



**IFPHK's Response to the Securities and Futures
Commission (SFC) Consultation Paper on
Proposed Amendments to Enforcement-related
Provisions of the Securities and Futures
Ordinance**

August 2022

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Profile of IFPHK

About IFPHK

IFPHK was established in June 2000 as a non-profit organization for the fast-growing financial services industry. It aims to be recognized in the region as the premier professional body representing financial planners dedicated to upholding the highest professional standards.

The Institute is the sole licensing body in Hong Kong authorized by Financial Planning Standards Board Limited to grant the much-coveted and internationally-recognized CFP® Certification and AFP® Certification to qualified financial planning professionals in Hong Kong and Macau.

Currently there are more than 188,100 CFP certificants in 26 countries/regions; the majority of these professionals are in the U.S., Canada, China, Australia and Japan, with approximately 4,400 CFP certificants in Hong Kong.

IFPHK has more than 7,500 members in Hong Kong including 1,100 Qualified Retirement Adviser (QRA) holders; and represents financial planning practitioners in diverse professional backgrounds such as banking, insurance, independent financial advisory, stock broking, accounting, and legal services.

The IFPHK's interest in this consultation

The IFPHK was established in June 2000 as a non-profit organization for the fast-growing financial services industry. It aims to be recognized in the region as a professional body representing those financial planners that uphold the highest standards for the benefit of the public. The IFPHK is the sole licensing body in Hong Kong authorized by FPSB to grant the much-coveted and internationally-recognized CFP® Certification and AFP® Certification to qualified financial planning professionals in Hong Kong and Macau.

As the leading professional institute representing the interests of the financial planning industry, the IFPHK has a duty to respond to any consultation paper that may impact its members and their clients. The IFPHK has previously provided feedback on the Consultation Papers that related to board level of investor protection and resolution regime. We have provided our feedback to the proposal to enhance protection of the

investing public as early as in 2009. Here are examples of relevant responses submitted by IFPHK:

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| Dec 2009 | Proposal to Enhance Protection of the Investing Public |
| Jun 2011 | Proposed Establishment of a Policyholder's Protection Fund |
| Apr 2014 | Consultation Document on an Effective Resolution Regime for Financial Institutions in Hong Kong |
| Dec 2014 | Consultation Document on enhancements to the Deposit Protection Scheme |
| Dec 2016 | Consultation Paper of the Proposals to Enhance the Financial Dispute Resolution Scheme by the Financial Dispute Resolution Centre |
| Jun 2018 | Consultation Paper on Proposed Enhancements to the Investor Compensation Regime and Related Legislative Amendments |
| Jan 2019 | Consultation Paper on Draft Guidelines on Exercising Power to Impose Pecuniary Penalty in Respect of Regulated Persons Under the Insurance Ordinance (Cap.41) |

In view of the above, the IFPHK has a strong interest in responding to this Consultation Paper related to enforcement reform of SFC.

The IFPHK's representation

The IFPHK was founded by 30 members (the "Founding Members") to raise the standards of financial planners and highlight the importance of sound financial planning.

The IFPHK currently has 26 Corporate Members, including banks, independent financial advisers, insurance companies, and securities brokerages. With our Corporate Members providing a full spectrum of client services and products, the IFPHK is well positioned to understand the needs, concerns, and aspirations of the financial planning community.

The SFC Consultation

On 10 Jun 2022, the Securities and Futures Commission (SFC) launched a two-month consultation on proposed enforcement-related amendments to the Securities and Futures Ordinance (SFO) to enable it to take more effective enforcement action (the “Consultation Paper”). The two month deadline ended on 12 August 2022.

The amendments would broaden the scope of some SFO provisions to expand the basis for the SFC to apply for remedial and other orders against a regulated person under section 213. Section 213 of the SFO enables the SFC to apply to the Court of First Instance for injunctions and other orders, including an order to restore the parties to any transaction to the position in which they were before the transaction was entered into. They would also enable the SFC to address insider dealing perpetrated in Hong Kong involving overseas-listed securities and insider dealing involving Hong Kong-listed securities perpetrated elsewhere. This would also apply to derivatives of these securities.

