

# THE GROUP OF TEN - SECURITIES & FUTURES BILL

## SUMMARY OF MAJOR ISSUES

### **1 Expansion of criminal liability, with heavy penalties, where this is not justified**

- many offences are ones of strict liability, with (in some cases) limited defences, the onus of proof being on the defendant. Unless the defendant can demonstrate that the highest standards of care and diligence were shown, he will be guilty of a serious criminal offence
- the SFC will have power to make rules a breach of which will automatically be a criminal offence by a company and its executive officers, punishable with large fines and imprisonment
- the act of any employee is deemed to be that of the company, so a company commits a criminal offence if any of its employees acts in a criminal manner
- any officer of a company is also guilty of an offence committed by a company if due to his “neglect”
- serious criminal penalties are imposed for administrative matters, such as failing to notify the SFC within 2 business days that an individual has ceased to act as a licensed representative (fine of HK\$200,000, 6 months imprisonment and daily default fine)

### **2 Undue risk of criminal, civil and disciplinary sanctions for directors and other managers of licensed corporations, where not personally involved in wrongdoing**

- for breach of some rules made by SFC, all executive officers will automatically commit an offence (subject to very restricted defence)
- any officer is also guilty of offence committed by the company (or Market Misconduct Tribunal can treat him as guilty of “market misconduct”) if due to his “neglect”
- SFC can also discipline any responsible officer or other person involved in the management of the business for “misconduct” by a third party that arose through any “neglect” of that person
- every director is liable to compensate investors for misrepresentations made by the company (unless the director can prove a defence)

### **3 Market Misconduct**

- unnecessarily complex, with 20 categories of “market misconduct” and two other criminal offences
- the categories are unduly wide and uncertain eg when is a market “artificial”
- creates some offences of strict liability subject (in some cases) to restricted defence eg for false or misleading statements
- company can be criminally liable for “market misconduct” of any employee, and senior management can also be criminally liable, if “market misconduct” arose through their “neglect”

- potential for unlimited exposure of individuals, companies and their management to civil actions by investors

#### **4 Disclosure of interests in shares**

- concept of “interests” is extended to unissued shares and cash-settled derivatives, and disclosure of both long and short positions, and changes in the nature of an interest, will be required
- this is out of line with international market practice and makes the law immensely complex and onerous to comply with

#### **5 Scope of activities requiring licence**

- extended to provision of automated trading services. The scope of this definition is very unclear, and if the ATS is a “stock market” the ATS provider would need to become an Exchange participant. This is highly unsatisfactory for overseas exchanges and ECNs
- existing deficiencies remain e.g. leveraged foreign exchange trading is too widely defined

#### **6 Regulation of licensed persons**

- it should not be necessary for all executive directors (e.g. those based overseas) to be individually licensed with the SFC
- overseas qualifications and experience should suffice for licensing in Hong Kong
- concerns over extension of compensation fund, and risk of cross-subsidies from one industry sector to another
- unclear what the effect of the Bill will be because rules to be made by SFC have not been published
- SFC should be required to consult the public before making any rules

#### **7 Offers of investments**

- current (unsatisfactory) rules largely remain in place
- new definitions of “investment arrangements” and unsolicited calls are far too wide

#### **8 Overall length, complexity, drafting deficiencies and inconsistencies**

- 381 Sections and 10 Schedules - yet most of the regulations applying to licensed persons will be in rules to be made by the SFC
- Part XV on disclosure of interests is almost incomprehensible
- Provisions on “false and misleading information” are scattered across Parts IV, X, XIII and XIV of the Bill

The Group would welcome the opportunity for substantive discussions with the FSB and the SFC on all its comments on the Bill.