

Updating Your Study Manual

Instructions for Inserting Version 1.3, 2003

The followings serve as the instructions for updating **Topic 3: The Securities and Futures Ordinance** of Study Manual 1 for the Licensing Examination for Securities and Futures Intermediaries. Please be reminded that only the updated sections are provided for downloading. You may replace the relevant sections with this updated version for the study manual you possess.

Instructions:

1. Download and print out the following pages.
 2. **Remove** pages 3-9 to 3-10 and **Insert** new pages 3-9 to 3-10.
 3. **Remove** pages 3-21 to 3-22 and **Insert** new pages 3-21 to 3-22.
 4. **Remove** pages 3-25 to 3-26 and **Insert** new pages 3-25 to 3-26.
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in the information it must advise the SFC of changes **within** 7 business days after the change.

- 7.10 An associated entity of an intermediary other than an AFI, which receives or holds client assets of the intermediary cannot conduct any other business unless authorised in writing by the SFC.
- 7.11 If an associated entity contravenes any matters in paragraphs 7.9 and 7.10, it is guilty of an offence.

Safeguarding of clients' money

- 7.12 The SFC is empowered to make rules for the holding of and dealing with clients' money by *licensed corporations* (not AFIs) and their associated entities. A breach of the rules will be an offence. The SFC has made the Securities and Futures (Client Money) Rules under s.149 (Please refer to section 4 of topic 4 for details).

Keeping of records

- 7.13 The SFC is empowered to make rules for:
- the keeping of records by intermediaries (including registered institutions); and
 - the keeping of records by their associated entities of the intermediaries' clients' assets received or held by them.

The SFC has made the Securities and Futures (Keeping of Records) Rules under s.151 (Please refer to section 5 of topic 4 for details.)

- 7.14 If, with the intention of committing fraud, a person:
- makes false or misleading entries;
 - destroys any records; or
 - does not maintain records;

he is guilty of an offence.

Contract notes, receipts, statements of accounts and notifications

- 7.15 The SFC is empowered to make rules requiring:

- *intermediaries* (including registered AFIs) to prepare and issue to clients, contract notes, receipts, statements of account, and notifications; and
- their associated entities to prepare and issue receipts, statements of account and notifications.

The SFC has made the Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules under s.152 (Please refer to section 6 of topic 4 for details).

Provisions relating to audit matters

- 7.16 Please note that the audit provisions apply to *licensed corporations* (not to registered AFIs) and also to *associated entities of intermediaries*. Unlike the other sections of this part, most of the requirements relating to audits are contained in the SFO and not delegated to subsidiary legislation made by the SFC. The exceptions are that the Securities and Futures (Accounts and Audit) Rules have been made by the SFC under s.397 specifying the contents of audited financial statements to be prepared under s.156 and the form of the audit report on the statements (Please refer to section 7 of topic 4 for details).
- 7.17 The audited accounts of licensed corporations (not registered AFIs) must be submitted to the SFC not later than 4 months after the end of the financial year or, in the case of cessation accounts, the date of cessation of the business. Failure to submit accounts as required is an offence (s.156).

Appointment of auditors

- 7.18 Part VI provides that licensed corporations and associated entities of intermediaries will appoint auditors within one month of being licensed or becoming an associated entity and notify the SFC of such appointments within 7 days of the appointment. Failure to appoint auditors, in the manner above or where there is a vacancy, is an offence (s.153).

Removal or resignation of auditors

- 7.19 A licensed corporation or an associated entity of an intermediary must notify the SFC in writing within one business day if it gives notice of a resolution to remove or to replace an auditor, or the auditor ceases to be its auditor (s.154).

Special reports by auditors (s.157) and immunity provisions (s.158)

- 7.20 An auditor shall make a written report as soon as practicable:

- requiring it to maintain property in Hong Kong or elsewhere of a value or description specified by the SFC to ensure that it may be able to meet its liabilities in such a way as to allow the licensed corporation to freely transfer or dispose of the property.
- 11.3 The SFC may withdraw, vary or make substitutions to notices, giving reasons (s.209). The notices remain valid even if the licence is suspended or revoked (s.210). If the licensed person refuses or fails to comply with a notice, the SFC may apply to the Court of First Instance to order it to comply (s.211).

Winding up and bankruptcy orders and injunctions

- 11.4 The SFC may also petition or apply to the Court of First Instance respectively for:
- winding up orders for *corporations* (other than AFIs) under the Companies Ordinance on just and equitable grounds and bankruptcy orders for licensed representatives under the Bankruptcy Ordinance respectively, if it considers it desirable in the public interest (s.212); and
 - injunctions to prevent contravention by any person of the relevant provisions or any orders made or notices issued or any terms and conditions of any licence or registration (s.213).