Other amendments include clarifying an exemption in section 103(3)(k) of the SFO such that, unless authorised by the SFC, advertisements of investment products which are intended to be sold only to professional investors may only be issued to professional investors who have been identified in advance as such by an intermediary through its know-your-client and related procedures. Section 103 of the SFO prohibits the issue of advertisements and other documents containing prescribed content unless the issue has been authorised by the SFC. By virtue of the application of section 103(3)(k), this prohibition currently does not apply to advertisements and other documents made in respect of investment products which are or are intended to be sold only to professional investors, eg, individuals having a portfolio valued at not less than \$8 million.¹

The Consultation Paper contains 5 questions in three parts

Part 1 – Amendments to section 213 of the SFO to expand the basis on which the SFC may apply for remedial and other orders against a regulated person

1. Do you agree with: (i) the proposal to amend section 213 of the SFO to expand the basis on which the SFC may apply to the CFI for remedial and other orders after having exercised any of its powers under section 194 or 196 of the SFO against a regulated

¹ SFC press release on 10 Jun 2022

person, and; (ii) the proposed consequential amendments to section 213(1), (2), (7) and (11)? Please explain your view.

2. Do you have any comments on the proposed consequential amendments to section 213(3A) in respect of OFCs? Please explain your view.

Part 2 – Amendments to exemptions in section 103 of the SFO

3. Do you agree with the proposal to amend the exemption set out in section 103(3)(k) and the consequential amendments to section 103(3)(j)? Please explain your view.

Part 3 – Amendments to the insider dealing provisions of the SFO

4. Do you agree with the proposal to expand the scope of insider dealing provisions of the SFO to cover insider dealing perpetrated in Hong Kong with respect to overseas-listed securities or their derivatives? Please explain your view.

5. Do you agree with the proposal to expand the scope of insider dealing provisions of the SFO to cover insider dealing perpetrated outside of Hong Kong, if it involves any Hong Kong-listed securities or their derivatives? Please explain your view.

The IFPHK's Submission

The views expressed in this submission paper are not necessarily summaries of the views taken from the industry. They may have undergone more independent and critical analysis and consideration by the IFPHK as a professional body. As a result, not all the views collected by the IFPHK are recorded in this submission paper and neither have all the views expressed in this submission paper been directly endorsed by those industry representatives or members consulted.

Key Principles

Prior to providing our views on the questions stipulated in the Consultation Paper, we wish to point out that the IFPHK's responses are formed upon the following two principles:

Enhancing consumer protection

The IFPHK has always believed that qualified intermediaries and well-informed and educated consumers, together with a robust framework, should form the core pillars for protecting the investing public. As financial products get more complex and sophisticated, it is of utmost importance that investors/consumers are provided with proper and adequate protection under a sound and effective regulatory system. The IFPHK supports a regulatory system which would facilitate delivering better financial products and services to the benefit of members of the public, as well as protecting them. Hence, the effectiveness of consumer protection and a healthy balance of robust regulations and market development are the IFPHK's areas of focus. A robust regulatory framework to IFPHK includes sound redress or dispute resolution mechanisms.

Moreover, investor protection is the responsibility as well as one of the top priorities of securities regulators worldwide. Investor protection is one of the three main objectives of securities regulation and of IOSCO. IOSCO Objectives and Principle 3 of the Principles of Securities Regulation and the IOSCO Assessment Methodology ("IOSCO Methodology") states that a regulator should have adequate power to impose credible and effective corrective measures².

² Complaint Handling and Redress System for Retail Investors, Final Report, OICU-IOSCO, January 2021.

Aligning with international standard

Globalization and financial market integration have increased rapidly in the past decades. As an international financial centre, Hong Kong is not immune from international financial market and regulatory development. This has been illustrated by waves of financial crisis, where problems originating in one country quickly spread across the globe. In order to enable Hong Kong to continue to excel in its status as an international financial centre, it is essential that we keep abreast of the development of international standard.

