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INSIDER DEALING UNDER HONG KONG LAW

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INTRODUCTION

Securities and Futures Ordinance (**SFO**) contains:

- civil market misconduct offences (Part XIII)
- criminal market misconduct offences (Part XIV)

6 types of market misconduct:

- insider dealing
 - false trading
 - price rigging
 - disclosure of information about prohibited transactions
 - disclosure of false and misleading information inducing transactions
 - stock market manipulation
-
- Market Misconduct Tribunal (**MMT**) deals with civil cases
 - Courts deal with criminal cases



WHAT IS INSIDER DEALING?

A person connected with an HKEX-listed company (Listco) has privileged information which could impact Listco's share price if it becomes publicly known, and that person deals, or procures someone else to deal, in Listco's listed securities or their derivatives to make a profit or avoid a loss before the information is made public

OR

A person obtains information from another person they know to be connected with a Listco and deals, or procures someone else to deal, in Listco's listed securities or their derivatives to make a profit or avoid a loss before the information is made public

1. PERSON WITH INSIDE INFORMATION DEALS IN SECURITIES OF LISTCO WITH WHICH HE IS CONNECTED – SFO s 270(1)(a) + s291(1)(a)

Person connected with a Listco has information they know is inside information and:

- **deals in** Listco's listed securities or derivatives (or those of a related corporation)

OR

- **counsels or procures** another person to deal in those listed securities or derivatives, knowing or having reasonable cause to believe that the other person will deal in them

2. TAKEOVER OFFER - BIDDER DEALS IN LISTED TARGET'S SHARES SFO – s270(1)(b) + s291(1)(b)

A person who is contemplating or has contemplated making a **take-over offer** for a Listco + **knows the information** that the offer is contemplated, or is no longer contemplated, is inside information:

- **deals in** the Listco's listed securities or their derivatives or those of a related corporation, otherwise than for the purpose of the takeover;

OR

- **counsels or procures another person** to deal in those listed securities or derivatives, otherwise than for the purpose of the takeover



3. PERSON CONNECTED WITH LISTCO LEAKS INSIDE INFORMATION – SFO s270(1)(c) + s291(3)

When a person connected with a Listco:

- **has information** they know is inside information; and
- **discloses the information** (directly or indirectly) to another person , knowing or having reasonable cause to believe that the other person will use the information to deal

OR

- **counsels or procures** another person to deal in Listco's listed securities or their derivatives or those of a related corporation



4. BIDDER LEAKS TAKEOVER INFORMATION - SFO s270(1)(d) + s291(4)

A person who is contemplating or has contemplated making a takeover offer for a Listco + knows that the information that the offer is contemplated or no longer contemplated is inside information:

- **discloses the information** (directly or indirectly) to another person, knowing or having reasonable cause to believe that the other person will use the information to deal, or to counsel or procure another person to deal, in the Listco's listed securities or their derivatives or those of a related corporation

5. RECIPIENT OF INSIDE INFORMATION FROM PERSON CONNECTED WITH A LISTCO DEALS IN ITS LISTED SECURITIES OR THEIR DERIVATIVES – SFO s271(1)(e) + s291(5)

Person who has received information they know to be inside information relation to a Listco from a person they know is connected with the Listco and they know, or have reasonable cause to believe, that the person held the information because of their connection with the Listco:

- **deals** in Listco's listed securities or their derivatives or those of a related corporation; or
- **counsels or procures** another person to deal in those listed securities or derivatives



6. RECIPIENT OF INSIDER INFORMATION ABOUT A TAKEOVER DEALS IN THE TARGET'S SHARES – SFO s270(1)(f) + s291(6)

When a person has received, directly or indirectly, from a person they know or have reasonable cause to believe is contemplating, or no longer contemplating, making a take-over offer for a Listco, information to that effect and they know that is inside information in relation to the Listco + they

- deal in Listco's listed securities or their derivatives or those of a related corporation; or
- counsel or procure another person to do so

7. PERSON WITH INSIDE INFORMATION SEEKS TO FACILITATE DEALING ON OVERSEAS MARKET – SFO s270(2) + s291(7)

A person who knowingly has inside information under SFO s270(1) or s291(1):

- counsels or procures another person to deal in Listco's listed securities or their derivatives or those of a related corporation, knowing or having reasonable cause to believe that the other person will deal in those securities or derivatives **outside Hong Kong on an overseas stock market**; or
- discloses the inside information to another person knowing or having reasonable cause to believe that they **or some other person** will use the inside information to deal, or to counsel or procure another person to deal, in the Listco's listed securities or their derivatives or in those of a related corporation **outside Hong Kong on an overseas stock market**

INSIDER DEALING – DEFINITIONS

“SECURITIES”

- shares, stocks, debentures, loan stocks, funds, bonds or notes of, or issued by (or reasonably foreseeable will be issued by), a body, a government or municipal government authority
- rights, options or interests (described as units or otherwise) in, or in respect of, any of the above
- certificates of interest or participation in, temporary or interim certificates for, receipts for, or warrants to subscribe for or purchase, any of the above
- interests in a collective investment scheme
- interests, rights or property commonly known as securities (whether in the form of an instrument or not)



“SECURITIES” (Cont’d)

- structured products not within the above

“Structured product” is defined as:

- an instrument under which some or all of the return or amount due (or both) or the method of settlement is determined by reference to one or more of:
 - changes in the price, value or level (or a range within the price, value or level) of any type or combination of types of securities, commodity, index, property, interest rate, currency exchange rate or futures contract; or
 - changes in the price, value or level (or a range within the price, value or level) of any basket of more than one type, or any combination of types, of securities, commodity, index, property, interest rate, currency exchange rate or futures contract;
 - the occurrence or non-occurrence of any specified event or events (excluding an event or events relating only to the issuer or guarantor of the instrument or both the issuer and the guarantor)
- a regulated investment agreement
- any interests, rights or property the SFC prescribes as structured products (SFO s392)



INSIDER DEALING FOREIGN-LISTED SECURITIES

SFO definition of “listed” securities:

- HKEX-listed securities
- issued unlisted securities
- unissued securities
- suspended securities

DOES NOT include securities listed on overseas exchanges
(unless dual-listed in Hong Kong)

- courts rely on SFO s300 for overseas-listed shares
- see *SFC v. Young Bik Fung and others*





SFC V. YOUNG BIK FUNG & OTHERS

- Betty was a lawyer seconded to a HK bank working on its takeover of Taiwan-listed Hsinchu Bank
- She knew of proposed takeover + tender offer price before its public announcement
- Sister of one of solicitors opened a securities account in HK and purchased >1.5 million Hsinchu shares before announcement
- Sept 2006 – tender offer announced
- Sister accepted the offer for all the shares + distributed profits of approx. HK\$2.7 million among defendants

SFC V. YOUNG BIK FUNG & OTHERS

- Involved shares listed in Taiwan → outside the scope of the HK insider dealing regime
- Court relied on s.300 SFO
 - offer to buy the shares was made in HK
 - the sister's acceptance of the tender offer in HK
- Betty's misuse of material price sensitive information + breach of dealing restrictions amounted to a scheme or act of deception under s. 300

SFC V. YOUNG BIK FUNG & OTHERS

- **Court of Final Appeal** – s.300 SFO applied in respect of securities listed outside HK
 - *“substantial activities constituting the crime”* occurred in HK
- Proposed amendments to SFO will extend insider dealing to cover insider dealing conducted in HK involving securities listed on overseas stock markets or their derivatives
 - will not have to rely on SFO s300



