

MEMO# 34192

June 23, 2022

Hong Kong SFC Proposes to Strengthen Enforcement Capabilities

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TO: ICI Global Members
Chief Compliance Officer Committee
Global Regulated Funds Committee
Global Regulated Funds Committee - Asia SUBJECTS: Advertising
Compliance
Distribution
International/Global
Litigation & Enforcement RE: Hong Kong SFC Proposes to Strengthen Enforcement Capabilities

On 10 June 2022, the Hong Kong Securities and Futures Commission (SFC) published a consultation^[1] on proposed amendments to the Securities and Futures Ordinance (SFO) to enhance the regulatory tools available for effective enforcement. The proposed amendments relate to the SFO provisions on remedial orders, advertisement of investment products, and insider dealing. This memorandum briefly summarizes the proposed amendments.

The consultation deadline is 12 August 2022. ICI Global will track this consultation but does not intend to comment.

Remedial Orders against Regulated Persons^[2]

The SFC currently has a range of disciplinary powers against a regulated person who has been found guilty of misconduct or not to be a fit and proper person to remain a regulated person under sections 194 and 196 of the SFO.^[3] However, the SFC does not have the statutory powers to seek orders to restore, compensate, or otherwise protect the interests of investors or clients who may have been adversely affected by the regulated person's conduct, unless such conduct also constituted to a contravention of one of the "relevant provisions"^[4] or other regulatory requirements and conditions specified in section 213 of the SFO.^[5]

In other words, however serious a breach of the SFC's codes and guidelines (e.g., the Code of Conduct^[6]), the SFC could only apply to the Court of First Instance for orders to provide remedies if the breach falls within any of the circumstances outlined in section 213. To

close this gap, the SFC proposes to amend the section 213, enabling the SFC to apply for injunction and other orders under section 213 after having exercised any of its powers under section 194 or 196 against a regulated person. In particular, the SFC would be able to seek orders to restore the parties to any transaction to the position in which they were before the transaction was entered into and pay damages to any other persons. The amendments will also enable the SFC to apply for orders under section 213 where it has exercised any of its power under section 194 or 196 against a regulated person who is a director, investment manager, custodian, or a sub-custodian of an open-ended fund company.

Advertising of Investment Products to Professional Investors

As background, section 103(1) of the SFO prohibits the issue of advertisement, invitation, or document (collectively referred to as "advertisements") containing an invitation to the public to enter into agreement to deal in securities or any other structured products without getting the authorization of the SFC. Among others, advertisements of investment products intended only for professional investors (PIs) are exempted from SFC's pre-vetting requirement ("PI Exemption").[\[7\]](#)

The Court of Final Appeal has provided a wider construction to the PI Exemption, which states that even if the intention to sell only to PIs is not clearly stated in the advertisement, the exemption applies to any advertisement having some connection or relation to investment products that are or are intended to be disposed of only to PIs.[\[8\]](#) The SFC considers that this may expose the retail investors to unauthorized offers or solicitations to invest in risky or complex products which are unsuitable for them, as well as create difficulty in enforcement in practice.

The SFC, therefore, proposes to clarify the PI Exemption such that, regardless of whether the intention to sell only to PIs has been stated in the advertisements, a person may only issue to PIs, who have been identified as such in advance by an intermediary through its know-your-client and related procedures, advertisements of investment products which are or are intended to be sold only to PIs. Such advertisements should not be issued to the general public without the SFC's authorization. Further, the SFC notes that the exemption in relation to investment products sold or intended to be sold only to persons outside Hong Kong[\[9\]](#) is phrased in the same way as the PI exemption. For consistency and to avoid confusion, the SFC proposes to amend this provision in identical terms.

Enforcement for Insider Dealing

The current insider dealing regime in the SFO only applies to insider dealings with respect to Hong Kong-listed securities or their derivatives, as well as securities dully listed in Hong Kong and another jurisdiction or their derivatives. Where the insider dealings concern overseas-listed securities or their derivatives, the SFC could only deal with transactions involving specific persons rather than conduct that impacts the integrity of the wider market. On the other hand, the insider dealing provisions do not expressly cover insider dealing with respect to Hong Kong-listed securities or their derivatives where such acts have taken place overseas. Consequently, the SFC has to apply the common law test to determine the territorial jurisdiction in each case.