As aforementioned, Principle 3 of IOSCO Methodology states that a regulator should have adequate power to impose credible and effective corrective measures, e.g. redress and correction of securities law violations. Principle 12 also states that the regulator should provide for an effective and credible use of enforcement powers.³ Regulators in Hong Kong shall therefore constantly review whether their enforcement powers are aligned to international best practice.

Part 1 – Amendments to section 213 of the SFO to expand the basis on which the SFC may apply for remedial and other orders against a regulated person

Question 1

Do you agree with: (i) the proposal to amend section 213 of the SFO to expand the basis on which the SFC may apply to the CFI for remedial and other orders after having exercised any of its powers under section 194 or 196 of the SFO against a regulated person, and; (ii) the proposed consequential amendments to section 213(1), (2), (7) and (11)? Please explain your view.

Question 2

Do you have any comments on the proposed consequential amendments to section 213(3A) in respect of OFCs? Please explain your view.

At present, section 213 provides the SFC with the power to seek various forms of relief⁴.

³ Complaint Handling and Redress System for Retail Investors, Final Report, OICU-IOSCO, January 2021.

⁴ Form of relief available under section 213, include the followings

- an order restraining or prohibiting a breach of the relevant provisions;
- an order requiring a person to take steps to restore the parties to any transaction to the position in which they were before the transaction was entered into;

However, under the current drafting of section 213, the SFC may only seek this relief in order to provide remedies for persons affected by contraventions of another person of certain “relevant provisions” and any notice, requirement, conditions, and terms of any license or registration. “Relevant provisions” is defined comparatively broadly in Schedule 1 of the SFO. Therefore, this definition does not include the SFC’s codes and guidelines, including most notably the Code of Conduct.

The SFC has therefore proposed in the Consultation Paper that section 213 be amended to, amongst other matters:

- that section 213(1) be amended to introduce an additional ground under a new paragraph (c) for the SFC to apply for orders under section 213 where it has exercised any of its powers under section 194(1), 194(2), 196(1) or 196(2) against a regulated person.
- that section 213(2) be amended to introduce an additional order that may be made by the CFI to restore the parties to any transaction to the position in which they were before the transaction was entered into, where the SFC has exercised any of its powers under section 194 or 196 in respect of the regulated person.
- to ensure that the grounds for seeking additional orders in respect of open-ended fund companies (**OFC**) were consistent with those set out in section 213(1), we also propose to make a consequential amendment to section 213(3A) to add an additional ground to enable the SFC to apply for orders under section 213 where it has exercised any of its powers under section 194(1), 194(2), 196(1) or 196(2) against a regulated person who is a director, investment manager, custodian or a sub-custodian of an OFC.
- enable the CFI to make an order under section 213(8) against a regulated person to pay damages where the SFC has exercised any of its disciplinary powers against a regulated person.
- consequential amendments are also proposed to be made to section 213(7) so

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- an order restraining or prohibiting a person from dealing in a specified property;
 - an order appointing an administrator;
 - an order declaring that a contract is void or voidable; and
 - an order directing a person to do or refrain from doing any act to ensure compliance with any other court order made.

that an order may be made under subsection (1), irrespective of whether or not the person against whom the order is made intends to engage again, or to continue to engage, in any matters which gave rise to the SFC's exercise of a disciplinary power referred to in the new section 213(1)(c). This is modelled upon the existing section 213(7)(a), which applies to matters referred to in section 213(1)(a)(i) to (v). In addition, a definition of "regulated person" is proposed to be added to section 213(11) which would have the meaning given to it by section 194(7) or 196(8) of the SFO (as applicable).

The purpose of the proposed amendments to section 213 of the SFO is to provide a cause of action to enable the SFC to apply to the Court of First Instance ("CFI") for injunctions and other orders under section 213 after having exercised any of its powers under section 194 or 196(5) of the SFO against a regulated person; in particular, to seek orders to restore the parties to any transaction to the position in which they were before the transaction was entered into (similar to an order under section 213(2)(b)) and pay damages to any other persons (section 213(8)). The proposed changes will give the SFC more effective means to protect investors and the interests of clients of regulated persons.