PERSONS CONNECTED WITH A CORPORATION

SFO s247 + s287

- a director or employee of the Listco or a related corporation
- a substantial shareholder ($\geq 5\%$ shareholder) of the Listco or a related corporation
- person whose position may reasonably be expected to give them access to inside information due to a professional or business relationship between:
 - the person (or their employer, a company of which the person is a director, or a firm of which they are a partner) and the Listco, a related corporation, or an officer or substantial shareholder of either; or
 - the person being a director, employee or partner of a substantial shareholder of the Listco or a related corporation

PERSONS CONNECTED WITH A CORPORATION: SFO s247 + s287

- the person has access to inside information by virtue of being connected (within the meaning above) with another corporation + the inside information relates to a transaction (actual or contemplated) involving both corporations or one of them and the listed securities of the other or their derivatives, or to the fact that such transaction is no longer contemplated
- the person was connected with the corporation at any time in the 6 months before a relevant dealing
- a corporation is connected with another corporation if any of its directors or employees are connected
- SFO s248 + s288 — any public officer, member or employee of certain bodies who, in that capacity, obtains inside information about a corporation is deemed to be connected with that corporation



“CORPORATION”

Includes companies which are listed on HKEX but incorporated abroad

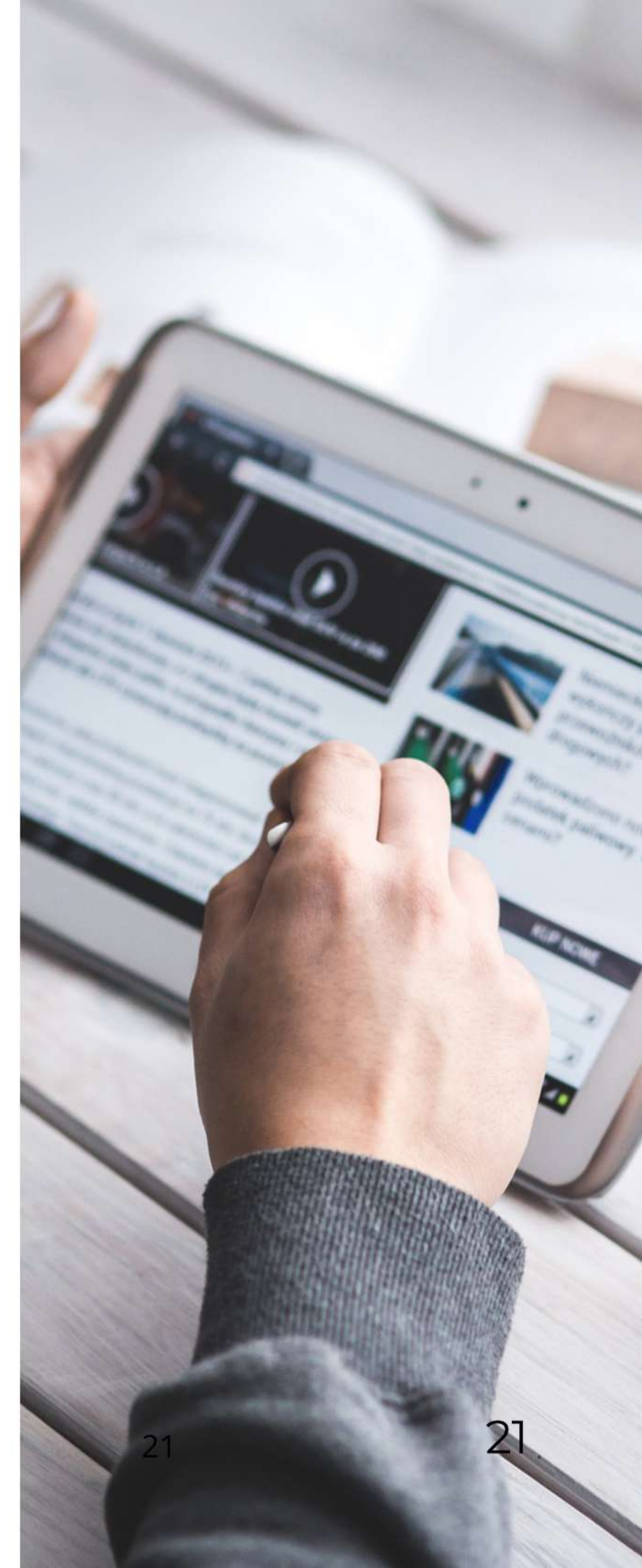
“RELATED CORPORATIONS”

- 1) 2 or more corporations are “**related corporations**” of each other if one of them is:
 - the holding company or subsidiary of the other; or
 - a subsidiary of the holding company of the other
- 2) Corporations are related if the same individual:
 - controls composition of the board of directors of 2 or more corporations
 - controls >50% of the voting power at general meetings of 2 or more corporations
 - holds >50% of the issued share capital (excluding any part with no right to participate beyond a specified amount on a profit or capital distribution) of 2 or more corporations

“INSIDE INFORMATION”

SFO s.245(1) — “inside information” in relation to a corporation is specific information about:

- the corporation
 - its shareholder or officer or
 - its listed securities or their derivatives
- not generally known to the persons who are accustomed, or would be likely, to deal in the corporation’s listed securities
 - but would, if it were generally known to them, be likely to materially affect the price of the listed securities
 - same definition as under the obligation to publicly announce inside information under SFO Part XIVA



“INSIDE INFORMATION” - MUST BE SPECIFIC

- means it must be capable of being identified, defined & unequivocally expressed

FIRSTONE INTERNATIONAL HOLDINGS LTD

- Information will be sufficiently specific:
 - *“if it carries with it such particulars as to a transaction, event or matter, or proposed transaction, event or matter, so as to allow that transaction, event or matter, to be identified and its nature to be coherently described and understood”*

“INSIDE INFORMATION” - MUST BE SPECIFIC

- Information does not need to be precise to be specific
 - not necessary for all particulars or details of the transaction, event or matter to be precisely known
- Information can still be deemed specific even if it has a vague quality
- Contrast with mere rumours, vague hopes and worries, and unsubstantiated conjecture ← NOT inside information

(See SFC Guidelines on Disclosure of Inside Information at para 17)



INSIDE INFORMATION - “NOT GENERALLY KNOWN”

- Information must not be generally known to the market
- Rumours or media speculation does not mean information is “generally known”
 - Information in the media, analyst research reports or electronic subscription databases cannot be assumed to be generally known to the market (See IDT 1990 report re. Lafe Holdings Limited)
- Considerations:
 - how widely the information is disseminated
 - whether information is accurate and complete
 - whether the information is reliable

INSIDE INFORMATION - “NOT GENERALLY KNOWN”

Information in the Media, Analyst Research etc., consider:

- whether the sources contain all the information that would need to be disclosed as inside information under SFO s307B(3) with no material omissions that could make the disclosure false or misleading;
- whether the market will realise that the information in those sources reflects information known to the corporation; and
- whether the information will be regarded as speculation or opinion of persons outside the corporation

If the information is incomplete or there are material omissions or doubts as to its bona fides → NOT generally known

INFORMATION “LIKELY TO HAVE A MATERIAL EFFECT ON THE PRICE OF LISTED SECURITIES”

- The information must be price sensitive
- The effect must be material
- HK MMT discussed test for “likely to materially affect the price of listed securities in its Nov 2024 report on the insider dealing by the CEO of China Forestry
- legal standard for “likely”
 - must be a “real prospect” of the information affecting the price
→ less than 50% probability would suffice



INFORMATION “LIKELY TO HAVE A MATERIAL EFFECT ON THE PRICE OF LISTED SECURITIES”

Materiality standard — whether the information on the particular share would influence persons who would be likely to deal in the share in deciding whether or not to buy or sell it

- hypothetical test
- no fixed thresholds of price movements or quantitative criteria
- magnitude of share price movement after information becomes publicly known is not conclusive – may be due to mixed impact of information released and other factors

DEALING IN SECURITIES

- SFO s249 – a person deals, whether they act as principal or agent
- agreeing to deal & buying or selling the right to deal are also “dealing”



WHAT IS NOT INSIDER DEALING?

