salesman be asked to call him. The salesmen were prohibited from publishing or distributing any advertisement circular relating to the sale of the trees. The company did not advertise or make, other than as above, personal approaches to solicit potential growers. Notwithstanding this, the High Court of Australia held that there was an offer of an interest to the public for subscription or purchase. Mason J said at 136 that:

> "Although the company through the brokers negotiated with members of the public individually, the persons signed up were approached as members of the public. The facts do not suggest that the company or the brokers looked to a particular class of person as growers. The documents contain no hint of any restriction to a class or group of persons having some common characteristic or qualification, except that of possessing the money with which to buy the trees."

In *Corporate Affairs Commission (SA) v Australian Central Credit Union* (1985) 157 CLR 201, a credit union with about 23,000 members proposed to put certain land into a unit trust and to offer a proportion of the units to its members (and only its members) for purchase. The High Court of Australia unanimously held that there was no offer to the public. Mason ACJ, Wilson, Deane and Dawson JJ said at pp.208–210 that:

> "For some purposes and in some circumstances, each citizen is a member of the public and any group of persons can constitute a section of the public. For other purposes and in other circumstances, the same person or the same group can be seen as identified by some special characteristic which isolates him or them in a private capacity and places him or them in a position of contrast with a member or section of the public. In a case where an offer is made by a stranger and there is no rational connection between the characteristic which sets the members of a group apart and the nature of the offer made to them, the group will, at least ordinarily, constitute a section of the public for the purposes of the offer. If, however, there is some subsisting special relationship between offeror and members of a group or some rational connection between the common characteristic of members of a group and the offer made to them, the question whether the group constitutes a section of the public for the purposes of the offer will fall to be determined by reference to a variety of factors of which the most important will ordinarily be: *the number of persons comprising the group, the subsisting relationship between the offeror and the members of the group, the nature and content of the offer, the significance*

> *of any particular characteristic which identifies the members of the group and any connection between that characteristic and the offer* ...
>
> No particular number of persons can be designated as being, of itself, necessarily sufficient or inadequate to constitute the public or a section of the public for every purpose. 'Anything from two to infinity may serve: perhaps even one, if he is intended to be the first of a series of subscribers, but makes further proceedings needless by himself subscribing the whole'. See *Nash v Lynde* (1929) AC 158, at p.169; see also Loss, Securities Regulation, 2nd edn (1961), vol. I, pp.655–656).
>
> The characteristic which sets the proposed offerees apart as a group is both restrictive and well-defined. It is membership of ACCU. The rules of ACCU restrict eligibility for membership by reference to employment and/or residence and prescribe clear procedures for applications for membership and their rejection or acceptance. ... The proposed offer by ACCU to its members would have a perceptible and rational connection with their membership ... [T]he direct interest in the beneficial ownership which a member would acquire by the purchase of a unit would, if all members were to take equal advantage of the opportunity to acquire units, be matched by a diminution of his or her indirect interest, through the credit union, in that ownership. In these circumstances, the offer of units to the members of ACCU would be an offer to them in their domestic or private capacity as members of ACCU. It would arise from their membership, would relate to property in which they would be already indirectly interested as members and would have a perceptible and rational connection with that membership." (Emphasis added)

In a separate judgment, Brennan J said at 213 that:

> "When the offerees' special interest is substantially greater than or substantially different from the interest which the offerees would have had in the subject matter of the offer if the antecedent relationship did not exist, the ground for distinguishing them from a section of the public is substantial. In my opinion the criterion which distinguishes an offer to a group of offerees who are not a section of the public from an offer to a section of the public is this: whether the offerees are members of a group who, by reason of their antecedent relationship with the offeror, have an interest in the subject matter of the offer substantially greater than or substantially different from the interest which others who do not have that relationship would have in the subject matter of the offer. As the ACCU offer to its members was an offer to a group whose relationship with the offeror gave them an interest in the subject matter of the offer substantially greater than

"Professional investor" is defined in Part 1 of Sch.1 of the SFO which includes specified entities, such as banks and insurance companies set out in paras.(a)–(i) of the definition. Paragraph (j) of the definition refers to "any person of a class which is prescribed by rules made under section 397 of this Ordinance for the purposes of this paragraph as within the meaning of this definition …", namely the Securities and Futures (Professional Investor) Rules (Cap.571D) (PI Rules). Following the enactment of the Securities and Futures (Professional Investor) (Amendment) Rules 2011 ("PI Amendment Rules") which came into effect on 16 December 2011, s.3 of the PI Rules provides that the following persons are prescribed as within the meaning of para.(j) of the definition of "professional investor" for the purpose of any provision of the SFO other than Sch.5:

(1) any trust corporation with total assets of not less than HK$40 million: (i) at the offer date; or (ii) as stated in the most recent audited financial statement prepared for the trust corporation within 16 months before the offer date; or (iii) as ascertained by referring to the custodian statements issued to the trust corporation within 12 months before the offer date;

(2) any individual, either alone or with any of his or her associates on a joint account, having a portfolio of not less than HK$8 million: (i) at the offer date; or (ii) as stated in a certificate issued by an auditor or a certified public accountant of the individual within 12 months before the offer date; or (iii) as ascertained by referring to the custodian statements issued to the individual within 12 months before the offer date;

(3) any corporation or partnership having a portfolio of not less than HK$8 million or total assets of not less than HK$40 million: (i) at the offer date; or (ii) as ascertained by referring to the most recent audited financial statements prepared for the corporation or partnership within 16 months before the offer date; or (iii) as ascertained by referring to the custodian statements issued to the corporation or partnership within 12 months before the offer date; and

(4) any corporation the sole business of which at the offer date is to hold investment and which at the offer date is wholly owned by a trust corporation, an individual, a corporation or a partnership that falls within the descriptions in paragraph 1 to 3 above.

While the issue of marketing materials to professional investors need not obtain SFC authorisation, however, before such issue, an intermediary is still required to comply with the *Code of Conduct* on how to classify professional investors, namely, paras.15.1 to 15.4 of the *Code of Conduct*, including, for example, that the individual is knowledgeable and has sufficient expertise in the relevant products and markets and that the individual formally

agrees in writing that he wishes to be classified as a professional investor.[64] The purposes of the PI Amendment Rules are:

(i) to relax the evidential requirements for classifying a professional investor so that firms may use any methods to satisfy themselves that an investor meets the relevant assets or portfolio threshold at the offer date to qualify as a professional investor;

(ii) to preserve the existing methods set out in the PI Rules so that firms that wish to continue with the existing practices may use the existing methods; and

(iii) to extend the existing scope of s.3(d) to all three types of professional investors under ss.3(a) to 3(c) of the PI Rules, namely, trust corporations, individuals and corporations/partnerships.

The SFC expects proper records of assessment processes to be kept so as to demonstrate that the firms have exercised professional judgment and have reached a reasonable conclusion.[65]

Following a *Consultation Paper on the Proposed Amendments to the Professional Investor Regime and the Client Agreement Requirements* (15 May 2013), the SFC issued the *Consultation Conclusions on the Proposed Amendments to the Professional Investor Regime and Further Consultation on the Client Agreement Requirements* on 25 September 2014 (2014 PI Consultation Conclusions). In summary, the SFC has decided:

(1) to continue allowing Individual Professional Investors (an individual who has a portfolio of not less than HK$8 million) and Corporate Professional Investors (a corporation having a portfolio of not less than HK$8 million or total assets of not less than HK$40 million) to participate in private placement activities if they meet the prescribed monetary thresholds under the PI Rules and to maintain such monetary thresholds at current levels;

(2) not to allow intermediaries to be exempt from the suitability requirement or rely on the other existing Code of Conduct exemptions that are inherently linked with the suitability requirement and/or have significant bearing on investor protection (e.g., the need to enter into a written client agreement) when serving Individual Professional Investors;

[64] Administration's paper on *Definition of Professional Investors and Update on the Progress on Reviewing/Amending the Definition* dated 16 December 2010 (LC Paper No. CB(1)788/10-11/(02)).

[65] SFC's *Consultation Conclusions on the Evidential Requirements under the Securities and Futures (Professional Investor) Rules* dated Feb 2011; SFC's Press Release "SFC gazettes rule changes to refine evidential requirements for proving professional investor status" dated 9 Sep 2011, see <http://www.sfc.hk/sfcPressRelease/EN/sfcOpenDocServlet?docno=11PR105> (accessed 3 Oct 2011).

based on common law misrepresentation or the Misrepresentation Ordinance (Cap.284) are: (1) the definition of 'representation' under s.108 of the SFO includes 'forecasts' which, are not representation of facts that could give rise to remedies under common law misrepresentation or the Misrepresentation Ordinance (Cap.284); and (2) a claim under s.108 of the SFO is confined to compensatory damages. Note that there is no relief for rescission, damages in lieu of rescission, or restitution.