IFPHK's Response

Based on the investor protection principle, IFPHK agrees to implement changes to enhance enforcement measures and give SFC a more effective means to protect investors. Although the SFC can pursue enforcement action by way of criminal prosecution as well as civil, disciplinary, and market misconduct proceedings, in recent years, the SFC has focus on using its civil enforcement measures. The cost of disciplinary fines significantly increased between 2015 and 2019, and within the 2020/2021 Period, the SFC's fines rocketed to a historical high. These fines are mostly focused on intermediary misconduct. These also include IPO sponsor failures, anti-money laundering (AML) related breaches, and deficient selling practices (such as internal control failures).⁵ Notwithstanding of the above, there are limitations in SFC's current disciplinary powers in respect of breaches of its codes, guidelines, and circulars, particularly with the implementation of financial penalties. At present, fines are capped at a maximum of HK\$10 million or three times of the profit gained or loss avoided,

⁵ Allen & Overy, The SFC's recent regulatory enforcement trends.

whichever is the higher. However, these fines are not remedies that compensate retail investors.

When referring to international practice. Globally, financial regulators use various enforcement tools to protect investors and maintain market discipline. However, most regulators do not have the authority to file lawsuits on behalf of individual investors. They have little direct involvement in investors' legal proceedings, except that in certain jurisdictions, they may be available to provide expert witness testimony. (Please refer to **Annex 1** for redress mechanism of selected overseas jurisdiction). Though SFC do have such power in terms of criminal prosecution, the limitation as mentioned in the paragraph above makes it impossible to exercise such power.⁶

IFPHK understands that aggrieved retail investors can also initiate legal action against financial service providers or their employees, provided applicable jurisdictional and other requirements are satisfied. Civil damages or remedies can be beneficial for retail investors, but the complexity and cost of legal proceedings may make it difficult for many investors. Individual investors may also wish to pursue in class actions which is quite common in the US. As Hong Kong's legislation currently only provides for a very limited class action regime and there are restrictions on litigation funding, this has limited the ability of individuals to seek class redress for violations, in particular for breaches of securities legislation.⁷ Therefore, it is logical to amend the SFO to enlarge SFC's enforcement power to protect retail investors.

The anticipated impacts of the amendments shall includes,

- these amendments will likely have a significant impact on the enforcement landscape. It significantly enhances the SFC's ability to act on the retail investors. In particular, the CFI should be able to make an order under section 213(8) against a regulated person to pay damages.
- as mentioned above, the SFC's fining power is currently capped at a maximum of \$10 million or three times of the profit gained or loss, but the new amendments presume to be not subject to the current cap on the SFC's fining powers. It is unclear what the size of compensations that would order by the courts under the new amendments, albeit IFPHK envisages future investor compensation claims will be

⁶ OICU-IOSCO, Complaint Handling and Redress System for Retail Investors Final Report, January 2021.

⁷ *ibid*

enormous, especially in the context of product mis-selling, market misconduct, and IPO-related misconduct.

- the proposed changes have given the Code of Conduct a legal status. Given the wide spectrum and breadth of requirements under its codes and guidelines. It is also important to note that a “regulated person” includes not only licensed person but also individuals involved in the management of the business. Hence, the impacts will be more far-reaching which the industry has to carefully study.

Part 2 – Amendments to exemptions in section 103 of the SFO

Question 3

Do you agree with the proposal to amend the exemption set out in section 103(3)(k) and the consequential amendments to section 103(3)(j)? Please explain your view.

The change proposed by the SFC in Part 2 of the Consultation Paper concerns section 103 of the SFO. Section 103(1) makes it a criminal offence to issue or be in possession for the purposes of issue an advertisement, invitation or document which, to the person’s knowledge, contains an invitation to the public to enter into an agreement to deal in securities or any other structured products, to enter into regulated investment agreements, or to participate in a collective investment scheme, unless authorized by the SFC to do so. Section 103(3) further contains a list of exemptions to the marketing restrictions under s 103, including s 103(3)(k), which provides an exemption from the authorization requirement for advertisements of offers of investments that are disposed of, or intended to be disposed of, only to professional investors (the “**PI Exemption**”).