THE DEFENCES ss. 271 + 292

The dealing, counselling or procuring was made:

- for the sole purpose of acquiring qualifying shares as a director or intending director of a corporation;
- in good faith in performance of an underwriting agreement for the listed securities or derivatives; or
- in good faith as a liquidator, receiver or trustee in bankruptcy

INSIDER DEALING DEFENCES

CHINESE WALL DEFENCE

A corporation (eg an investment bank or sponsor firm) may have a defence if:

- there were effective internal controls in place (a “Chinese wall”) to ring-fence inside information in the possession of any directors or employees; and
- each individual who made the decision for the corporation to deal, or counsel or procure a dealing, in the relevant listed securities or derivatives did not have access to the inside information at that time and did not receive advice from those in possession of that information



INNOCENT PURPOSE DEFENCE

- The purpose in dealing, counselling or procuring **DID NOT** include the purpose of securing or increasing a profit or avoiding or reducing a loss, whether for themselves or another, by using the inside information

DEFENCE AVAILABLE TO AN AGENT

- the person dealt, or counselled or procured another to deal, in a corporation's listed securities or their derivatives as agent and:
 - did not select or advise on the selection of the listed securities or derivatives; AND
 - did not know that the person for whom he acted was connected with that corporation or had the inside information

OFF-MARKET DEALINGS

It is a defence if the dealing occurred off-market in Hong Kong and:

- the person dealing in listed securities or their derivatives and the other party:
 - entered into the dealing directly with each other; and
 - at the time of the dealing, the other party knew, or ought reasonably to have known, of the inside information **OR**
- where a person counselled or procured another person to deal in listed securities or their derivatives, he counselled or procured the other party to enter into the dealing directly with him + at that time, the other party knew, or ought reasonably to have known, of the inside information



OTHER DEFENCES

It is a defence if a person dealt in listed securities or their derivatives, but did not counsel or procure the other party to deal

IF at the time of the dealing the other party knew, or ought reasonably to have known, that the person was a **person connected with the corporation**



OTHER DEFENCES (CONT'D)

A defence is available to a person who counselled or procured another to deal in listed securities or their derivatives if they establish that:

- the other person did not counsel or procure the counterparty to the dealing to deal in the listed securities or derivatives;

AND

- at the time he counselled or procured the other person to deal, the other party knew, or ought reasonably to have known, that the counterparty was a person connected with the corporation

OTHER DEFENCES (CONT'D)

A person who deals or counsels or procures another to deal in a corporation's listed securities or their derivatives has a defence if:

- they acted in connection with a dealing under consideration or the subject of negotiation (or in the course of a series of such dealings) with a view to facilitating the accomplishment of the dealing/ series of dealings

AND

- the inside information was **market information** arising directly out of their involvement in the dealing or series of dealings

MARKET INFORMATION - SFO s292

Market information includes information containing one or more of the following facts:

- that there has or is to be, or has not been or will not be, a dealing in listed securities or their derivatives, or that such dealing is under consideration or negotiation
- the quantity and price or price range of the listed securities or their derivatives involved; and
- the identity of the persons involved

Defence if a person trades with knowledge of their own trading intentions or activities and for those who simply execute or facilitate a trade on their behalf

DEALINGS SUBJECT TO RULES OF A RECOGNISED CLEARING HOUSE

“Dealing” subject to the rules of a recognised clearing house has a defence where the deal is entered into by the clearing house with a clearing participant for the purposes of the clearing and settlement of a market transaction

DEFENCE FOR TRUSTEES or PERSONAL REPRESENTATIVES

SFO s272 + s293 – defence for a trustee or personal representative who deals in, or counsels or procures a dealing, in listed securities or their derivatives:

- acting on advice obtained in good faith from a person appearing to be an appropriate person to provide that advice +
- that person does not appear to be someone who would be insider dealing if they dealt in the listed securities or their derivatives

DEFENCE FOR PERSONS EXERCISING SUBSCRIPTION RIGHTS

SFO s273 + s294 – defence for a person who dealt in listed securities or their derivatives:

- in exercising a right to subscribe for, or otherwise acquire those securities or their derivatives where that right was granted or derived from securities held before the person became aware of the inside information

INNOCENT PURPOSE DEFENCE

SFC V. YIU HOI YING CHARLES & OTHERS

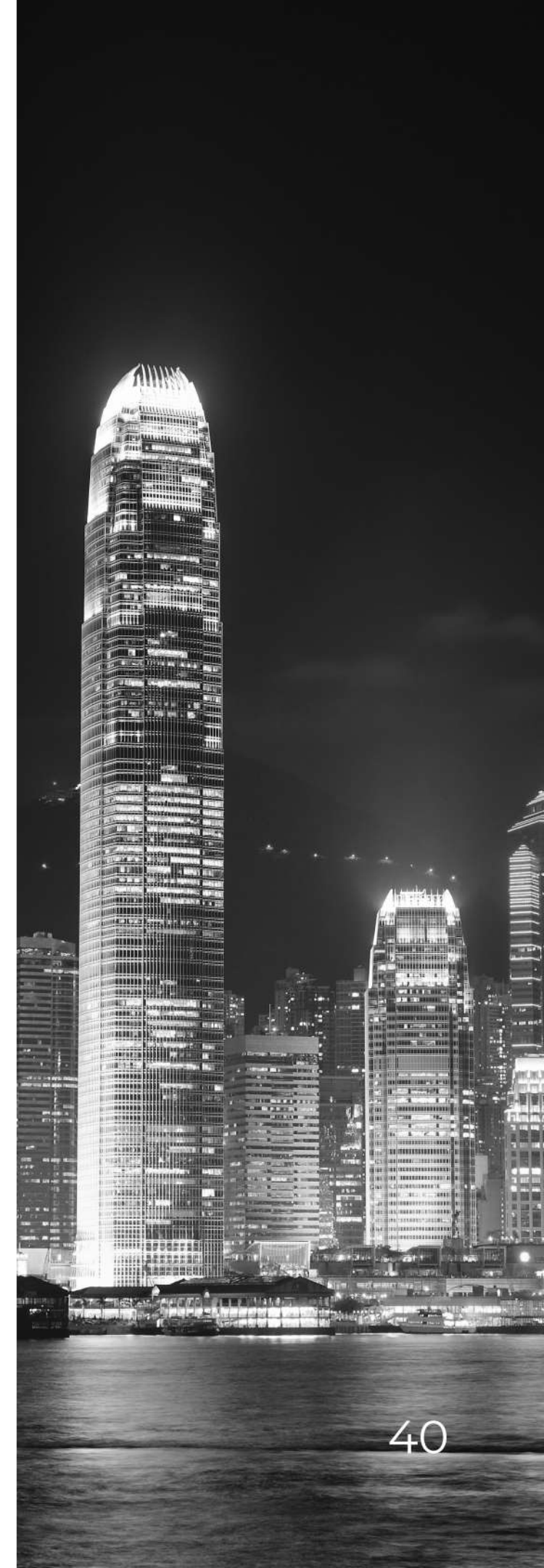
- 2 respondents held 6 million shares + 10 million shares in Asia Telemedia Limited (Asia Telemedia), respectively
- Asia Telemedia owed HK\$58 million to Goodpine Limited
- Goodpine Limited served a statutory demand and said it would issue a winding-up petition against Asia Telemedia if the debt was not repaid within 21 days
- There was a price surge in Telemedia's shares
- Respondents sold their shares making profits of HK\$5.3million + HK\$5.1million, respectively

