

## Updating Your Study Manual

### Instructions for Inserting Version 1.3, 2003

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The followings serve as the instructions for updating **Topic 9: Market Misconduct, Improper Trading Practices and Compliance** 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.

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#### **Instructions:**

1. Download and print out the following pages.
  2. **Remove** pages 9-5 to 9-6            and            **Insert** new pages 9-5 to 9-6.
  3. **Remove** pages 9-23 to 9-24        and            **Insert** new pages 9-23 to 9-24.
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- up to 10 years imprisonment and/or HK\$10 million on indictment and conviction; and/or
- up to 3 years imprisonment and/or HK\$1 million on summary conviction; and
- in addition the court may impose a disqualification order, a ‘cold shoulder’ order or a disciplinary referral order on conviction.

### *Private civil actions and ensuing liability*

1.9 These are provided under s.281 (Part XIII) and s.305 (Part XIV) and include:

- the right of the affected person to sue for financial loss, available even if there are no MMT hearings, criminal actions or convictions involving the target person;
- the right to use MMT evidence in bringing such an action; and
- injunctions as an available remedy.

The statutory right of action does not affect or limit any common law rights or liabilities.

### **Transitional applications**

1.10 Insider dealing that has taken place in whole or in part before the implementation of the SFO ([discovered after 1 April 2003](#)) will be handled under the Securities (Insider Dealing) Ordinance and before the Insider Dealing Tribunal which will be preserved to hear such cases.

## **2 Definition of market misconduct in the SFO**

2.1 In this topic we shall consider market misconduct as defined in the SFO as well as other malpractices that may have the lesser impact of adversely affecting the fitness and properness of an intermediary or its staff. Market misconduct is identified in roughly the same way in Parts XIII and XIV, SFO to include:

- insider dealing;
- false trading;
- price rigging;

- disclosure of information about prohibited transactions;
- disclosure of false or misleading information inducing transactions; and
- stock market manipulation.

2.2 Part XIV specifies 3 additional types of offences that are not specified in Part XIII:

- fraudulent or deceptive acts or the use of fraudulent or deceptive devices in Type 1, 2 and 3 regulated activities (s.300);
- disclosure of false or misleading information inducing others to enter into LFE contracts (s.301); and
- falsely representing that a person has dealt in futures contracts on behalf of another (s.302).

### **3 Insider dealing (Division 4, Part III and Division 2, Part XIV, SFO)**

3.1 Two definitions have to be referred to in explaining what is insider dealing under the SFO:

*Relevant information* is specific information:

- in relation to a corporation, its shareholders or officers or its listed securities or their derivatives;
- which is not generally known to the persons who are accustomed or would be likely to deal in its listed securities; but
- if it were generally known to them,
- would be likely to materially affect the price of the securities.

*Connected persons* include:

- directors, employees or substantial shareholders (those holding at least 5% of nominal value of the shares for the purpose of insider dealing) of a corporation and its related corporation;
- persons who have access to relevant information by reason of having a professional or business relationship with the corporation or related corporation; and

## Checklist

Our last list of revision points includes the following:

- The Market Misconduct Tribunal ('MMT') will be established under Part XIII, SFO and will replace the Insider Dealing Tribunal.
- The SFC will, after investigation, refer cases of market misconduct to the FS or the Secretary of Justice for civil proceedings or criminal prosecutions.
- The MMT will review cases of market misconduct referred to it by the FS in civil proceedings.
- Criminal prosecutions will be launched by the Secretary of Justice before the court.
- Civil actions may be brought by third parties under Part XIV, SFO for loss suffered as a result of misconduct.
- The MMT will consist of 3 full-time members, a judge and two members.
- The MMT can compel witnesses to give evidence. Contempt rules will apply if a witness refuses to answer questions.
- The MMT will apply civil standards of proof, i.e. the balance of probabilities test.
- Civil proceedings and criminal prosecutions will not be brought against the same person on account of the same misconduct.
- The SFC has the power to prosecute minor cases summarily in a Magistrate's Court.
- The MMT may disqualify a person guilty of misconduct from holding office in a company, or from investing or trading in Hong Kong markets for up to a period of 5 years.
- The MMT may make a disgorgement order for an amount up to the profits made or loss avoided and interest as a result of the misconduct.
- Criminal sanctions for misconduct may be applied up to 10 years imprisonment and/or HK\$10m on conviction; or 3 years imprisonment and/or HK\$1m on summary conviction.
- Private civil actions are available to persons suffering loss even if no action has been taken in civil or criminal proceedings.
- Insider dealing which has taken place in whole or in part before the implementation of the SFO ([discovered after 1 April 2003](#)) will be handled under

the provisions of the Securities (Insider Dealing) Ordinance before the Insider Dealing Tribunal.

- Market misconduct includes insider dealing, etc. (Refer to paragraph 2.1).
- What is insider dealing? (Refer to paragraph 3.1).
- Name the defences against a charge of insider dealing. (Refer to paragraph 3.4).
- What is false trading? (Refer to paragraph 4.1).
- Wash trades are transactions involving sales and purchases without a change in beneficial ownership.
- What is price rigging? (See paragraph 5.2).
- Define stock market manipulation. (See paragraph 6.1).
- Market misconduct include transactions carried out in Hong Kong or elsewhere in respect of securities traded on a recognized stock market or an authorized ATS, or in Hong Kong, in respect of securities traded on an overseas market.
- Define the two cases of disclosure of information that constitute market misconduct. (Refer to section 7 and 8).
- If the provision of false or misleading information is intentional, reckless or negligent then it may give rise to civil proceedings; if it is intentional or reckless it may also give rise to criminal prosecution.
- State defences for disclosure in each of the two cases. (See paragraphs 7.2 and 8.3).
- The SFC may make rules under ss.273 and 397 excluding any acts defined as market misconduct in Parts XIII or XIV, SFO from the definition.
- Define boiler room activities, churning, front running, naked short selling, rat trading, switching and unsolicited calls. (Refer paragraphs 11.2 to 11.14).
- The SFC has made rules providing for installing an Investor Compensation Fund operated by a recognized Investor Compensation Company which will be available to clients trading in HKEx products through intermediaries (including licensed corporations, AFIs and securities margin financiers) and their associated persons such as employees and associated entities.
- Matters relating to ethics and compliance with the regulatory laws, rules, codes and guidelines are the concern of all directors and staff of intermediaries and not merely the concern of the compliance department.
- Personal data means any data relating directly or indirectly to a living individual, from which it is practicable for his identity to be found.