Fraudulent misrepresentation, reckless misrepresentation and negligent misrepresentation

[108.03] Fraudulent misrepresentation, reckless misrepresentation and negligent misrepresentation are separately defined in subs.108(7). The definitions for fraudulent misrepresentation and reckless misrepresentation in subs.108(7) are the same as those in previous subsection 107(3) of the SFO.

Subsection 108(7) herein uses the word "mean" in "fraudulent misrepresentation means …", "reckless misrepresentation means …" and "negligent misrepresentation means …"; the intention appears to be that fraudulent misrepresentation, reckless misrepresentation and negligent misrepresentation in s.108 are understood exclusively as formulated in subs.108(3) of this provision.

Liability of directors

[108.04] Subsection 108(2) provides that if a company or body corporate has made the misrepresentation, the director of the company or body corporate shall be presumed also to have made the misrepresentation unless it is proved that he did not authorise the making of the misrepresentation.

In *Terkild Johan Terkildsen v Barber Asia Ltd* (unrep, HCA 1963/2003, 27 March 2007), Saunders J said at paragraphs 12–13 of s.8(3) of the repealed Protection of Investors Ordinance (Cap.335) (PIO) (the predecessor provision of s.108(2)) as follows:

> "The Protection of Investors Ordinance, by s.8(3), imposes liability on a director of a company, who has not personally made a negligent representation, by way of rebuttable presumption. For a plaintiff to succeed against such a director, he need only establish an appropriate negligent representation inducing him to enter into an agreement, and that that representation was made by some other director or employee of the company. That established, liability is presumed against the other directors, a burden then falling on those other directors to establish that they have neither caused nor authorised the representation.
>
> It must always be open to plaintiff who seeks to bring a cause of action based upon the statutory tort to make a sensible assessment, prior to commencing his proceedings, as to whether or not he wishes to draw into those proceedings all of the directors of the company, other than the person who has actually made the representation upon which reliance was placed. A sensible plaintiff will look at the burden on those other directors to rebut the presumption, and may well say to himself that those other directors may easily meet that burden. He may then, sensibly, elect not to bring them into the action, in order to avoid the risk of costs."

Injunction

[108.05] Subsection 108(3) of this provision is to put beyond doubt that the Court has the power to grant an application made by a party to the proceedings for an injunction order against the other party, e.g., the Court may make an order restricting the manner in which the defendant is permitted to deal with any assets, including any of the plaintiff's assets over which he has control, pending disposal of the claim, thereby serving to prevent the dissipation of assets which may be relevant to the proceedings.[82]

No overlaps with civil liability for misstatements in prospectus under the retitled Cap.32

[108.06] Subsection 108(4) herein provides that s.108 does not confer a right of action to which s.40 of the retitled Cap.32 applies. Section 40 of the retitled Cap.32 essentially provides a statutory cause of action to investors who have subscribed for shares in or debentures in a company and have sustained loss or damage as a result of mis-statements in the prospectus. The intention appears to be to avoid any overlaps in conferring the statutory cause of action to investors between the prospectus regime of the retitled Cap.32 and this Part IV regime.

109. Offence to issue advertisements relating to carrying on of regulated activities, etc.

(1) Subject to subsections (3) to (6), a person commits an offence if he issues, or has in his possession for the purposes of issue –

(a) an advertisement in which to his knowledge –

(i) a person holds himself out as being prepared to carry on Type 4, Type 5, Type 6, Type 9 or Type 11** regulated activity; and

(ii) the person is not licensed or registered for such regulated activity as required under this Ordinance; or

[82] *Part IV of and Schedule 4 to the Securities and Futures Bill Committee Stage Amendments* dated 17 Nov 2001 (Paper No. CSA03/01; LC Paper No. CB(1)358/01-02(02)), Annex 1 at fn 36.

Overview

[138.02] This section deals with annual fees payable by licensed persons and registered institutions, and annual returns by licensed persons (but not registered institutions).

139. Prohibition of use of certain titles

(1) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless:

(a) the person is licensed or registered for Type 1 regulated activity; or

(b) his name is entered in the register maintained by the Monetary Authority under s.20 of the Banking Ordinance (Cap.155) as engaged in respect of Type 1 regulated activity by a person registered for that regulated activity, while acting in that capacity.

(2) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless:

(a) the person is licensed or registered for Type 2 regulated activity; or

(b) his name is entered in the register maintained by the Monetary Authority under s.20 of the Banking Ordinance (Cap.155) as engaged in respect of Type 2 regulated activity by a person registered for that regulated activity, while acting in that capacity.

(3) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless the person:

(a) is licensed for Type 3 regulated activity;

(b) is an authorised financial institution; or

(c) is engaged by an authorised financial institution, while acting for the institution in an activity that would have fallen within the meaning of the definition of "leveraged foreign exchange trading" in Part 2 of Sch.5 but for para.(xii) of that definition.

(4) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless:

(a) the person is licensed or registered for Type 4 regulated activity; or

(b) his name is entered in the register maintained by the Monetary Authority under s.20 of the Banking Ordinance (Cap.155) as engaged in respect of Type 4 regulated activity by a person registered for that regulated activity, while acting in that capacity.

(5) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless:

(a) the person is licensed or registered for Type 5 regulated activity; or

(b) his name is entered in the register maintained by the Monetary Authority under s.20 of the Banking Ordinance (Cap.155) as engaged in respect of Type 5 regulated activity by a person registered for that regulated activity, while acting in that capacity.

(6) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless:

(a) the person is licensed or registered for Type 6 regulated activity; or

(b) his name is entered in the register maintained by the Monetary Authority under s.20 of the Banking Ordinance (Cap.155) as engaged in respect of Type 6 regulated activity by a person registered for that regulated activity, while acting in that capacity.

(7) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless:

(a) the person is licensed or registered for Type 7 regulated activity;

(b) the person is granted an authorisation under s.95(2) to provide automated trading services;

(c) his name is entered in the register maintained by the Monetary Authority under s.20 of the Banking Ordinance (Cap.155) as engaged in respect of Type 7 regulated activity by a person registered for that regulated activity, while acting in that capacity; or

(d) the person is an employee of a person authorised under s.95(2) to provide automated trading services, while acting for that person in that regulated activity.

(8) A person shall not take or use any of the specified titles set out opposite to the reference to this subsection in column 2 of Sch.6 unless the person:

(a) is licensed for Type 8 regulated activity;

(b) is an authorised financial institution; or

(c) is engaged by an authorised financial institution, while acting for the institution in an activity that would have fallen within the meaning of the definition of "securities margin financing" in Part 2 of Sch.5 but for para.(v) of that definition.

(3) Subsection (1) does not apply to:

(a) a person who acts in good faith, believing and having reasonable grounds to believe that he has a right, title, or interest to or in the securities which he sells within the meaning of subs.(1);

(b) a person who, as a representative of an intermediary that carries on Type 1 regulated activity for the intermediary, acts in good faith on behalf of some other person, believing and having reasonable grounds to believe that such other person has a right, title, or interest to or in the securities which he sells within the meaning of subs.(1) on behalf of such other person;

(c) a sale of securities by an exchange participant acting as a principal, when he acts in the course of his business of dealing in odd lots of securities, in accordance with the rules of the recognised exchange company which operates a stock market, being a sale effected solely for the purpose of:

(i) accepting an offer to purchase an odd lot of securities; or

(ii) disposing of an odd lot of securities, by means of the sale of one board lot of those securities;

(d) a sale of securities effected pursuant to a transaction in an options contract traded on a recognised stock market;

(e) a sale of securities falling within a class of transactions prescribed by rules made under s.397 for the purposes of this paragraph.

(4) A person who contravenes subs.(1) commits an offence and is liable on conviction to a fine at level 6 and to imprisonment for 2 years.

COMMENTARY

Predecessor provisions

[170.01] Section 80 of the repealed Securities Ordinance and s.3 of the Securities (Exchange—Traded Stock Options) Rules (Cap.333K).

Overview

[170.02] This section makes it a criminal offence for a person to sell securities at or through a recognised stock market unless at the time of the sale that: he (or his client, if he is an agent) has a presently exercisable and unconditional

right to vest the securities in the purchaser of them or believes *and* has reasonable grounds to believe that he (or his client, as the case may be) has such a right.

Recognised stock market

[170.03] At present, the Stock Exchange of Hong Kong Limited (SEHK) is the only recognised stock exchange and the restriction only applies to short sales conducted at or through SEHK. Therefore, the restriction on short-selling does not apply to off-exchange short sales.