SFC alleged:

- respondents' knowledge of Goodpine Limited's statutory demand was inside information
- they engaged in insider dealing when they relied on that information to dispose of their shares at a profit

SFC V. YIU HOI YING CHARLES & OTHERS (CONT'D)

- Respondents relied on the innocent purpose defence – they sold because of the rise in share price– not because of the inside information
- CFA rejected it in 4-to-1 decision for the SFC
- CFA: using inside information = turning the possession of inside information into action
 - mere withholding or non-disclosure of inside information is insufficient
 - the inside information must be exploited for financial advantage
- Respondents knew share price was artificially high because of the inside information they possessed + sold the shares to profit from that knowledge
- Innocent purpose defence does not apply if the inside information played a role in the decision making



MMT PROCEEDINGS

- MMT oversees civil proceedings and, where appropriate, imposes civil sanctions
 - independent body
 - inquisitorial in nature
 - entitled to direct that the SFC carry out further investigations & report its findings to the MMT

SFC can institute proceedings before MMT under SFO s. 252 to determine:

- whether any market misconduct has taken place +
- the identity of the persons engaged in market misconduct +
- the amount of any profit gained or loss avoided as a result of the market misconduct

MMT PROCEEDINGS (CONT'D)

MMT can identify a person as having engaged in insider dealing if:

- they committed insider dealing; OR
- the insider dealing was committed by a corporation of which the person is an officer with their consent or connivance; OR
- another person committed insider dealing + they assisted or connived with that person in the perpetration of the insider dealing, knowing that the conduct constituted or might constitute insider dealing

Civil standard of proof applies

- MMT must be satisfied that a person has engaged in insider dealing on the balance of probabilities
- MMT has powers to receive any evidence
 - SFO s 253(4) – allows the MMT to consider self-incriminatory evidence

MMT PROCEEDINGS (CONT'D)

SFC V. CHENG CHAK NGOK: FACTS

- Mr. Cheng was the executive director, CFO + company secretary of ENN Energy Holdings Limited (ENN)
- He obtained information on:
 - ENN's proposed acquisition of China Gas
 - the timing of the announcement of the general offer (the Announcement) +
 - the offer price
- Mr. Cheng used 3rd party's securities account to buy China Gas shares before Announcement → sold the shares for HK\$3 million profit
- MMT not satisfied on the balance of probabilities that Mr. Cheng dealt in the shares at the material times
 - insider dealing could not be proved

MMT PROCEEDINGS (CONT'D)

SFC V. CHENG CHAK NGOK: FACTS

SFC specified 4 grounds of appeal:

1

- MMT had erred in law in:
 - misdirecting itself that the inquiry was adversarial in nature
 - misdirecting itself that burden of proof applied and rested with the SFC +
 - failing to exercise its investigative powers under the SFO

2

- MMT had applied the criminal standard of proof

3

- MMT erred in concluding that it could not be satisfied that Mr. Cheng had engaged in insider dealing on a balance of probabilities

4

- MMT failed to consider exercising its investigative powers under the SFO before reaching its conclusion

MMT PROCEEDINGS (CONT'D)

SFC V. CHENG CHAK NGOK: Principles set out by the Court of Appeal

Nature of MMT Inquiry

- the nature of the MMT's inquiry on market misconduct is civil and inquisitorial

Standard of Proof

- on a balance of probabilities
- case law - the standard of proof will be proportional to the seriousness of the allegations

Burden of Proof

- Only relevant in adversarial proceedings
- In inquisitorial proceedings, no party has the burden of proof



MMT PROCEEDINGS (CONT'D)

SFC V. CHENG CHAK NGOK: Decision

Standard of proof

- MMT had not properly evaluated the available evidence
- Wrong in applying the criminal standard

Burden of proof

- MMT incorrectly imposed the burden of proof on the SFC - no burden of proof in an inquisitional inquiry
- SFC is only required to present evidence and information to the MMT, which should investigate the facts to reach a decision on the balance of probabilities

Remittal

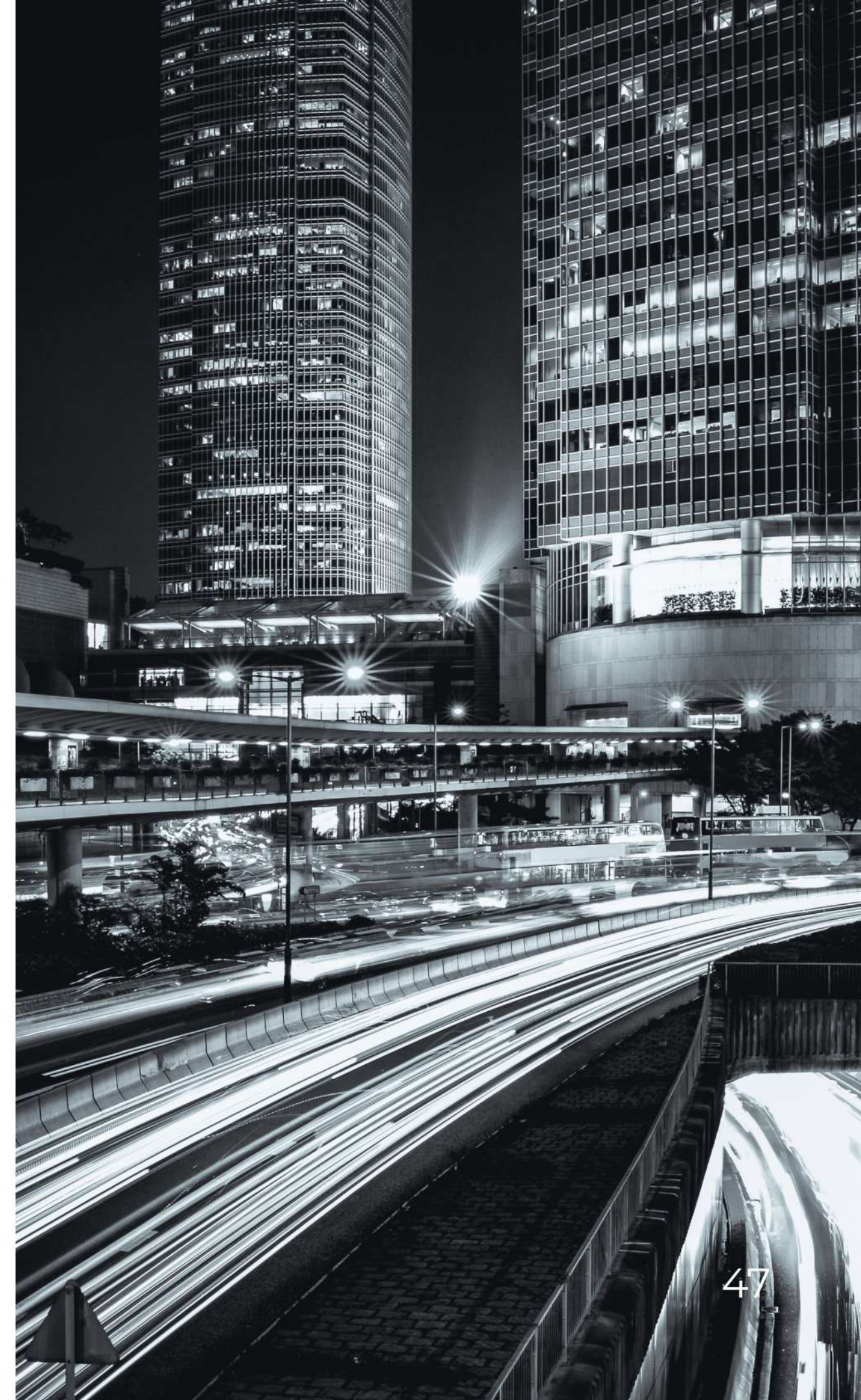
- CA upheld the SFC's appeal and remitted the matter to MMT to determine whether Mr. Cheng had dealt in the shares



