



Regulatory Update Series

Securities and Futures Ordinance

Part IV - Offers of Investments

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Outline

- ◆ Regulatory approach under Part IV of the SFO
- ◆ Degree of flexibility to address changing regulatory and market conditions
- ◆ Measures to facilitate product and market development



*Regulatory Approach under
Part IV of the SFO*



Functions and Duties of the SFC

- ◆ To secure an appropriate degree of protection for members of the public investing in or holding financial products (section 5(1)(1))
- ◆ To take into consideration the desirability of facilitating innovation in connection with financial products (section 6(2)(b))



Investments Covered by Part IV of the SFO

- ◆ Securities
- ◆ Regulated investment agreements
- ◆ Collective investment schemes



Offence to Fraudulently or Recklessly Induce Others to Invest Money

- ◆ In general, a person commits an offence if he makes any “fraudulent misrepresentation” or “reckless misrepresentation” for the purpose of inducing another to invest money (section 107(1))
 - ❖ Statements that are false, misleading or deceptive
 - ❖ Promises that are not capable of being fulfilled
 - ❖ Forecasts that are not justified on the facts then known



Civil Liability for Inducing Others to Invest Money

- ◆ In general, where a person makes any “fraudulent misrepresentation”, “reckless misrepresentation” or “negligent misrepresentation” by which another person is induced to invest money, the inducer shall be liable to pay compensation for any pecuniary loss that the other person has sustained as result of the reliance on the misrepresentation (section 108(1))



Restrictions on Financial Promotion

- ◆ The policy is that only those investments which are subject to certain regulatory safeguards should be offered to the public
- ◆ In general, a person commits an offence if he issues an advertisement, invitation or document which is or contains an invitation to the public to invest money unless the issue is authorized by the SFC (section 103(1))



Authorization by the SFC

- ◆ The SFC may authorize collective investment schemes subject to certain conditions where it considers appropriate (section 104(1))
- ◆ The SFC may also authorize the issue of advertisements, invitations or documents regarding investments subject to certain conditions where it considers appropriate (section 105(1))
- ◆ One of the authorization conditions is that there is an “approved person” for the purpose of being served by the SFC with notices and decisions in relation to the authorization (sections 104(2) and 105(2))



Withdrawal of Authorization

- ◆ The SFC may withdraw an authorization upon a request in writing made by the corresponding approved person (section 106(2))

- ◆ The SFC may also withdraw an authorization if it decides that
 - ❖ the information concerning the application was, at the time when it was submitted, false or misleading in a material particular
 - ❖ any of the authorization conditions imposed in respect of the authorization are not being complied with
 - ❖ it is desirable to withdraw the authorization in order to protect the interest of the investing public (section 106(1))



Withdrawal of Authorization (II)

- ◆ The SFC shall not withdraw an authorization without first giving the corresponding approved person a reasonable opportunity of being heard (section 106(5))
- ◆ Where the SFC withdraws an authorization, it shall by notice in writing notify the corresponding approved person of the decision and, in some cases, the reasons for which it is made (section 106(6))



Recognition of Other Regulatory Safeguards

- ◆ Exemptions from the general prohibition having regard to the “status” of the issuers
 - ❖ Invitations made by a licensed person or registered institution in respect of a financial product covered by its regulated activity (section 103(2)(a) - (c))
 - ❖ Invitations made by a recognized exchange company or recognized clearing house in respect of the provision of its services (section 103(2)(d))
 - ❖ Invitations made by a person who is engaged in the business of selling and purchasing property other than securities in the ordinary course of that business (section 103(2)(i))

- ◆ These exemptions do not apply to anything done in respect of unauthorized collective investment schemes (section 103(11))



Recognition of Other Regulatory Safeguards (II)

- ◆ Exemptions from the general prohibition having regard to the “status” of the materials issued
 - ❖ Prospectuses which comply with the Companies Ordinance (section 103(3)(a))
 - ❖ Application forms for shares or debentures issued together with prospectuses which comply with the Companies Ordinance (section 103(3)(c))
 - ❖ Materials made in respect of the issue of listed securities approved by the recognized exchange company and in compliance with the rules made under Part III of the SFO governing the listing of securities (section 103(3)(h))



*Degree of Flexibility to Address Changing
Regulatory and Market Conditions*



Scope of the Regime

- ◆ The Financial Secretary may by notice published in the Gazette prescribe that
 - ❖ any interests, rights or properties are to be regarded as securities or not to be so regarded
 - ❖ certain arrangements are to be regarded as collective investment schemes or not to be so regarded



Securities and Futures (Collective Investment Schemes) Notice

- ◆ Based on the existing Protection of Investors (Gold Purchase) Order
- ◆ “Paper gold schemes” to be regarded as collective investment schemes and subject to the regime under Part IV of the SFO



Measures to Facilitate Product and Market Development



Product Development

- ◆ Adopted a single notion of “collective investment scheme”
- ◆ Moved away from the “antique” terms focusing on the form or structure of the products
- ◆ Based on the nature of the products
 - ❖ collective management by a third party operator in such a way that investors would have no day-to-day control over the underlying properties
 - ❖ pooling of interests among investors
 - ❖ provision of profits or returns



Product Development (II)

- ◆ Exemption for invitations made in respect of certificates of deposit issued by authorized financial institutions (section 103(3)(e))
- ◆ Subsequent submission requirements (section 110(1))
- ◆ Securities and Futures (Exempted Instruments - Information) Rules



Market Development

- ◆ Introduced a new exemption for securities admitted to trading on a recognized stock market pursuant to rules made under Part III of the SFO regarding exchange companies
- ◆ Introduced another new exemption for investments that are offered only to “professional investors”



“Professional Investor”

- ◆ Defined in Schedule 1 to the SFO
 - ❖ Any intermediary or any other person carrying on the business of the provision of investment services and regulated outside Hong Kong
 - ❖ Any authorized financial institution or any bank regulated outside Hong Kong
 - ❖ Any authorized insurer or any other person carrying on insurance business and regulated outside Hong Kong
 - ❖ Any authorized collective investment scheme or any other scheme which is similarly constituted and regulated outside Hong Kong
 - ❖ Any person of a class which is prescribed by rules made under section 397 of the SFO



Securities and Futures (Professional Investor) Rules

- ◆ Trust corporations having been entrusted with total assets of not less than HK\$40 million
- ◆ Individuals having a portfolio comprising of securities or certificates of deposit of not less than HK\$8 million
- ◆ Corporations or partnerships having a portfolio comprising of securities or certificates of deposit of not less than HK\$8 million or total assets of not less than \$40 million



Q & A Session