Circumstances which fall outside s.170

[170.04] The Commission accepts there are circumstances that a seller has a "presently exercisable and unconditional right to vest the securities in the purchaser of them" even though the seller does not actually have the securities at the time of placing the sale order. Examples of these circumstances are set out in the Guidance Note on Short Selling Reporting and Stock Lending Record Keeping Requirements.

Technical breach

[170.05] While it is an intermediary's duty to check if his clients have adequate securities available to sell, the Commission has recognised that mistake or errors to occur from time to time. The Commission has stated that it is not its policy to penalise genuine mistakes or errors.

Exemptions from s.170(1)

[170.06] Under s.170(3)(e), the Commission exempts a sale of securities falling within a class of transactions prescribed by rules made under s.397 of this SFO. Section 3 of the Securities and Futures (Short Selling and Securities Borrowing and Lending (Miscellaneous)) Rules (Cap.571R) lists out the classes of transactions exempted.

Generally speaking, those organisations exempted are market makers and liquidity providers of the SEHK and the Hong Kong Future Exchange Limited to make it easier for them to fulfil their market making obligations.

Offence

[170.07] A person who contravenes s.170(1) of this SFO is liable on conviction to a fine at level 6 and to imprisonment for 2 years.

Level 6

[170.08] Under Sch.8 of the Criminal Procedure Ordinance (Cap.221), a level 6 fine is HK$100,000.

Section 203D General provisions relating to exercise of powers under Division 4
Section 203E Recovery and payment of pecuniary penalty
Section 203F Application to Court of First Instance relating to non-compliance with prohibition under section 203A

Background

Part IX of the Securities and Futures Ordinance (Cap.571) (SFO) gives the Securities and Futures Commission (SFC) power to discipline those that it licences or registers.

As the SFC explained in its Regulatory Handbook, 14 December 2004, Volume 1, Chapter 4, one of the important factors behind the success of Hong Kong's securities and futures markets is that the laws and standards governing these markets have been rigorously and credibly enforced. The SFC's key enforcement-related aims are to: (1) protect investors; and (2) maintain market integrity and confidence. These aims are derived from the Objectives and Principles of Securities Regulation of the International Organization of Securities Commissions (IOSCO). The international financial community recognises these Objections and Principles as a benchmark for all markets.

The importance of the abovementioned dual objectives of the SFC have recently been acknowledged by the Court of Appeal in the matter of *Tsien Pak Cheong David v Securities and Futures Commission* [2011] 3 HKLRD 533, para.55.

More specifically, there are various purposes of disciplinary sanctions, including:

1. punishment;
2. deterrence;
3. where suspension, revocation or prohibition is involved, to ensure that the offender does not have the opportunity to repeat the offence, either for a limited period or indefinitely; and
4. to maintain and promote confidence in securities and futures industry.

See *Chu Kwok Shing Godwin v SFC* (SFAT 1/2009, 30 June 2010), para.100; see also *Tsien Pak Cheong David v Securities and Futures Commission*, para.77.

The SFC sets out at p.2 of its publication, *Disciplinary Proceedings at a Glance*, September 2005, various criteria for determining whether to take disciplinary action and the level of sanctions. Such criteria include the nature and seriousness of the conduct, the amount of profits accrued or loss avoided, other circumstances of the firm or individual and other relevant factors.

As disciplinary sanctions are not purely punitive and include a deterrent aspect: "*... in principle mitigating factors have less resonance within domestic disciplinary regimes as compared with the influence of such factors within the criminal system*". See *Wong Wing Fai Eric v Securities and Futures Commission* (SFAT 4/2004, 2 August 2004), para.26. For example, whilst it is not unusual for financial hardship to be sought to be relied upon as a factor to be taken into account, provided the disciplinary sanction in question is otherwise merited, as a matter of general principle resultant financial deprivation cannot in itself justify lack of imposition of the appropriate penalty. See *Hung Hing Chuen v Securities and Futures Commission* (SFAT 10/2006, 31 August 2006), para.44.

The SFC is not fettered by precedent and can respond to prevailing market conditions when deciding upon what disciplinary approach to take. See *Radland International Ltd v Securities and Futures Commission* (SFAT 3/2008, 7 August 2008), paras.63–64.

All the SFC's sanctions, other than a private reprimand, are published by means of a press release, and all press releases are available on the SFC's website. In particular, enforcement-related press releases can be found in the section "Enforcement News".

Parallel proceedings in foreign jurisdictions are covered in s.386 of the SFO.

In the case of *Nomura International (Hong Kong) Ltd v Securities and Futures Commission* (1997–98) 1 HKCFAR 250, involved here was the situation where there were court proceedings commenced by the Australian Securities Commission in Australia as well as disciplinary proceedings commenced by the SFC in Hong Kong.

Nomura sought to stay the Hong Kong disciplinary proceedings until the conclusion of the Australian action. At First Instance, Stone J did not grant the stay but gave Nomura some "breathing space" by prohibiting the SFC from issuing a requiring a response to the "letters of mindedness" until a certain date. The Court of Appeal allowed the appeal and discharged Stone J's order, and Nomura applied for leave to appeal from the Court of Final Appeal.

Importantly, Nomura did not challenge the lawfulness of the SFC having instituted disciplinary proceedings in Hong Kong. The Court of Final Appeal described this as the "inherent weakness" of Nomura's case.

The Court of Final Appeal emphasised that the pace of disciplinary proceedings was uniquely for the body charged with the responsibility of those proceedings to decide, and it was in the public interest that the inquiry be concluded speedily. Where there was no dispute that the Hong Kong disciplinary proceedings needed to be completed, a temporary stay would

(iii) there is now a right of civil action in favour of a person who has suffered financial loss to seek compensation from a person who has committed market misconduct or a Part XIV offence; and

(iv) a duty is imposed on officers of a corporation to take reasonable measures to ensure that the corporation does not contravene the market misconduct provisions.

Division 1 – Interpretation

285. Interpretation of Part XIV

(1) In this Part, unless the context otherwise requires

associate (有聯繫者), in relation to a person, means –

(a) the person's spouse or reputed spouse, any person cohabiting with the person as a spouse, the person's brother, sister, parent, step-parent, child (natural or adopted) or step-child;

(b) any corporation of which the person is a director;

(c) any employee or partner of the person;

(d) where the person is a corporation, each of its directors and its related corporations and each director or employee of any of its related corporations;

(e) without limiting the circumstances in which paragraphs (a) to (d) apply, in circumstances concerning the securities of or other interest in a corporation, or rights arising out of the holding of such securities or such interest, any other person with whom the person has an agreement or arrangement –

(i) with respect to the acquisition, holding or disposal of such securities or such interest; or

(ii) under which they undertake to act together in exercising their voting power at general meetings of the corporation;

controller (控制人), in relation to a corporation, means any person –

(a) in accordance with whose directions or instructions the directors of the corporation or of another corporation of which it is a subsidiary are accustomed or obliged to act; or

(b) who, either alone or with any of his associates, is entitled to exercise or control the exercise of more than 33% of the voting power at general meetings of the corporation or of another corporation of which it is a subsidiary;

relevant overseas market (有關境外市場) –

(a) in relation to securities, means a stock market outside Hong Kong; or

(b) in relation to futures contracts, means a futures market outside Hong Kong;

relevant recognized market (有關認可市場) –

(a) in relation to securities, means a recognized stock market; or

(b) in relation to futures contracts, means a recognized futures market.

(2) In this subsection and sections 286 to 289 and Division 2, unless the context otherwise requires – <* Note - Exp. X-Ref.: Sections 286, 287, 288, 289 *>

derivatives (衍生工具), in relation to listed securities, means –

(a) rights, options or interests (whether described as units or otherwise) in, or in respect of, the listed securities;

(b) contracts, the purpose or pretended purpose of which is to secure or increase a profit or avoid or reduce a loss, wholly or partly by reference to the price or value, or a change in the price or value, of –

(i) the listed securities; or

(ii) any rights, options or interests referred to in paragraph (a);

(c) rights, options or interests (whether described as units or otherwise) in, or in respect of –

(i) any rights, options or interests referred to in paragraph (a); or

(ii) any contracts referred to in paragraph (b);

(d) instruments or other documents creating, acknowledging or evidencing any rights, options or interests or any contracts referred to in paragraph (a), (b) or (c), including certificates of interest or participation in, temporary or interim certificates for, receipts (including depositary receipts) in respect of, or warrants to subscribe for or purchase –

(i) the listed securities; or

(ii) the rights, options or interests or the contracts,

whether or not the derivatives are listed and regardless of who issued or made them;

inside information (內幕消息), in relation to a corporation, means specific information that –

(a) is about –

(i) the corporation;