MMT PROCEEDINGS (CONT'D)

SFC V. CHENG CHAK NGOK: MMT Retrial

- MMT concluded it was more probable than not that Mr. Cheng dealt in the shares from the following evidence:
 - Mr. Cheng received all correspondence + statements re. the securities accounts
 - Clear correlation between the share trading + the acquisition of inside information
 - Correlation between Mr. Cheng's whereabouts + the sources of the orders placed
 - No 3rd party nominee or other individual would have been in a position to place the orders
- Orders by the MMT after the retrial:
 - 54-month disqualification order
 - 52-month cold shoulder order
 - cease and desist order
 - disgorgement order (almost HK\$3 million)
 - Government + SFC costs orders
 - HKICPA disciplinary referral order





MMT ORDERS

s. 257(1) SFO

1. disqualification order
2. cold-shoulder order
3. cease and desist order
4. disgorgement order
5. cost orders
6. disciplinary referral

- SFO s.257(2) – MMT can take into account previous convictions in Hong Kong
- SFO ss. 253(2) + 254(6) – failure to comply with various requirements of the MMT or disrupting its proceedings
 - maximum fine of HK\$1million + maximum 2 years' imprisonment

APPEALS

- May appeal to the Court of Appeal on a point of law
- SFO s266 - Need to obtain leave of the Court of Appeal for an appeal based on a question of fact
- In the case of SFC disciplinary actions, can appeal to the SFAT
 - SFAT proceedings are civil in nature + use the civil standard of proof



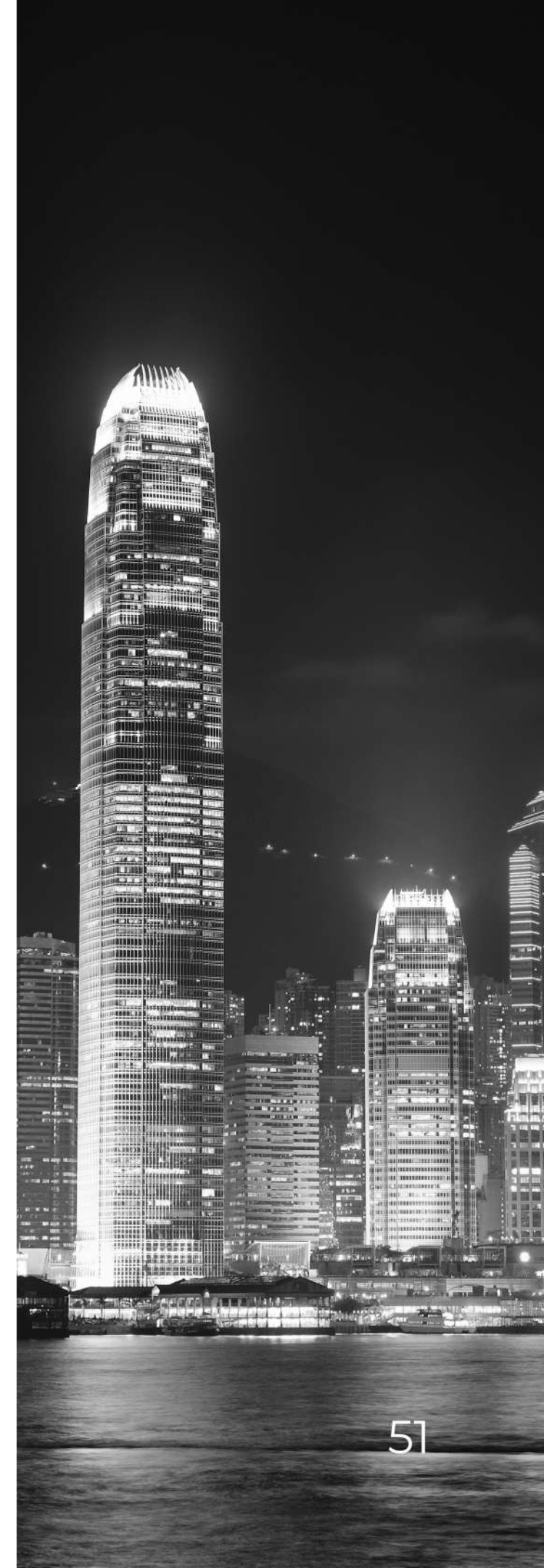
MMT CASE – RE. CHINA HUIYUAN JUICE GROUP LTD

- Ms. Sun Min had bought around 8.6 million shares of China Huiyuan Juice Group Ltd.
 - sold the shares within 48 hours after the public announcement of the company's take-over by Coca-Cola
 - made a profit of over HK\$55 million
- She denied having inside information or knowledge of the take-over
 - SFC's case centred on circumstantial evidence
 - handwritten notes in Ms. Sun's secretary's diary → notes for a meeting between Ms. Sun, her husband, her secretary and the COO of Ms. Sun's shipping company



MMT CASE – RE. CHINA HUIYUAN JUICE GROUP LTD (CONT'D)

- MMT held - if the identity of the connected person who passed on the inside information could not be ascertained, the MMT would decide, based on all available evidence, whether a compelling inference could be drawn
 - MMT inferred that the information came from an insider even though the insider's identity could not be ascertained
- The inside information in the diary must have come from Ms. Sun or she must have known of the information
 - rejected the secretary's evidence that she is not sure whether she passed on the information to Ms. Sun



MMT CASE – WARDERLY INTERNATIONAL HOLDINGS LIMITED

- Former company secretary (Lo) + lender and potential investor (Luu) held Warderly shares
 - Mid-2006 - Warderly had cash flow problems
 - Lo + Luu sold their shares in March + April 2007
- SFC alleged Lo & Luu engaged in insider dealing
 - when they sold their shares, they had price sensitive information concerning Warderly's poor financials, which was not publicly known
 - avoided losses by selling their shares



MMT CASE – WARDERLY INTERNATIONAL HOLDINGS LIMITED (CONT'D)

- SFC alleged the following events were “inside information”:
 - tightening of banking facilities from July 2006
 - overdue loans
 - rescheduled payments
 - issuance of demand letters and writs by banks and lenders
 - Warderly’s failure to repay loan and interest
 - grant of further loans
- MMT decision - the information regarding Warderly’s poor financial state was already known to the public + there was no adverse impact on the stock price
 - The information was therefore not inside information
 - Lo & Luu were found not to have engaged in insider dealing



CRIMINAL LIABILITY

- All forms of market misconduct are liable to prosecution as a criminal offence under Part XIV SFO
 - maximum penalty is 10 years' imprisonment + a fine up to HK\$10 million
- The court can also make disqualification, cold shoulder + disciplinary referral orders
- Non-compliance → offence liable to a maximum fine of HK\$1 million + up to 2 years' imprisonment