The SFC seeks an amendment to section 103(3)(k) to restore the PI exemption to the original point in time when the advertising materials are issued, by exempting from the authorisation requirement those advertisements which are issued only to PIs. Therefore, following the proposed amendments, unauthorised advertisements of investment products which are or are intended to be sold only to PIs may only be issued to PIs who have been identified as such in advance by an intermediary through its know-your-client and related procedures, regardless of whether or not such an intention has been stated on the advertisements. To better protect the interests of the investing public, advertisements of investment products which are or are intended to be sold only to PIs should not be issued to the general public without the SFC’s authorisation.

The SFC argues that this amendment is necessary on the basis that the *Pacific Sun* decision mentioned in the Consultation Paper has created a situation in which:

- unauthorized advertisements of products unsuitable for retail investors may be issued to the general public even if only intended for sale to PIs, exposing retail investors to offers to invest in risky and unsuitable products; and
- enforcement action needs to wait until the sale of a product has taken place in order to determine to whom it has been sold and whether the section 103(3)(k) exemption applies.

IFPHK Response

IFPHK supports the proposals and thinks it is sensible that the advertisement of unauthorized products should be confined to professional investors who have the experience and knowledge to understand complex products. It has been almost seven years since the *Pacific Sun* case, since then financial products have become more complex and diverse. The clarification or amendments means SFC in the future could protect retail investors against unauthorized advertisements of virtual asset-related products (which are not authorized products).

Part 3 – Amendments to the insider dealing provisions of the SFO

Question 4

Do you agree with the proposal to expand the scope of insider dealing provisions of the SFO to cover insider dealing perpetrated in Hong Kong with respect to overseas-listed securities or their derivatives? Please explain your view.

Question 5

Do you agree with the proposal to expand the scope of insider dealing provisions of the SFO to cover insider dealing perpetrated outside of Hong Kong, if it involves any Hong Kong-listed securities or their derivatives? Please explain your view.

The final change proposed by the SFC concerns the civil and criminal regimes under sections 270 and 291 of the SFO in respect of insider dealing, both of which currently apply to insider dealing concerning Hong Kong-listed securities or their derivatives, and securities that are dual-listed in Hong Kong and another jurisdiction or their derivatives. However, as noted by the SFC, the current regime has limitations on insider dealing:

- committed in Hong Kong with respect to overseas listed securities or their derivatives; and
- committed outside of Hong Kong in respect of Hong Kong listed securities or their derivatives.

Thus, the SFC proposes that:

- the definition of “listed” as defined in sections 245(2) (civil regime) and 285(2) (criminal regime) of the SFO be amended to include overseas-listed securities or their derivatives; and
- a new section be added to Part XIII and Part XIV of the SFO to expand the territorial scope of the insider dealing regimes to include: (i) any acts of insider dealing involving Hong Kong-listed securities or their derivatives regardless of where they occur; and (ii) any acts of insider dealing involving overseas-listed securities or their derivatives if any one or more of such acts occur in Hong Kong.

In support of the proposal, the SFC has cited in the Consultation Paper a few case examples in the Consultation Paper such as the case of *Securities and Futures Commission v Young Bik Fung & Ors*⁸. The SFC has also noted that the insider dealing laws of comparable common law jurisdictions such as Australia, Singapore and the UK govern overseas conduct relating to securities of local issuers as well as local conduct relating to securities of overseas issuers and that as such it is important to ensure that the SFO is aligned with those of other major common law jurisdictions and the other market misconduct provisions of the SFO.

⁸ Four defendants in Hong Kong, including two practising solicitors, dealt in the shares of a company listed elsewhere outside Hong Kong based on inside information acquired in Hong Kong. Since the corporation concerned was not listed on a recognised stock market in Hong Kong, the insider dealing provisions in section 270 or 291 of the SFO were not applicable. As a result of this limitation, the SFC resorted to seeking civil remedies under section 213 of the SFO and ultimately succeeded in obtaining a court order against the defendants in civil proceedings brought under section 213 by establishing that there had been contraventions of section 300 of the SFO. (from the Consultation Paper)

In particular, the SFC has noted that following the launch of Stock Connect, the proposed amendments would strengthen the SFC's regulatory powers in tackling insider dealing conducted in Hong Kong involving A-shares listed in mainland China.