(ii) a shareholder or officer of the corporation; or

(iii) the listed securities of the corporation or their derivatives; and

> Yet, if "likely" means a "real chance", a trader who neither creates nor intends to create a misleading appearance, commits a criminal offence if his or her conduct merely creates a real chance of a misleading appearance. In my opinion, the language of the sub-section creates an ambiguity which should be resolved in favour of an alleged contravener. The narrower construction of "likely" does no violence to the object of the legislation …"

Lunn J in the Market Misconduct Tribunal[3] considered the word "likely" to mean more probable than not. This would appear to accord with the Australian authorities. More recently, however, the NSW Court of Appeal in *James Hardie Industries NV v ASIC* [2010] NSWCA 332 accepted that for the purposes of section 1041E and section 1041H[4] of the now repealed Australian Corporations Act 2001, the word "likely" means "real and not remote chance".[5] The Court dismissed earlier authorities expounding the "more probably than not" view, including *ASC v Nomura International plc* (1998) 160 ALR 246 and found 'compelling' the notion that:

> "… Parliament can always use the word 'probable' if that is what it means …"[6]

The courts in Hong Kong have consistently followed the approach enunciated in *ASC v Nomura International plc* (1998) 160 ALR 246. The shift by the NSW Court of Appeal in *James Hardie Industries NV v ASIC* [2010] NSWCA 332 may give fresh impetus to the issue here in Hong Kong. Indeed, the question will likely be laid to rest by the Court of Final Appeal with leave being granted in *HKSAR v Fu Kor Kuen, Patrick*[7] to elucidate fully the "elements of false trading". As previously noted, the convictions of the defendants were overturned as they were able to raise the statutory defence laid out in subsection 295(7) of the SFO. See *Fu Kor Kuen Patrick and Lee Shu Yuen Francis v HKSAR*, FACC 4/2011.

[3] The report of the Market Misconduct Tribunal into dealings in the shares of Mobicon Group Limited on and between 1 April 2003 and 25 May 2005 (Dated 23 March 2009).

[4] Section 1041H(1): A person must not, in this jurisdiction, engage in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive.

[5] *James Hardie Industries* at §184.

[6] Baroness Hale of Richmond in *SCA Packaging Ltd v Boyle* [2009] 4 All ER 1181 at §68.

[7] *HKSAR v Fu Kor Kuen, Patrick* [2011] 1 HKLRD 655 (CACC 179 of 2010, 23 December 2010). This case was granted leave to appeal by the CFA - "The circumstances of this case give rise to arguable points of law of great and general importance in regard to the elements of the offence of false trading under s.295 of the Securities and Futures Ordinance Cap.571, and, if it arises, the scope of the statutory defence thereto." FAMC7/2011 7 June 2011. The Court of Final Appeal overturned the convictions based on the statutory defence raised under s.295(7) of the SFO. See *Fu Kor Kuen Patrick and Lee Shu Yuen Francis v HKSAR*, FACC 4/2011.

"Recklessness"

The position in Hong Kong was stated by Mason NPJ in the Court of Final Appeal matter of *HKSAR v Sin Kam Wah* [2005] 8 HKCFAR 192, and in accordance with the judgment in *R v G* [2004] 1 AC 1034 which held that: **[295.07]**

> "… it has to be shown that the defendant's state of mind was culpable in that he acted recklessly in respect of a circumstance *if he was aware of a risk which did or would exist, or in respect of a result if he was aware of a risk that it would occur, and it was, in the circumstances known to him, unreasonable to take the risk.* Conversely, a defendant could not be regarded as culpable so as to be convicted of the offence if, due to his age or personal characteristics, he genuinely did not appreciate or foresee the risks involved in his actions." (emphasis added)

This approach has been applied by the Market Misconduct Tribunal in both the matters of *QPL International Holdings* (25 February 2009) and *Mobicon Group Limited* (23 March 2009).

The Court of Appeal confirmed this approach in the recent matter of *HKSAR v Fu Kor Kuen, Patrick* [2011] 1 HKLRD 655 (CACC 179 of 2010, 23 December 2010).[8] But do note that the convictions of the defendants were overturned as they were able to raise the statutory defence laid out in subsection 295(7) of the SFO. See *Fu Kor Kuen Patrick and Lee Shu Yuen Francis v HKSAR*, FACC 4/2011.

False trading provision prohibits four different types of behaviour

(i) *False trading by creating a false or misleading appearance of active trading* **[295.08]**

Subsection 295(1) of the SFO identifies false trading as having taken place when a person does, causes to be done, anything:

(i) with the intention that, or being reckless as to whether it has or is likely to have the effect of;
(ii) creating a false or misleading appearance;
(iii) of active trading with respect to securities or futures traded on a recognised market or through an authorised automated trading system (ATS).

[8] This case was granted leave to appeal by the CFA - "The circumstances of this case give rise to arguable points of law of great and general importance in regard to the elements of the offence of false trading under s.295 of the Securities and Futures Ordinance Cap.571, and, if it arises, the scope of the statutory defence thereto." FAMC7/2011 7 June 2011. The Court of Final Appeal overturned the convictions based on the statutory defence raised under s.295(7) of the SFO. See *Fu Kor Kuen Patrick and Lee Shu Yuen Francis v HKSAR*, FACC 4/2011.

(2) No person shall be liable to pay compensation under subsection (1) unless it is fair, just and reasonable in the circumstances of the case that he should be so liable.

(3) A defence under this Part to a charge for an offence in respect of a contravention of any of the provisions of Divisions 2 to 4 shall also be a defence in an action brought under subsection (1) in respect of the same contravention.

(4) A person may bring an action under subsection (1) in respect of a contravention of any of the provisions of Divisions 2 to 4 even though the person against whom the action is brought has not been charged with or convicted of an offence by reason of the contravention.

(5) For the avoidance of doubt, where a court has jurisdiction to determine an action brought under subsection (1), it may, where it is, apart from this section, within its jurisdiction to entertain an application for an injunction, grant an injunction in addition to, or in substitution for, damages, on such terms and conditions as it considers appropriate.

(6) Without prejudice to section 62 of the Evidence Ordinance (Cap.8), in an action brought under subsection (1) –

(a) the fact that there is a determination by the Market Misconduct Tribunal pursuant to section 252(3)(a) that market misconduct has taken place;

(b) the fact that there is a determination by the Market Misconduct Tribunal pursuant to section 252(3)(b) identifying a person (whether or not a party to the action) as having engaged in market misconduct, shall, in so far the determination is still subsisting, be admissible in evidence for the purpose of proving, where to do so is relevant to any issue in the action –

(i) in the case of a determination referred to in paragraph (a), that the market misconduct has taken place; or

(ii) in the case of a determination referred to in paragraph (b), that the person has engaged in market misconduct.

(7) In an action brought under subsection (1), where the fact that there is a determination referred to in subsection (6)(a) or (b) is admissible in evidence under subsection (6) –

(a) then –

(i) in the case of a determination referred to in subsection (6)(a), the market misconduct that is the subject of the determination shall, unless the contrary is proved, be taken to have taken place; or

(ii) in the case of a determination referred to in subsection (6)(b), the person that is the subject of the determination shall, unless the contrary is proved, be taken to have engaged in market misconduct; and

(b) without prejudice to the reception of any other admissible evidence as evidence of the determination or for the purpose of identifying the facts on which the determination was based, the contents of a report of the Market Misconduct Tribunal containing the determination and published under section 262(2)(b)(i), or the contents of a copy of a report of the Market Misconduct Tribunal containing the determination and made available under subsection (8), shall also be admissible in evidence for such purpose.

(8) Where in an action brought under subsection (1) –

(a) the fact that there is a determination referred to in subsection (6)(a) or (b) is admissible in evidence under subsection (6); and

(b) a report of the Market Misconduct Tribunal containing the determination has not been published under section 262(2)(b)(i), the court having jurisdiction to determine the action may, where it considers appropriate, require that a copy of the report be made available to the court to enable it to be used for the purposes of subsection (7)(b), whereupon –

(i) the Market Misconduct Tribunal shall cause a copy of the report to be made available to the court to enable it to be used for the purposes of subsection (7)(b); and

(ii) the contents of the report shall be admissible for the purpose specified in subsection (7)(b).

(9) In this section, a reference to a transaction includes an offer and an invitation (however expressed).

(10) Nothing in this section affects, limits or diminishes any rights conferred on a person, or any liabilities a person may incur, under the common law or any other enactment.

COMMENTARY

Predecessor provisions [305.01]

This section came into effect on 1 April 2003. It is a new section which was influenced by section 141 of the Securities Ordinance (Cap.333), section 40 of the predecessor Companies Ordinance, and section 150 of the UK Financial Services and Markets Act 2000.

Overview

[307N.02] As in corollary section 257 of the SFO, this section 307N of the SFO gives the MMT its power to impose sanctions upon those identified in breach of the disclosure provisions as so required under this Part XIVA of the SFO. See also s.257 of the SFO.