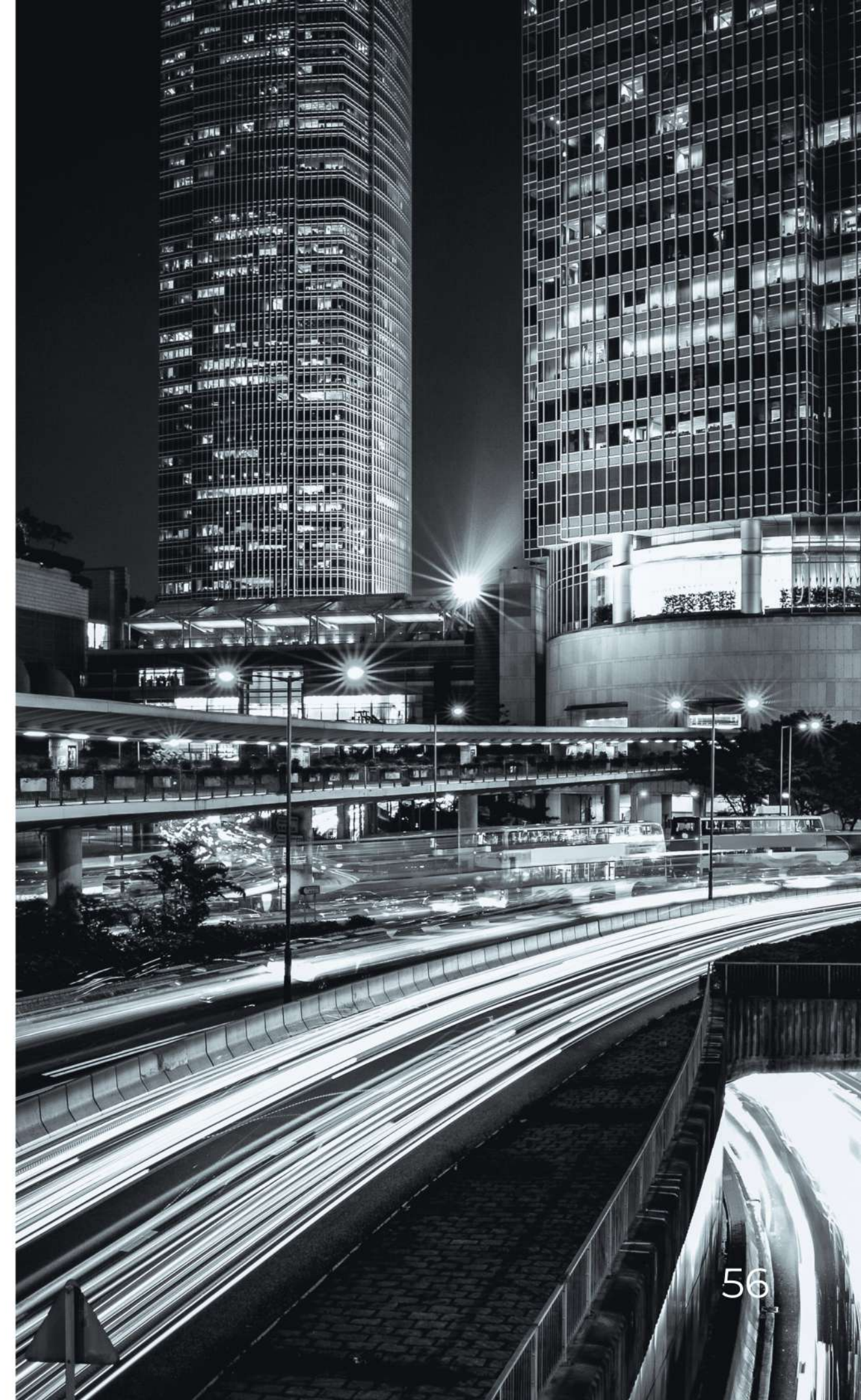
NO DOUBLE JEOPARDY

- A person who has been subject to criminal proceedings under Part XIV may NOT be subject to MMT proceedings if:
 - those proceedings are still pending or
 - no further criminal prosecution could be brought against that person again under Part XIV in respect of the same conduct + vice versa (SFO s283 + s307)
- Decision as to whether to take civil or criminal proceedings is made by the Secretary for Justice
 - whether there is sufficient evidence; and
 - whether it is in public interest
- SFC can institute summary criminal proceedings before a magistrate for less serious market misconduct offences



CIVIL LIABILITY: PRIVATE RIGHT OF ACTION

- SFO s281 + s305 - private right of civil action against the perpetrator in favour of anyone who has suffered a pecuniary loss as a result
 - ONLY if fair, just and reasonable
- A person is taken to have committed market misconduct if:
 - he has perpetrated any market misconduct
 - a corporation of which he is an officer perpetrated the market misconduct with his consent or connivance
 - any other person committed market misconduct + he assisted or connived with that person in perpetrating the market misconduct, knowing that such conduct constitutes or might constitute market misconduct
- Not necessary to have a finding of market misconduct before civil proceedings
 - but findings are admissible as prima facie evidence



TRANSACTIONS NOT VOID OR VOIDABLE

SFO s280 + s304 - a transaction is not void or voidable by reason only that it constitutes market misconduct

OFFICERS' LIABILITY

- SFO s279 – duty on every Listco officer to take reasonable measures regularly to ensure that proper safeguards are in place to prevent it from perpetrating any market misconduct
 - “officer of a corporation” includes:
 - a director, manager or secretary of, or any other person involved in the management of, the Listco
- SFO s258 – where a corporation has been identified as having been engaged in market misconduct + the market misconduct is directly or indirectly attributable to a breach by any person as an officer of the corporation of the duty imposed on him under SFO s279
 - MMT can make one or more orders even if that person has not been identified as having engaged in market misconduct himself





LIABILITY

- SFO s390 – where it is proved that an offence committed was aided, abetted, counselled, procured or induced by, or committed with the consent or connivance of, or attributable to the recklessness of, any officer of the corporation, or any person purporting to act in any such capacity
 - that person, as well as the corporation, is guilty of the offence
 - liable to be punished in accordance with Part XIV

DISCIPLINARY PROCEEDINGS

- SFO Part IX - Disciplinary procedures on any regulated person who is guilty of misconduct or who, in the opinion of the SFC, is not a fit and proper person to be or to remain the same type of regulated person
 - “Misconduct” = any contravention of the SFO or of the terms of any licence issued or registration
- Examples of disciplinary orders:
 - a. revocation or suspension of a person's licence in respect of all or any regulated activities
 - b. a fine $\leq$ the greater of HK\$10 million or 3 times the profit gained or loss avoided
 - c. prohibition orders
 - d. suspension or revocation of approval as a responsible officer



DISCIPLINARY PROCEEDINGS (CONT'D)

- The definition of “Persons” =
 - Corporations licensed under the SFO +
 - their Responsible Officers + persons involved in their management
 - Registered institutions +
 - their executive officers, persons involved in the management of their regulated business + individuals named in their register as carrying on a regulated activity



PROCEEDINGS UNDER SFO s213

- SFO s213 – on the application of the SFC, CFI can grant orders to prevent or remedy breaches of the SFO + other relevant ordinances
 - to ensure that assets of those suspected of market misconduct will be available to compensate investors for their losses resulting from the misconduct
 - to obtain financial compensation for investors through the grant of so-called 'restoration orders'

PROCEEDINGS UNDER SFO s213 (CONT'D)

s. 213 of the SFO also covers:

- aiding, abetting or assisting, counselling or procuring another person to commit a breach of the SFO
- inducing another person to commit a breach of the SFO
- directly or indirectly being knowingly involved in, or a party to, a breach of the SFO
- attempting or conspiring with others to commit a breach of the SFO



PROCEEDINGS UNDER SFO s213 (CONT'D)

Remedies

Injunctions + orders

- requiring the person to take steps to restore the parties to a transaction to the position they were in before the transaction OR
- restraining or prohibiting a person from acquiring, disposing of or dealing in any property

“Restoration orders”

- take the necessary measures to put the affected investors back in the same position they were in before the transaction was entered into