The SFC acknowledges that insider dealing laws in other major common law jurisdictions govern overseas conduct relating to securities of local issuers as well as local conduct relating to securities of overseas issuers.[\[10\]](#) The SFO provisions governing other market misconduct such as false trading, price rigging, and stock market manipulation adopt a

comparable approach in terms of the territorial scope. These provisions cover unlawful acts committed in Hong Kong or elsewhere that affect Hong Kong's financial markets, as well as unlawful acts committed in Hong Kong that affect non-Hong Kong financial markets.

In order to bring alignment with other major common law jurisdictions and the other market misconduct provisions of the SFO, the SFC proposes to expand the territorial scope of the insider dealing regime to include: (i) insider dealing involving Hong Kong-listed securities or their derivatives, regardless of where they occur; and (ii) any insider dealing involving overseas-listed securities or their derivatives, if any one or more of such acts occur in Hong Kong. However, a person suspected of perpetrating insider dealing in Hong Kong, in relation to overseas-listed securities or their derivatives, would not be regarded as having engaged in insider dealing unless the conduct is also unlawful in the relevant overseas jurisdiction.

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endnotes

[1] See Consultation Paper on Proposed Amendments to Enforcement-related Provisions of the Securities and Futures Ordinance, June 2022, available at <https://apps.sfc.hk/edistributionWeb/api/consultation/openFile?lang=EN&refNo=21CP3> ("Consultation Paper").

[2] Regulated person means a person who is or at the relevant time was a licensed person, a responsible officer of a licensed corporation, or a person involved in the management of the business of a licensed corporation. See SFO, at section 194(7), available at https://www.elegislation.gov.hk/hk/cap571?xpid=ID_1438403468858_002.

[3] The SFC may exercise a number of powers against a regulated person, including suspending or revoking licenses or registration, imposing fines, issuing reprimands and other powers, in cases where the regulated person is or was guilty of misconduct or the SFC is of the opinion that the regulated person is not a fit and proper person to be or to remain the same type of regulated person. See SFO Sections 194 and 196.

[4] "Relevant Provisions" refers to the provisions of the SFO, its subsidiary legislation and certain provisions of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32), Companies Ordinance (Cap. 622) and Anti-Money Laundering and Counter-Terrorist Finance Ordinance (Cap.615). See SFO at Schedule 1.

[5] The SFC may apply to the Court of First Instance for various orders to provide remedies for persons affected by contraventions by another person of: (i) any of the relevant provisions, (ii) any notice or requirement given or made under or pursuant to any of the relevant provisions, (iii) any of the terms and conditions of any license or registration under the SFO, or (iv) any other condition imposed under or pursuant to any provision of the SFO.

The remedial and other orders under section 213 the SFC may apply include: (i) an order restraining or prohibiting a breach of the relevant provisions; (ii) an order requiring a person to take such steps as the Court of First Instance may direct, including steps to restore the parties to any transaction to the position in which they were before the transaction was entered to; (iii) an order restraining or prohibiting a person from dealing in a specified property; (iv) an order appointing an administrator; (v) an order declaring that a contract is void or voidable; and (vi) an order directing a person to do or refrain from doing any act to ensure compliance with any other court order made

See SFO Section 213(1) and Section 213 (2).

[6] See Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission, available at https://www.sfc.hk/-/media/EN/assets/components/codes/files-current/web/codes/code-of-conduct-for-persons-licensed-by-or-registered-with-the-securities-and-futures-commission/Code_of_conduct-Dec-2020_Eng.pdf.

[7] See SFO, *supra* note 2, at Section 103(3k).

[8] See *SFC v. Pacific Sun Advisors Ltd and Mantel, Andrew Pieter*, FACC 11 of 2014 dated 20 March 2015, available at https://legalref.judiciary.hk/lrs/common/search/search_result_detail_frame.jsp?DIS=97598&QS=%2B&TP=JU.

[9] See SFO, *supra* note 2, at Section 103(3j).

[10] See Consultation Paper, *supra* note 1, at paragraph 44-46.