In summary, MMT is able to impose one or more of the following penalties for those corporations found in breach of the disclosure provisions as so required under this Part XIVA of the SFO:

i. a fine of up to HK$8 million on the corporation, a director or chief executive (but not officers) of the corporation;
ii. disqualification of the director or officer from being a director or otherwise involved in the management of a corporation for up to five years;
iii. a "cold shoulder" order on the director or an officer (i.e. the person is deprived of access to market facilities for dealing in securities, futures contracts and other investments) for up to five years;
iv. a "cease and desist" order on the corporation, director or officer (i.e. an order not to breach the statutory disclosure requirement again);
v. an order that anybody of which the director or officer is a member be recommended to take disciplinary action against him; or
vi. payment of costs of the civil inquiry and/or the SFC investigation by the corporation, director or officer.

In an effort to try and prevent the occurrence of further breaches of the disclosure requirement, the MMT may additionally *require:*

i. the appointment of an independent professional adviser to review the corporation's procedures for disclosure of PSI and advise it on matters relating to compliance; and
ii. the officer to undertake a training programme approved by the SFC on compliance with Part XIVA of the SFO, directors' duties and corporate governance.

307O. Notice and effect of orders of Tribunal

(1) The Tribunal must by notice in writing notify a person of an order made in respect of the person under section 307N(1).

(2) The order takes effect at the time when it is notified to the person or at the time specified in the notice, whichever is the later.

(3) If the Tribunal makes an order under section 307N(1)(b), the Commission may notify any licensed person or registered institution of the order in any manner the Commission considers appropriate.

(4) A person who fails to comply with an order made under section 307N(1)(a), (b) or (c) commits an offence and is liable –

(a) on conviction on indictment to a fine of $1000000 and to imprisonment for 2 years; or
(b) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

COMMENTARY

Predecessor provisions

[307O.01] This section came into effect on 1 January 2013 which was implemented under Part 2 of the Securities and Futures (Amendment) Ordinance 2012 which was gazetted on 4 May 2012.

Overview

[307O.02] Section 307O is self explanatory as once an Order is produced under previous s.307N of the SFO, written notice that an Order has since been handed down by the MMT as well as a copy of the Order itself must be sent to the offending party in a manner the SFC deems appropriate.

The Order will effect at the time when the offending party is notified or at the time as specified in the notice, whichever is the later time period.

307P. Costs

(1) Subject to subsection (4), at the conclusion of any disclosure proceedings, or as soon as reasonably practicable after the conclusion of the proceedings, the Tribunal may by order award to any of the following persons a sum it considers appropriate in respect of the costs reasonably incurred by the person in relation to the proceedings –

(a) a person whose attendance, whether as a witness or otherwise, has been necessary or required for the purposes of the proceedings;
(b) a person whose conduct is the subject, whether wholly or in part, of the proceedings.

(2) Any costs awarded under this section are a charge on the general revenue.

(3) Subject to any rules made by the Chief Justice under section 307X, Order 62 of the Rules of the High Court (Cap.4 sub. leg. A) applies to the award of costs, and to the taxation of any costs awarded, by the Tribunal under this section.

(7) The existence of the duty of disclosure in a particular case depends (in part) on the circumstances obtaining before and after whatever is in that case the relevant time.

COMMENTARY

Predecessor provisions

[310.01] Historically, this section replaced section 3 of the repealed Securities (Disclosure of Interests) Ordinance (Cap.396).

Duty of disclosure for substantial shareholders

[310.02] This section sets out the various scenarios in which substantial shareholders of listed corporations (meaning, in the context of Part XV, a person interested in 5% or more of the company's voting shares) will have a duty to disclose their interests in shares or debentures of the listed corporation or an associated corporation. The circumstances set out in this section must be read together with the provisions of s.313, as referred to in each of the scenarios.

The method of drafting makes it somewhat cumbersome for substantial shareholders to determine if a particular event gives rise to a duty of disclosure. It is necessary to first check if the event falls within one of the situations set out in s.310, and if so, to proceed to check whether the event also falls within the corresponding part of s.313. Only if the particular event falls within *both* ss.310 and 313 must the shareholder file a disclosure notice. To illustrate, section 310(1)(a) provides that where a person acquires an interest in shares, then in the circumstances specified in s.313(1) he comes under the duty of disclosure. Turning then to s. 313(1)(a), the circumstance described there is where the person had a "notifiable interest" (i.e. interest in 5% or more of the company's shares: s.311(3)) immediately *after* the occurrence of the event but not immediately *before*. Putting this all together: a person must make disclosure when he first acquires an interest in 5% or more of the company's shares.

In summary, a substantial shareholder has a duty of disclosure on the occurrence of the following events:

(1) When he first becomes interested in 5% or more of the company's shares (i.e. he becomes a substantial shareholder) (ss.310(1) and 313(1)(a)).
(2) When his interest in shares drops below 5% (i.e. he ceases to be a substantial shareholder) (ss.310(1) and 313(1)(b)).

(3) When his interest in shares crosses a whole percentage level (ss.310(1), 313(1)(c), and s.314(1)). For example: if the shareholder's interest rises from 5.8% to 6.2%, that event is disclosable (because this crosses the 6% level). However, if the shareholder's interest rises from 4.2% to 4.8%, that does not trigger the disclosure obligations.
(4) When the nature of his interest changes (ss.310(1) and 313(1)(d)).
(5) When he comes or ceases to have a short position of 1% or more (ss.310(4), 313(4)(a) and 313(4)(b)). Note that this only applies if the person also holds a interest in shares (a 'long' position) of 5% or more (i.e. he is a substantial shareholder).
(6) When he already holds a short position of 1% or more, and his short position crosses a whole percentage level (ss.313(4), 313(4)(c), and 314(4)). For example: if the shareholder's short position falls from 3.4% to 2.8%, that event is disclosable (because this crosses the 3% level). Again, this only applies if the person also holds a long position of 5% or more.
(7) When the company first becomes listed (ss.310(2)(a) and 313(2)).
(8) When the particular class of shares in which he is interested first becomes voting shares (ss.310(2)(b) and 313(2)).
(9) On commencement of the SFO (ss.310(2)(c), 310(5), 310(2), and 313(5)).
(10) If there is a reduction in the notification thresholds (currently 5% for long positions and 1% for short positions) (ss.310(3), 310(6), 313(3), and 313(6)).

Interest in 'voting shares'

[310.03] Substantial shareholders *only* have to disclose their interests in "voting shares" of a listed corporation, *not all* types of shares. Those shares that are considered "voting shares" and are as such applicable under this provision are those shares of a class that carry a right to vote in all circumstances at general meetings of a listed corporation. They also include unissued shares which, if issued, would have such rights. Voting shares of a corporation listed in Hong Kong refers to all classes of shares and would normally include "A shares", "B shares" and "H shares" as well as "Ordinary shares" as these all normally carry a right to vote in all circumstances at general meetings of a listed corporation.

'Interest' in shares

[310.04] A shareholder will be considered to have an "interest" in shares for the purposes of Part XV if he has an interest of any kind whatsoever in the shares (Section 322(2) of the SFO). For example:

(4) Unless a corporation is –

(a) a listed corporation;

(b) a wholly owned subsidiary of a listed corporation;

(c) a corporation listed on a specified stock exchange; or

(d) a wholly owned subsidiary of a corporation listed on a specified stock exchange,

it shall, in performing a duty of disclosure arising under section 310, also specify in the notification the name and address of any person in accordance with whose directions or instructions it, or its directors, are accustomed or obliged to act.

(5) For the purposes of subsection (4), a person shall not be regarded as a person in accordance with whose directions or instructions a corporation or its directors are accustomed or obliged to act by reason only that the corporation or its directors act on advice given by him in a professional capacity.

(6) A notification given by a person who is for the time being a party to an agreement to which section 317 applies shall also –

(a) state that the person giving the notification is a party to such an agreement;

(b) include –

(i) the names and (so far as he is aware) the addresses of the other parties to the agreement, identifying them as such; and

(ii) the number and class of shares in which each of those other parties is interested (apart from the agreement);

(c) state whether or not any of the shares to which the notification relates are shares in which he is interested by the application of sections 317 and 318 and, if so, the total number and class of those shares;

(d) include a copy of any written agreement, contract, document or other instrument which records any terms or details of the agreement to which section 317 applies; and

(e) (where there is no written agreement, contract, document or other instrument of the type referred to in paragraph (d) or where the agreement is only partly recorded in writing) include a written memorandum recording the material terms of the agreement to which section 317 applies, which are not otherwise recorded in writing, including, but not limited to –

(i) any cash or other consideration involved; and

(ii) the identity of all persons between whom such cash or other consideration is passed or is intended to pass.