SFC v. TIGER ASIA

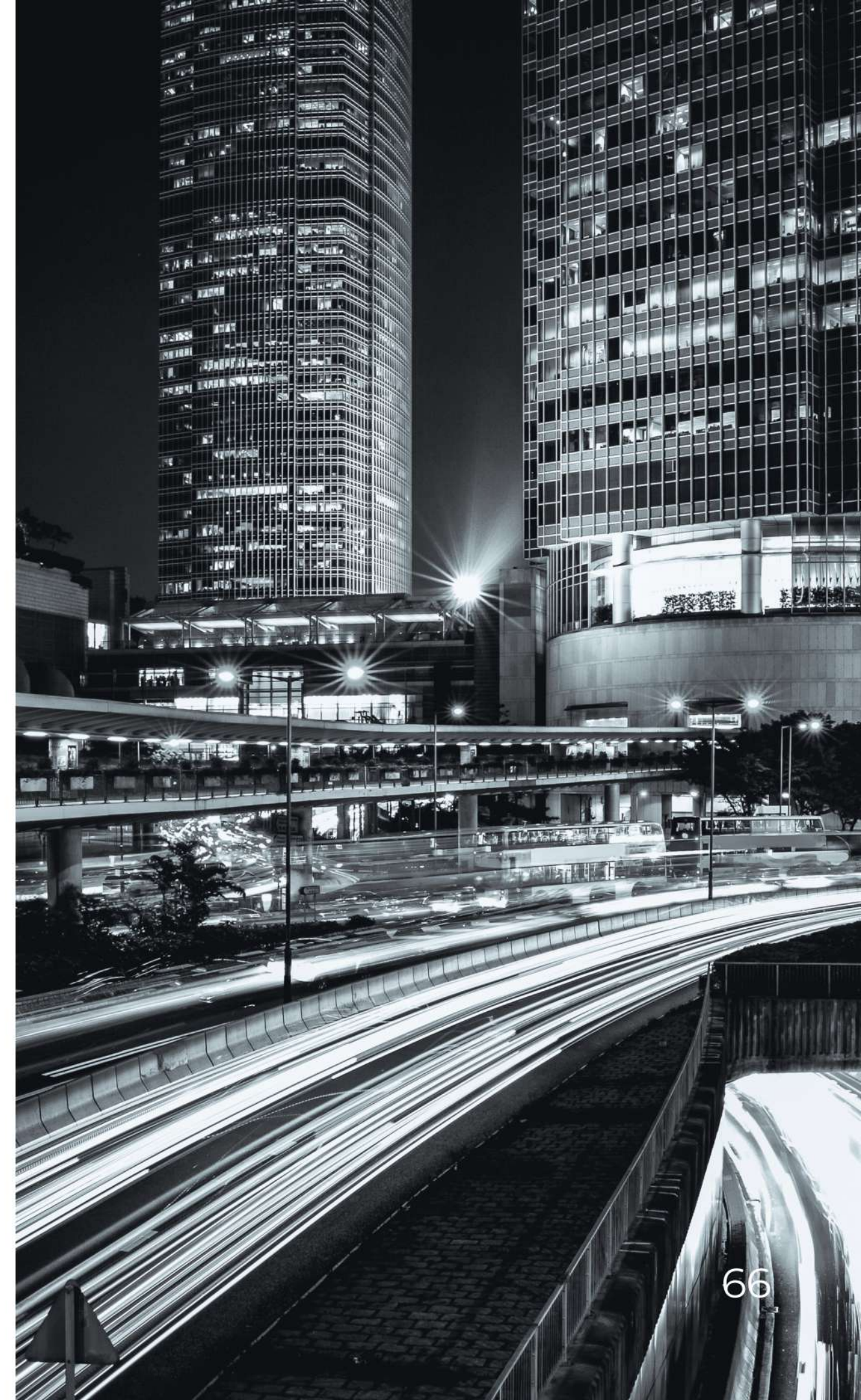
Case confirmed CFI's ability to make orders sought by SFC under s. 213 even in the absence of a prior finding of insider dealing by the MMT or a criminal court

- Tiger Asia received confidential + price sensitive information regarding placements of the shares of 2 banks
 - took short positions in the banks' shares before the placings were announced to the public + made a substantial profit
- Tiger Asia also manipulated the CCB share price downwards during the closing auction session
- Court ordered Tiger Asia + the 2 senior officers to pay around HK\$45.3 million to investors affected by their insider dealing

HKSAR v. Du Jun

- Du Jun was convicted of insider dealing in the shares of China Resources Holdings
 - shares worth HK\$86 million
 - sentenced to 6 years' imprisonment + fined HK\$1.7 million
- Civil proceedings under SFO s213 proceedings
 - court granted a restoration order against Du Jun, ordering him to pay approximately HK\$24 million to 237 affected investors
 - 5-year ban from serving as a director or managing director of a listed company
 - 5-year ban from dealing in securities in Hong Kong

SFC can pursue criminal insider dealing proceedings + s. 213 civil proceedings for investor compensation



RE. TELEEYE HOLDINGS LIMITED ("TELEEYE")

Facts:

- 2016 - Ms. Yik acted as TeleEye's controlling shareholder's representative in negotiating proposed takeover of TeleEye
 - Ms. Yik bought 22.7 million TeleEye shares through accounts she controlled before the takeover was announced
- TeleEye's share price rose by 70.7% on announcement of the takeover
- Ms. Yik then sold 15 million shares → profit of almost HK\$13 million

s. 213 proceedings:

- 2017: CFI granted Mareva injunction over Ms. Yik's assets and the 2 other defendants undertook to pay HK\$13 million into court

RE. TELEEYE HOLDINGS LIMITED ("TELEEYE") (CONT'D)

- 2021 - Ms. Yik convicted of insider dealing
- She was a person connected to TeleEye
 - acted as seller's representative in negotiations with buyer + involved in negotiating takeover
- That information was "specific information" + not generally known – not in dispute
- Material impact on share price was shown
- Ample evidence that Ms. Yik was aware the information was inside information
- 2 other defendants also convicted – they dealt in TeleEye shares having information they knew was inside information which they received from someone they knew to be connected with TeleEye
- In s. 213 proceedings, court ordered payment of HK\$13 million to share sale counterparties (restoration order)



CHOW CHIU CHI

- Dec. 2020 - Eastern Magistrates' Court convicted Mr. Chow (Chow), co. sec. of China Automation of insider dealing in its shares
 - Chow sentenced to 45 days' imprisonment + fined HK\$45,000
- Chow purchased 534,000 shares through his wife's securities account on learning of a possible general offer and being directed to arrange suspension of trading in the Company's shares
- Trading was suspended + China Automation published an announcement on 12 April about the possible general offer
- On resumption of trading on 13 April, the share price rose 18.81% from the previous closing price
- In April 2016, Chow sold China Automation shares realising HK\$7,417 profit
 - Notional profit of the remaining unsold shares was HK\$36,865
- Chow, by virtue of his position, had access to inside information + used it to profit from trading shares gaining an unfair advantage in the market



SFC V. CHAN PAK HOE PABLO

- Chan was found guilty of insider dealing and initially sentenced to 240 hours of community service + ordered to pay SFC's investigation costs
- On review, Eastern Magistrates Court sentenced Chan to 4 months' imprisonment + fined HK\$120,000
- On appeal, the CFI restored the original sentence - the Magistrate lacked jurisdiction to grant the application for review of a sentence once notice of appeal had been lodged
- CFA reversed that decision – a pending appeal against one part of a Magistrate's decision does not preclude review of another part. The 4 months' imprisonment + fine were restored
- Hon. Justice Ribeiro affirmed that the appropriate sentencing for insider dealing cases is a custodial sentence + a fine to disgorge all profits made from insider dealing

INSIDER DEALING IN LISTCO PRIVATISATIONS

BLOOMAGE BIOTECHNOLOGY CORPORATION LIMITED ("BLOOMAGE") PRIVATISATION

- Former executive general manager of China CITIC Bank International Limited, Mr Wu, worked on a loan to finance the privatisation of Main Board-listed Bloomage
- Wu bought >1 million Bloomage shares before the privatisation was made public + made HK\$3 million on share sale after the privatisation was announced