IFPHK Response

IFPHK has no major comments on the proposals as long as it aligns with international practice. The proposals seek to close this gap in the legislation by extending the scope of the insider dealing provisions in Hong Kong to address insider dealing in Hong Kong concerning overseas-listed securities or their derivatives and to address conduct outside of Hong Kong in respect of Hong Kong listed securities or their derivatives.

As aforementioned, Globalization and financial market integration have increased rapidly in the past decades. This has been illustrated by waves of the financial crisis, where problems originating in one country quickly spread across the globe. Therefore, it is sensible to amend the legislation so that the SFC can tackle cross-border insider dealing. The proposed changes also strengthen the SFC's regulator powers in tackling insider dealing conducted in Hong Kong involving A-shares listed in Mainland China.

Annex 1

Redress mechanisms of selected overseas jurisdictions

| Jurisdiction | Details |
|----------------|--|
| Australia | <p>If investors are not satisfied with the financial service provider’s response to their complaint, individuals may initiate legal action. They are not bound by the decision in the alternative disputes resolution (ADR). In cases where the investor has suffered a large loss that exceeds the ADR cap of \$5,000, court action may be the only avenue available for compensation.</p> <p>There will be occasions when ASIC intervene in private litigation as a party. Alternatively, we may appear as amicus curiae or do neither. ASIC do not lightly intervene in matters where a case primarily concerns the personal legal rights and remedies available to the parties unless there is a broader regulatory benefit that may be achieved through our intervention. The law envisages ASIC intervention through express statutory provisions and under the rules of superior courts, such as the Federal Court and the state Supreme Courts. In some circumstances, ASIC also have the power to commence proceedings on behalf of a private claimant, or to indirectly assist claimants to themselves enforce their rights.</p> <p><i>(information from ASIC website and OICU-IOSCO, Complaint Handling and Redress System for Retail Investors Final Report, January 2021)</i></p> |
| United Kingdom | <p>Investors may pursue legal action instead of alternative disputes resolution. The court has wide discretion to impose remedies, including ordering a financial service providers to pay compensation to the investor.</p> <p>To prevent or stop serious harm occurring Financial Conduct Authority (FCA) use a wide range of enforcement powers – criminal, civil and regulatory – to protect consumers and to take action against firms and individuals that do not meet our standards. This includes, where possible, seeking redress or remedy for those harmed.</p> <p>For example, the FCA used its powers to require restitution using section 384 of FSMA for the first time in March 2017. In this instance, a firm agreed to pay compensation to investors for giving a false or misleading impression of its expected trading profit. FCA used the power again in February 2018 leading to a credit card lender repaying an estimated £168,781,000 in compensation for failing to disclose the full price of an add-on product to a credit card.</p> <p><i>(information from FCA website and OICU-IOSCO, Complaint Handling and Redress System for Retail Investors Final Report, January 2021)</i></p> |
| United States | <p>In the United States, the SEC and CFTC may bring enforcement actions against a financial service provider or a commodity futures merchant, or any other market participant acting in possible violation of the relevant laws and regulations, seeking civil penalties and remedies, such as injunctions and</p> |

| Jurisdiction | Details |
|---------------------|---|
| | <p>disgorgement of ill-gotten gains. If sufficient assets can be obtained from defendants, the SEC may petition the court to establish a “Fair Fund” to compensate eligible harmed investors. Fair Funds are not able to be established in every SEC enforcement action.</p> <p>Class actions are typically brought on behalf of investors who bought or sold a company’s publicly traded securities within a specific period of time and suffered economic injury as a result of the company’s violation(s) of the federal securities laws.</p> <p><i>(information from OICU-IOSCO, Complaint Handling and Redress System for Retail Investors Final Report, January 2021)</i></p> |