(7) A notification given by a person in consequence of his ceasing to be interested in any shares by virtue of the fact that he or any other person has ceased to be a party to an agreement to which section 317 applies shall also –

(a) state that he or that other person (as the case may be) has ceased to be a party to the agreement; and

(b) (in the latter case) include the name and (so far as he is aware) the address of that other person.

(8) Nothing in subsection (1) or (2) shall require details of the price that has been paid or may be payable, or the consideration that has been given or may be given, for or under equity derivatives (where the underlying shares of the equity derivatives are shares which are the subject of the disclosure) to be specified in the notification.

COMMENTARY

Predecessor provisions **[326.01]**

Historically, this section replaced subsections 7(5) to 7(7) and 15(2) of the repealed Securities (Disclosure of Interests) Ordinance (Cap.396). See also section 10(4) of this repealed Ordinance. A comparison may be made to an equivalent provision found in section 202 of the UK Companies Act 1985. A parallel requirement can be found in this SFO in respect of substantial shareholders. This section was amended by the (new) Companies Ordinance (Cap.622) to bring references to sections in the (new) Companies Ordinance up to date.

Particulars **[326.02]**

This section sets out in detail the particulars required to be provided by directors and chief executives under the duty of disclosure in previous s.310 of the SFO above. Pursuant to the forms under s.324 of the SFO, reference should be made to the Notes to those forms published by the SFC. See para. 4.2 of the Outline of Part XV at: http://enrules.sfc.hk/en/display/display.html?rbid=3527&element_id=4511.

See also all the forms listed at the SFC website at: http://www.sfc.hk/web/EN/rule-book/sfo-part-xv-disclosure-of-interests/di-notices.html.

Financial information or consideration that need not be disclosed **[326.03]**

Subsection 326(8) prescribes that if the transaction that prompts disclosure is either:

(i) a change in the nature of your interest in shares (e.g. a securities (i) a change in the nature of your interest in shares (e.g. a securities borrowing and lending transaction);

the obligation to deliver shares may be settled by payment of cash or by delivery of shares or otherwise.

(14) Persons having a joint interest or short position are taken each of them to have that interest or short position (as the case may be).

(15) It is immaterial that shares in which a person has an interest or short position are unidentifiable.

COMMENTARY

Predecessor provisions

[345.01] This section parallels s.322 above in respect of substantial shareholders.

Determination of duty to disclose

[345.02] Section 345 sets out various scenarios in which a director or chief executive would have a duty to disclose their interests in shares, debentures or a short position.

This provision applies to all interests(and short positions) in shares be they direct interests (and short positions) in shares and indirect interests (and short positions) e.g., interests in shares which are the underlying shares of equity derivatives. This is clear from the reference in subsection 345(1) to "short positions" (which are principally positions arising under derivatives) and the many references to "equity derivatives" and "underlying shares" in this provision.

346. Interests and short positions to be disregarded for the purpose of notification by director and chief executive

(1) The following interests, and short positions, in shares in or debentures of a listed corporation or any associated corporation of the listed corporation shall be disregarded for the purposes of Divisions 7 to 9 –

(a) so long as a person is entitled to receive income from trust property comprising shares or debentures during the life-time of himself or another person, an interest in the shares or debentures in reversion or remainder;

(b) an interest of a person in shares or debentures if, and so long as, he holds the shares or debentures as a bare trustee;

(c) subject to subsection (3), an interest in shares or debentures comprised in the property under –

(i) a collective investment scheme authorized under section 104;

(ii) a pension scheme or a provident fund scheme registered under section 21 or 21A of the Mandatory Provident Fund Schemes Ordinance (Cap.485); or

(iii) a qualified overseas scheme,

of a holder, trustee or custodian of the scheme;

(d) an interest of a person subsisting by virtue of –

(i) a charitable scheme made by order of any court of competent jurisdiction; or

(ii) the vesting of a deceased's estate in any judicial officer between the time of death of the deceased and the grant of letters of administration; and

(e) such interests or interests of such a class, or such short positions or short positions of such a class, as are prescribed by regulations for the purposes of this section.

(2) A person is not taken to be interested in shares or debentures under section 345(5)(b) by reason only that he –

(a) has been appointed as a proxy to vote at a specified meeting of the listed corporation or associated corporation or of any class of its members and at any adjournment of that meeting; or

(b) has been appointed by a corporation to act as its representative at a meeting of the listed corporation or associated corporation or of any class of its members.

(3) An interest in shares or debentures of a holder, trustee or custodian of a scheme referred to in subsection (1)(c)(i), (ii) or (iii), comprised in the property under the scheme, shall not be disregarded under subsection (1)(c) if the holder, trustee or custodian (as the case may be) is also a manager of the scheme.

(4) For the purposes of subsection (1)(c), ***qualified overseas scheme*** (合資格海外計劃) means a collective investment scheme, pension scheme or provident fund scheme which –

(a) is established in a place outside Hong Kong recognized for the purposes of this section by the Commission by notice published in the Gazette; and

(b) is authorized by or registered with the authority (if any) responsible for the authorization or registration of such scheme in the place where it is established, and complies with the requirements of such authority,

but does not include –

(i) an arrangement operated by a person otherwise than by way of business;

another person to take delivery of shares, that the shares due to be delivered on the exercise of the right shall, upon delivery, be –

(a) subject to the restrictions under this Division; or

(b) sold.

(15) In this section, ***the corporation concerned*** (有關法團) –

(a) in relation to shares in a corporation that are subject to the restrictions under this Division, means that corporation; or

(b) in relation to equity derivatives that are subject to the restrictions under this Division, where the underlying shares of those equity derivatives are shares in a corporation, means that corporation.

COMMENTARY

Predecessor provisions

[371.01] Historically, this section replaced section 46 of the repealed Securities (Disclosure of Interests) Ordinance (Cap.396). A comparison may be made to an equivalent provision found in section 456 of the UK Companies Act 1985.

Application against restriction

[371.02] Where a restriction has been imposed under the foregoing sections, an application may be made under this section for the relaxation or removal of those restrictions by the Court of First Instance or the Financial Secretary, as the case may be.

The general rule, contained in s.371(4)(a), is that the Court or Financial Secretary (as the case may be) may only order a removal of restrictions where they are satisfied that: (1) the relevant facts about the shares have been disclosed to the company; and (2) the failure to disclose has not caused unfair advantage to any person. On the other hand, s.371(4)(b) provides what has been described as a "dispensation" to the general rule (*Re Westminster Property Group* [1985] 1 WLR 676, per Slade LJ at 685B), i.e. that an order can also be made if the shares are to be sold and that sale is approved by the court. Section 371(4)(b) is an independent ground of relief from s.371(4)(a) and can be invoked even where the court is *not* satisfied that the relevant facts about the shares have been disclosed etc. See *Re Geers Gross* [1987] 1 WLR 1649, per Nourse LJ at 1651H-1652A. However, where the Court is asked under s.371(4)(b) to remove restrictions on the ground that the shares are to be sold, the court retains a discretion whether or not to approve the sale. In exercising that discretion, it is legitimate for the Court to take into account,

among other factors, a failure to disclose relevant information about the shares. The Court may, for instance, consider whether the removal of restrictions would leave the company with "no real lever with which to prise open the casket in which the relevant facts about the shares are hidden." See *Re Geers Gross* [1987] 1 WLR 1649, per Nourse LJ at 1652A-H. On the other hand, the Court will also weigh in the balance any prejudice that would be caused to innocent third parties if the restrictions were to be continued. See *Re Geers Gross* [1987] 1 WLR 1649, per Nourse LJ at 1653H.

In deciding whether to order a sale under s.371(5), the court will act on the following principles: (1) the Court must be satisfied that it is in the public interest that the shares be sold; (2) the Court must be satisfied that adequate steps have been taken to ascertain the identity of the shareholders; and (3) the Court must have some regard to the protection of the shareholders whose interests have been blocked and are being overridden by the sale. See *Re World Trade Centre Group Ltd* [1994] 1 HKLR 243 per Rogers J at 246. The Court is unlikely to order a sale under subsection 371(5) where, before the imposition of restrictions, there was already in existence a contract for sale of the shares. In that situation, it is more appropriate to apply under subsections 371(1) and 371(4)(b) for a removal of the restrictions on the ground that a sale of the shares is intended. See *Re Westminster Property Group* [1985] 1 WLR 676, per Slade LJ at 687B-E.

Note that "sold" here refers only to a transfer of shares for cash. Thus, the court has no jurisdiction under s.371(4)(b) to order the removal of restrictions where the intended sale is for non-monetary consideration, such as shares in another company. See *Re Westminster Property Group* [1985] 1 WLR 676, per Slade LJ at 684C-685D.