Remedies against listed corporations

- 11.5 The SFC may, after consultation with the Financial Secretary and, in the case of an AFI, the HKMA, apply to the Court of First Instance for various orders where the business or affairs of a listed corporation are being conducted in a manner which is oppressive or fraudulent or unfairly prejudicial to its members (s.214).

Revision question:

Question 5: What is an associated entity for the purposes of the SFO? Why was this concept introduced?

12 Part XI – The Securities and Futures Appeals Tribunal

- 12.1 The SFO has established a full-time Securities and Futures Appeals Tribunal ('SFAT') chaired by a judge as Chairman to hear appeals against decisions made by the SFC and the HKMA (the latter in the case of SFC registered institutions). The decisions which can be reviewed by the SFAT are set out in Part 2 of Schedule 8 to the SFO.

13 Part XII – Investor Compensation

- 13.1 This part provides for a single investor compensation fund to cover losses incurred by clients of intermediaries in general including non-exchange participants. The compensation limits will be set by reference to individuals instead of brokers.

Formation of the Investor Compensation Fund

- 13.2 [The Investor Compensation Company Limited \('ICC'\) has been set up under the SFO to administer and manage the Investor Compensation Fund \('ICF'\).](#)

14 Part XIII – The Market Misconduct Tribunal and Part XIV – Offences Relating to Dealings in Securities and Futures Contracts

- 14.1 Parts XIII and XIV will be taken up in Topic 9.

15 Part XV – Disclosure of Interests

- 15.1 The disclosure provisions reflect the modern trend towards greater disclosure and transparency in securities markets, including the disclosure of interests in shares if they exceed specified levels (e.g. 5% of issued and unissued share capital), the interests of directors and chief executives (without limiting levels),

- shareholders of listed corporation taking up rights under qualifying bonus and rights issues;
- interests of bare trustees;
- interest in shares held by a custodian;
- discretionary trusts;
- interest in shares held by a qualified lender by way of security only for the purposes of a transaction entered into in the ordinary course of business as a qualified lender;
- interest acquired by an intermediary for not more than 3 business days as an agent for transactions entered into for principals of the intermediary who are not related corporations of the intermediary; and
- interest of intermediary arises under an exchange traded stock futures contract or an exchange traded stock options contract which it acquired in the ordinary course of its business under client's instructions and the intermediary enters into a back-to-back contract (as defined in the Securities and Futures (Disclosure of Interests – Exclusions) Regulations) with its client on the same day (s.3(1)(d) of the said Regulations).

Power to investigate ownership of listed companies

Investigation by company

- 15.8 A listed company may investigate (by requiring confirmations from relevant persons) any interests in its shares, short positions in shares comprised in its relevant share capital and interests in equity derivatives which have shares in the relevant share capital as the underlying instruments. It is obliged to issue its findings to the relevant exchange, the SFC and the HKMA. It must also carry out such an investigation if requisitioned by members holding at least 10% of the paid up capital (ss.329 and 331).

Appointment of inspectors by Financial Secretary

- 15.9 The Financial Secretary may appoint inspectors to investigate the ownership or control of a listed corporation (Division 11) if he thinks it necessary to determine the true persons financially interested or able to control the listed corporation. He may appoint if an application is made by a specified minimum number of members of the listed corporation and he is satisfied that there are reasonable grounds to make an appointment.

16 Part XVI – Miscellaneous

General

16.1 This is also a major Part of the SFO and gathers together a number of provisions of common application as well as regulatory powers. It includes miscellaneous provisions that do not fit elsewhere and additional ones which relate to the increase in civil law applications:

- The secrecy provisions (s.378) are transported from the old legislation; these specify various persons to whom the SFC may provide confidential information and the circumstances in which the SFC may do so (students need not know the details).
- Statutory immunity is provided to public officers performing SFC's statutory functions in good faith (s.380).
- Auditors of listed corporations reporting suspected fraud and other improper practices they encounter in the course of their audits are given immunity from liability under common law (s.381).

Provision of false and misleading information to the SFC

16.2 A person will be liable to criminal prosecution if he provides false or misleading information to the SFC in applications made or in other circumstances, knowingly, or reckless as to whether it is false or misleading (ss.383 and 384).

Power of SFC to intervene in civil proceedings

16.3 This new power enables the SFC to intervene in civil proceedings between third parties in cases which concern matters under the SFO, Parts II or XII, the Companies Ordinance, or statutory functions of the SFC (s.385).

Liabilities of officers of corporations for offences by the corporation

16.4 If an offence under the SFO committed by a licensed corporation is aided or abetted; counselled or procured by, or committed with the consent of, or is attributable to the recklessness of, an officer of the corporation, that officer will be guilty of the offence and be punishable accordingly (s.390).