I.T LIMITED PRIVATISATION

- Suspected insider dealing in shares of I.T. Limited ("IT Ltd")
- Ms Tsang was a manager at an investment bank and allegedly tipped off Mr. Kwok re. privatisation of IT Ltd
- They bought 2.8 million IT Ltd shares before the planned privatisation was announced
- When share price rose 44.8% on announcement of the privatisation, they sold the shares making a profit of > HK\$4 million
- May 2023: COFI granted freezing orders over assets of Ms Tsang + Mr. Kwok under s.213 SFO

INSIDER DEALING IN LISTCO PRIVATISATIONS (CONT'D)

ELEC & ELTEK INTERNATIONAL COMPANY LIMITED POSSIBLE PRIVATISATION

- Wong Pak Wai, personal assistant of the chairman and executive director of a company proposing the potential privatisation of Elec & Eltek International Company Limited
- Wong purchased 3,000 shares prior to the announcement was made public and made profit of HK\$19,080
- Sentenced to 240 hours of community services due to profit size and Wong's early admission

INSIDER DEALING - RECENT CASES

CHINA FORESTRY HOLDINGS COMPANY LIMITED

- False and misleading information in the Company's prospectus and annual results
- Former CEO sold 119 million shares avoiding HK\$353 million loss knowing of the false or misleading information and of further information likely to be uncovered by auditors
- MMT was satisfied that when he sold his shares, he knew revelations could severely impact the Company's share price

BRIGHT SMART SECURITIES INTERNATIONAL (H.K.) LIMITED

- s.204 and 205 of the SFO - SFC can issue written notice to prohibit a licensed corporation from disposing of or dealing in property it holds on behalf of clients
 - Aug. 2022 – SFC issued restriction notice to Bright Smart – an SFC-licensed broker – freezing assets held in a client account holding proceeds of suspected insider dealing
 - As Bright Smart was not suspected of insider dealing, the notice did not affect its operations or other clients
 - SFC considered that the issue of the restriction notice was desirable and served the interests of the investing public as it prevented dissipation of proceeds of suspected insider dealing held in clients' accounts
 - SFC withdrew restriction notice after obtaining injunction against client prohibiting disposal of/dealing with assets in the account



2023 Consultation Conclusions

Section 3 of SFC Consultation Conclusions on Proposed Amendments to Enforcement-related Provisions of the SFO published in August 2023:

- Proposed amendments will broaden territorial scope of HK's insider dealing regime
- Current regime does not apply to:
 - securities that are only listed overseas (or their derivatives), even if relevant conduct is perpetrated in HK
 - insider dealing involving HK-listed securities (or their derivatives) where relevant conduct is perpetrated outside HK
- Proposed amendments will extend SFO insider dealing to include:
 - insider dealing perpetrated in HK involving securities listed on overseas stock markets or their derivatives +
 - insider dealing perpetrated outside HK, if it involves HK-listed securities or their derivatives

INSIDER DEALING IN HK INVOLVING OVERSEAS-LISTED SECURITIES (OR THEIR DERIVATIVES)

- Difference in nature and amount of relief between SFO s300 and insider dealing
 - E.g. Young Bik Fung case: the SFO s213 restoration order granted based on the section 300 contravention was to return the profits from the illicit trades to the bank
- BUT if restoration order had been based on a contravention of the insider dealing provisions (SFO s270 or s291)
 - order would have been calculated on the basis of restoring the affected investors impacted by the illicit trades to the position they were in before entering into the share sale



INSIDER DEALING IN HONG KONG INVOLVING OVERSEAS-LISTED SECURITIES (OR THEIR DERIVATIVES) (CONT'D)

- In another previous case, an HK-licensed intermediary dealt in overseas-listed securities before the announcement of a placing exercise
 - Intermediary had inside information provided by another HK-based intermediary when the dealing occurred
 - Apart from the mechanics of trading, the acts relating to the offence occurred in HK
 - Inadequate evidence to demonstrate suspect engaged in fraudulent or deceptive acts ← precluded action under SFO s300
- SFO s300 is a criminal offence: criminal standard of proof applies
 - No civil equivalent provision under Part XIII



INSIDER DEALING IN HONG KONG-LISTED SECURITIES OR THEIR DERIVATIVES WHICH TAKES PLACE OUTSIDE HK

- To determine territorial jurisdiction, SFC applies common law test of whether a substantial measure of the crime's activities took place in HK
- SFC Consultation Paper:
 - More than 60% of insider dealing cases between 2017-2021 related to insider dealing perpetrated outside HK in HK-listed securities or their derivatives
- SFO insider dealing regime will be extended to cover any act which takes place outside Hong Kong involving HK-listed securities or their derivatives
- Section 12.5 of the *Code of Conduct for Persons Licensed by or Registered with the SFC*:
 - SFC - Licensed intermediaries should report any breaches of any insider dealing provisions to the SFC
 - must use their best endeavours to obtain the necessary data to include in their report to the SFC

PROPOSED AMENDMENTS TO SFO INSIDER DEALING REGIME

- 1** Amend definition of “listed” in SFO s245(2) + s285(2)
 - include overseas-listed securities + their derivatives
- 2** Add new section to to expand territorial scope to cover acts of insider dealing involving:
 - a. HK-listed securities or their derivatives regardless of where they occur +
 - b. overseas-listed securities or their derivatives if any one or more of such acts occur in HK provided the conduct is also unlawful in the relevant jurisdiction
- 3** Repeal SFO s270(2) + s291(7) — insider dealing provisions on dual-listed shares which will be redundant
 - overseas-listed securities also within the insider dealing regime
- 4** SFO s271(5) — Off-market dealings defence
 - defence will be available to insider dealing involving overseas-listed securities or their derivatives

PROPOSED AMENDMENTS TO SFO INSIDER DEALING REGIME (CONT'D)

- The formulation of mens rea that applies to HK-listed securities or their derivatives is currently narrower — does not cover “or some other person” dealing
- Align the 2 mens rea formulations for insider dealing taking place through disclosure of inside information by adopting formulation in SFO s270(2)(b) + s291(7)(b)

Mens rea under SFO s270(2)(b) and s291(7)(b)

- insider dealing apply to dual-listed securities or their derivatives if:
 - person disclosing inside information knows or has reasonable cause to believe that the other person to whom the information is disclosed “*or some other person*” will deal in the listed securities or their derivatives

Mens rea under other SFO s270 + s291 sub-sections

- apply to securities listed only in HK or their derivatives is met if:
 - person disclosing inside information knows or has reasonable cause to believe that only “*the other person*” to whom the information is disclosed will deal in the listed securities or their derivatives

SFC Market Sounding Guidelines

- Effective on 2 May 2025 - applicable to SFC-licensed or registered persons disclosing or receiving “Market Sounding Information” in the course of “Market Sounding”
 - “Market Sounding” = communication of information about a planned transaction to potential investors to gauge their interest in the transaction and to help determine the terms of the transaction (e.g. pricing)
 - “Market Sounding Information” includes confidential information entrusted to an SFC-licensed or registered person by its client, an issuer, or an existing shareholder selling or buying in the secondary market (i.e. the “Market Sounding Beneficiary”)
- Core principles and procedures that disclosing persons and recipient persons will need to follow when conducting market sounding:

Examples for disclosers:

- must obtain the consent of the Market Sounding Beneficiary to conduct market sounding;
- restrict market sounding to as few investors as possible;
- use a standardised script

Examples for recipients:

- must give consent to receiving market sounding information
- must agree to ensure confidentiality and prevent it being misused or leaked