Where a court-ordered sale takes place, the buyer of the shares or equity derivatives will receive good title. See *Re World Trade Centre Group Ltd* [1994] 1 HKLR 243 per Rogers J at 247 line 30.

Further powers

[371.03] This section 371 also allows for orders of sale of shares and exercise of rights under equity derivatives, as well as for the Financial Secretary to be heard and call evidence for the purposes of hearing an application under this section before the Courts.

372. Further provisions on sale by court order of restricted shares, etc.

(1) Subject to subsection (2), where shares or equity derivatives are sold in pursuance of an order of the Court of First Instance, or with the

issues is called for in order to resolve the conflicts, inconsistencies, gaps and duplications in regulatory requirements applying in cross-border contexts. See *OTC Derivatives Market Reforms: Eighth Progress Report on Implementation*, 7 November 2014, p.2.

Publication in Gazette

[381C.04] According to subsection 381C(6), if the conditions as set forth in those previous subsections 381C(4) or 381C(5) are satisfied, the HKMA must publish the name of the authority, regulatory organization or companies inspector in the Gazette.

Conditions imposed by the HKMA

[381C.05] Subsection 381C(7) empowers the HKMA to impose any condition when disclosing information. See [378.10].

381D. Restrictions on disclosure by persons to whom information is disclosed

(1) If information is disclosed pursuant to section 381A(2) or in any of the circumstances described in section 381A(4), 381B(1) or (2) or 381C(1), unless subsection (2) applies –

(a) the person to whom the information is disclosed; and

(b) any other person obtaining or receiving the information from the person to whom the information is disclosed, either directly or indirectly,

must not disclose the information or any part of it to any other person.

(2) Information disclosed as described in subsection (1) may be disclosed to any other person if –

(a) the Monetary Authority consents to the disclosure; (b) the information has already been made available to the public;

(c) the disclosure is of a part that has already been made available to the public;

(d) the disclosure is for the purpose of seeking advice from, or giving advice by, counsel or a solicitor or other professional adviser acting or proposing to act in a professional capacity in connection with a matter arising under a specified provision;

(e) the disclosure is in connection with any judicial or other proceedings to which the person or other person referred to in subsection (1)(a) or (b) is a party; or

(f) the disclosure is in accordance with an order of a court, or in accordance with a law or a requirement made under a law.

(3) The Monetary Authority may, in giving any consent under subsection (2)(a), impose any condition that the Monetary Authority considers appropriate.

(4) A person referred to in subsection (1)(a) to whom information is disclosed commits an offence if the person –

(a) discloses information in contravention of that subsection; and

(b) at the time of the disclosure knew or ought reasonably to have known that the information was previously disclosed to the person pursuant to section 381A(2) or in any of the circumstances described in section 381A(4), 381B(1) or (2) or 381C(1),

unless the person proves that the person had reasonable grounds to believe that subsection (2) applied to the disclosure by the person.

(5) A person referred to in subsection (1)(b) who obtains or receives information commits an offence if the person –

(a) discloses information in contravention of that subsection; and

(b) at the time of the disclosure knew or ought reasonably to have known that the information was previously disclosed to the person referred to in subsection (1)(a) under section 381A(2) or in any of the circumstances described in section 381A(4), 381B(1) or (2) or 381C(1),

unless the person proves that the person had reasonable grounds to believe that subsection (2) applied to the disclosure by the person.

(6) A person who commits an offence under subsection (4) or (5) is liable –

(a) on conviction on indictment to a fine of $1,000,000 and to imprisonment for 2 years; or

(b) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

(7) To avoid doubt –

(a) this section does not apply to information disclosed to the Commission under this Division; and

(b) section 378 applies to information disclosed to the Commission under this Division.

(8) In this section –

information (資料) has the meaning given by section 381B(7).

** *Added 6 of 2014 as these terms just came into effect this past 10 July 2015.*

COMMENTARY

Predecessor provisions

[399.01] Section 399 came into effect on 1 April 2003. Its predecessor provision was section 4(2) of the repealed Securities and Futures Commission Ordinance (Cap.24). See also the SFO Derivation Table, p.24.

Power to publish codes and guidelines

[399.02] Section 399 empowers the SFC to publish codes and guidelines to provide guidance for the furtherance of its regulatory objectives, in relation to its functions under the relevant provisions or in relation to the operation of provisions of the SFO (Section 399(1)). In particular, the SFC may publish codes on takeovers and mergers and share buy-backs (Section 399(2)). The codes or guidelines published by the SFC pursuant to section 399 are not considered subsidiary legislations under subsection 399(8) of this SFO.

The SFC's power to publish codes or guidelines *is in addition to* and not in derogation of any other statutory power of the SFC to publish codes or guidelines as prescribed under subsection 399(4).

The SFC also has the power to amend any published codes or guidelines. Such power to amend should be exercised in a consistent manner with its power to publish as prescribed under subsection 399(5).

The SFC is required to consult the HKMA regarding the proposed publications or amendments of codes or guidelines where the codes or guidelines or amendments (as the case may be) are applicable to authorized financial institutions as prescribed under subsection 399(9).

Non-compliance with any SFC code or guideline published pursuant to section 399 does not render the person liable to any judicial proceedings *per se*. However, the code or guideline shall be admissible in evidence in the proceedings where it is relevant a so allowed under subsection 399(6).

Securities and Futures (Amendment) Ordinance 2014

[399.03] The Securities and Futures (Amendment) Ordinance 2014, which amended the SFO to provide for the regulation of activities and other matters connected with over-the-counter derivative products, was gazetted on 4 April 2014.

Section 399 of the SFO was amended by the Securities and Futures (Amendment) Ordinance 2014 to extend its application to all the guidelines made by the SFC, including those made in relation to disciplinary actions against the registered systemically important participants under the new over-the-counter derivative product regulatory regime. See *Explanatory Memorandum of the Securities and Futures (Amendment) Bill 2013*, para.28.

This amendment came into operation on 10 July 2015. See Securities and Futures (Amendment) Ordinance 2014 (Commencement) Notice 2015 (L.N. 95 of 2015).

Codes and guidelines published by the SFC

The codes and guidelines published by the SFC can be found on the SFC's website at http://en-rules.sfc.hk/. [399.04]

Division 4 – Miscellaneous

400. Service of notices, etc.

(1) Subject to sections 111, 141 and 374 and any rules made under section 233 or 269, any written notice or direction or other document (however described) to be, or required to be, issued or served (however described) to or on any person, other than the Commission, for the purposes of this Ordinance shall for all purposes be regarded as duly issued or served if- (Amended 28 of 2012 ss.912 & 920)

(a) in the case of an individual, it is –
  (i) delivered to him by hand;
  (ii) left at, or sent by post to, his last known business or residential address; (Amended 28 of 2012 ss.912 & 920)
  (iii) sent by facsimile transmission to his last known facsimile number; or
  (iv) sent by electronic mail transmission to his last known electronic mail address;

(b) in the case of a company, it is –
  (i) delivered to any officer of the company by hand;
  (ii) left at, or sent by post to, the company's registered office in Hong Kong; (Amended 28 of 2012 ss.912 & 920)
  (iii) sent by facsimile transmission to its last known facsimile number; or
  (iv) sent by electronic mail transmission to its last known electronic mail address;

Defining 'client securities'

Sch.1.09] For treatment of client securities, refer to the Securities and Futures (Client Securities) Rules (Cap.571I).

Defining 'collective investment scheme'

Sch.1.10] Please refer to the SFC's outline of 27 August 2013 of what constitutes a collective investment scheme. As mentioned in the outline, a collective investment scheme has four elements:

- it must involve an arrangement in respect of property;
- participants do not have day-to-day control over the management of the property even if they have the right to be consulted or to give directions about the management of the property;
- the property is managed as a whole by or on behalf of the person operating the arrangements, and/or the contributions of the participants and the profits or income from which payments are made to them are pooled; and
- the purpose of the arrangement is for the participants to participate in or receive profits, income or other returns from the acquisition or management of the property.

Also note that in accordance with the Securities and Futures (Collective Investment Schemes) Notice (Cap.571M) any arrangement for the purchase of gold coins or gold bullion that allow participants to acquire ownership, defer possession or transfer ownership to another person who is party to or part of the arrangement will be regarded as a "collective investment scheme".

Please refer to the SFC press release 13 May 2013 relating to the sale of hotel room units at The Apex Horizon. The SFC was investigating whether the offer to purchase such units constituted an offer to acquire an interest in or participate in a collective investment scheme.

Please refer to the SFC circular dated 13 August 2009 relating to Investment-Linked Assurance Schemes (ILAS), where the SFC stated that ILAS falls within the definition of collective investment scheme.

Defining 'currency and interest rate-linked instrument'

[Sch.1.11] This term was introduced by the Securities and Futures and Companies Legislation (Structured Products Amendment) Ordinance. Such instruments are generally viewed as treasury products issued by authorized financial institutions which are not regulated by the SFO and therefore they have been excluded from the definition of "structured product".

Defining 'currency-linked instrument'

This term was introduced by the Securities and Futures and Companies Legislation (Structured Products Amendment) Ordinance. Such instruments are generally viewed as treasury products issued by authorized financial institutions which are not regulated by the SFO and therefore they have been excluded from the definition of "structured product". [Sch.1.12]

Defining 'dealing'

"Making or offering to make an agreement" means any act of acquisition, disposal, subscription or underwriting, such as an offer or formation of a contract. "Inducing or attempting to induce" includes marketing or promotion activities. [Sch.1.13]

Defining 'debenture'

This term generally means debt securities. The definition of "debenture" in the (new) Companies Ordinance (Cap.622) was amended to refer to "debt securities" (previously it was "securities") in 2011 pursuant to the Securities and Futures (Structured Products Amendment) Ordinance. [Sch.1.14]

Defining 'executive officer'

Please refer to sections 71C, 71D, and 71E of the Banking Ordinance (Cap.155) for the approval and appointment process of executive officers of registered institutions. Each registered institution needs at least 2 executive officers to supervise any regulated activity undertaken. This is generally the equivalent of "responsible officer" of licensed corporations. [Sch.1.15]

Defining 'financial accommodation'

This is part of the definition of Type 8 regulated activities "securities margin financing". Where financial accommodation is provided there are rules regarding how it is treated and reported, please refer to the: (i) Securities and Futures (Financial Resources) Rules (Cap.571N); (ii) the Securities and Futures (Contract Notes, Statements of Account and Receipt) Rules (Cap.571Q); (iii) the Securities and Futures (Client Securities) Rules (Cap.571H); (iv) the Securities and Futures (Client Money) Rules (Cap.571I); and (v) the Securities and Futures (Accounts and Audit) Rules (Cap.571P). [Sch.1.16]

Defining 'financial product'

The Securities and Futures and Companies Legislation (Structured Products Amendment) Ordinance added "structured" product" to the list of financial products. The SFC may make business conduct rules in relation to financial products under section 168 of the SFO. [Sch.1.17]

Schedule	6	**Specified Titles**	E.R. 1 of 2013	25/04/2013

[sections 113, 139 & 143]

Item	Provision	Specified titles
1.	Section 139(1) of this Ordinance	"bond broker", "bond dealer", "securities dealer", "stock dealer", "stockbroker", "股票經紀", "債券交易商", "債券經紀", "證券交易 商" and "證券經紀"
2.	Section 139(2) of this Ordinance	"futures broker", "futures dealer", "期貨交易商" and "期貨經紀"
3.	Section 139(3) of this Ordinance	"leveraged foreign exchange trader" and "槓桿式外匯交易商"
4.	Section 139(4) of this Ordinance	"securities adviser", "securities consultant", "stock adviser", "股票顧問" and "證券顧問"
5.	Section 139(5) of this Ordinance	"futures adviser", "futures consultant" and "期貨顧問"
6.	Section 139(6) of this Ordinance	"corporate finance adviser", "corporate finance consultant" and "機構融 資顧問"
7.	Section 139(7) of this Ordinance	"automated trading service provider" and "自動化交易服務提供者"
8.	Section 139(8) of this Ordinance	"margin lender", "securities margin financier" and "證券保證金融資人"

(Format changes – E.R. 1 of 2013)

COMMENTARY

Overview

:h.6.01] Schedule 6 is self-explanatory as it simply lists those specific titles which are permitted to be given to those persons who deal with the (now) twelve (12) types regulated activities listed in previous Schedule 5 of the SFO. See section 139 of the SFO.

Schedule	7	**Offers by Intermediaries or Representatives for Type 1, Type 4 or Type 6 Regulated Activity under Section 175 of this Ordinance**	L.N. 163 of 2013	03/03/2014

[sections 175 & 177]

PART 1

Requirements to be Satisfied in Relation to Offers to Acquire Securities

1. If the securities proposed to be acquired are currently listed or quoted on any stock market, whether a recognized stock market or any other stock market outside Hong Kong, the offer shall –

(a) state that fact and specify the stock markets on which the securities are currently listed or quoted;

(b) specify the closing price in respect of the securities on each stock market on the latest practicable date immediately preceding the date of the offer;

(c) specify the closing price in respect of the securities on the last trading day of each of the 6 months immediately preceding the date of the offer;

(d) specify the highest and the lowest closing prices in respect of the securities during the period of 6 months immediately preceding the date of the offer; and

(e) where the offer has been the subject of a public announcement, whether in a newspaper or any other form of information medium or otherwise, specify the closing price in respect of the securities on the last trading day immediately preceding the public announcement.

2. If the securities proposed to be acquired are not listed or quoted on any stock market, whether a recognized stock market or any other stock market outside Hong Kong, the offer shall contain –

(a) all information that the offeror may have as to the number and nominal value (if any) of those securities that have been sold in Hong Kong during the period of 6 months immediately preceding the date of the offer and the prices yielded by those sales; and (Amended 28 of 2012 ss.912 & 920)

(b) particulars of any restriction in the constitution, by whatever name called, of the body in question on the right to transfer the securities, that has the effect of requiring the offerees,

section 119(1) of this Ordinance for registration for Type 4, Type 6 and Type 9 regulated activities; or

(ii) where the applicant is not an authorized financial institution, be treated as an application under section 116(1) of this Ordinance for Type 4, Type 6 and Type 9 regulated activities.

Part VI of this Ordinance (Capital requirements, client assets, records and audit relating to intermediaries)

61. Where –

(a) before the commencement of Part VI of this Ordinance, any power could have been, but was not, exercised under –

(i) section 52 or 53 of the repealed Commodities Trading Ordinance;

(ii) section 90, 91, 121AW or 121AX of the repealed Securities Ordinance; or

(iii) section 33 or 34 of the repealed Leveraged Foreign Exchange Trading Ordinance; or

(b) before such commencement any power has been exercised under any of the provisions referred to in paragraph (a)(i), (ii) and (iii), and the exercise of the power would, but for the enactment of this Ordinance, continue to have force and effect on or after such commencement,

then –

(i) (A) where paragraph (a) applies, the power may be exercised; or

(B) where paragraph (b) applies, the exercise of the power shall continue to have force and effect as if this Ordinance had not been enacted; and

(ii) the provisions of the repealed Commodities Trading Ordinance, the repealed Securities Ordinance or the repealed Leveraged Foreign Exchange Trading Ordinance (as the case may be) shall continue to apply to the exercise of the power and to any matters relating thereto (including any further exercise of power) as if this Ordinance had not been enacted.

Part VIII of this Ordinance (Supervision and investigations)

62. Where –

(a) before the commencement of Part VIII of this Ordinance, any power could have been, but was not, exercised under –

(i) section 29A, 30, 31, 33 or 36 of the repealed Securities and Futures Commission Ordinance; or

(ii) section 12, 41, 42, 44 or 47 of the repealed Leveraged Foreign Exchange Trading Ordinance; or

(b) before such commencement any power has been exercised under any of the provisions referred to in paragraph (a)(i) and (ii), and the exercise of the power would, but for the enactment of this Ordinance, continue to have force and effect on or after such commencement,

then –

(i) (A) where paragraph (a) applies, the power may be exercised; or

(B) where paragraph (b) applies, the exercise of the power shall continue to have force and effect, as if this Ordinance had not been enacted; and

(ii) the provisions of the repealed Securities and Futures Commission Ordinance or the repealed Leveraged Foreign Exchange Trading Ordinance (as the case may be) shall continue to apply to the exercise of the power and to any matters relating thereto (including any further exercise of power) as if this Ordinance had not been enacted.

63. Without prejudice to section 62, section 179 of this Ordinance applies even if –

(a) in the case of subsection (1)(a), (b), (c), (d) or (e) of that section 179, the matter described in such subsection as being suggested by the circumstances referred to in such subsection has occurred, or appears to the Commission as occurring, before the commencement of Part VIII of this Ordinance; or

(b) in the case of subsection (1)(f) of that section 179, the matter in respect of the investigation of which the Commission decides to provide assistance under section 186 of this Ordinance has occurred, or appears to the Commission as occurring, before such commencement.

Part IX of this Ordinance (Discipline, etc.)

64. Where –

(a) before the commencement of Part IX of this Ordinance, any power could have been, but was not, exercised under –

(i) section 35 or 36 of the repealed Commodities Trading Ordinance;