

# Enforcement

Our mission is to protect investors and uphold the integrity of the Hong Kong markets by deterring unlawful or improper activities through effective surveillance and enforcement.

## [ Achievements ]

- Negotiated a record ex-gratia payment to investors of \$255 million by an investment adviser
- Reached a record \$30 million settlement with a sponsor
- First Dual Filing prosecution against a listed company and its director for providing false and misleading information
- Substantially concluded five cases before the Insider Dealing Tribunal
- Successfully prosecuted 76 entities for various offences, including a record high of nine market manipulators
- Concluded 99 disciplinary inquiries and took action against 88 licensees or concerned persons
- Referred 31 cases of fraud to the Police
- Concluded 553 investigations of which 394 were completed within 12 months

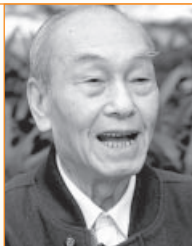
## [ This Chapter Is About ]

- Surveillance
  - Unusual price movements and trading
  - Market trading practices
  - Disclosure of interests
- Investigations
  - Listed companies
  - Market misconduct including insider dealing and market manipulation
  - Cold calling
  - FRR breaches
  - Failing to assist investigations
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  - Disclosure of interests
  - Others
- Discipline
  - Disciplinary priorities
  - Workload and penalty trends
  - Appeals
  - Settlements
- Co-operation with other law enforcement agencies and regulators

## Investors First



Lingnan University's Ms Lina Chau has taken a credit course on financial investing jointly offered by the SFC and the university.



Mr Chan Sum, 82, is a winner of a phone-in quiz in the Invest Wisely for Seniors radio programme.



Engineer Mr Leung Man Yan has shifted his investment focus from stocks to funds, as he is looking for a more stable return.

## What We Do

- Monitor the trading of Hong Kong's stock and derivative markets and inquire into irregularities;
- Inspect books and records of listed companies if impropriety is suspected;
- Enforce laws relating to the securities and futures industry, leveraged foreign exchange trading, and collective investment schemes;
- Discipline dishonest, incompetent and financially unstable regulated intermediaries;
- Report suspected civil market misconduct to the Financial Secretary;
- Suppress illegal or improper trading practices and irregularities relating to collective investment schemes and the provision of advice or other financial services;
- Enforce disclosure of interests of substantial shareholders, directors and chief executives of listed companies; and
- Co-operate with domestic and overseas regulatory bodies in local and overseas investigations.

## What We Did

In 2004-2005, we saw a considerable increase in the number of cases being dealt with under the SFO and more sanctions being imposed under the SFO as we concluded cases that predated 1 April 2003.

We continued to prioritise areas which would have the greatest impact on our statutory objectives and

our duty to protect investors. Our record achievements this year confirmed that approach. At the same time, we maintained high standards of forensic work and procedural fairness.

Our priorities for investigations were to combat corporate misgovernance, market misconduct and delinquent intermediaries. On discipline, our priorities were sponsors, investment advisers, fund managers and serious conflicts of interest.

## Surveillance

### ■ Unusual Price Movements and Trading

Our Surveillance Department is responsible for monitoring day-to-day trading in Hong Kong's securities and futures markets. With the help of sophisticated computer systems, we identify and inquire into unusual price and turnover movements.

In cases of suspected market manipulation, insider dealing or dissemination of false or misleading information, we obtain trading details from brokers to conduct preliminary assessments. We surf the Internet to detect possible unlicensed dealing, unauthorised advertising of investment services, or other abnormal financial activities. Our daily surveillance programme also actively monitors the media for reports of improper activities. Suspicious activities are reported to the Investigation Department.

Where we suspect there is a possible false or misleading announcement and if the situation warrants, we will recommend the suspension of trading in a listed company on the SEHK. During the year, we exercised this power twice. One of the stocks remains suspended while the other has resumed trading after making a clarification announcement.

## Enforcement

In addition, there were 280 other trading suspensions owing to unusual price or volume movements. Two of them were directed by HKEx because the management could not be contacted for clarification of potentially price sensitive matters. These matters are subject to further investigation. The other suspensions were requested by the companies concerned following inquiries by HKEx or the SFC. These suspensions were usually lifted on the day after the companies released news which might have an impact on their stocks, or statements that they were unaware of the reason for the unusual movements.

During the year, we conducted 142 inquiries into untoward share price and volume movements in which we sought trading records from brokers. On many occasions our early inquiries explained the untoward movements or stopped the potentially improper trading activities. Nevertheless, 40 cases were subject to full investigation.

### ■ Market Trading Practices

In early 2004, we investigated unusual trading activities relating to share placements of listed companies. We found that some placing agents might have acted inappropriately when testing market response to a pending placement. Specifics including the amount of money to be raised and the indicative price level of the placement shares were revealed to selected clients during trading hours, while the actual placing exercise commenced after the close of the market. This privileged information allowed the recipients to benefit in trading the concerned securities and created an unequal market. We inquired into eight such cases. Two cases are still under investigation. The rest were concluded with no further action. In May 2004, we issued a press

release reminding market practitioners of the importance of maintaining an equally informed market and to avoid passing potential insider information while conducting their placement activities.

2004-2005 witnessed an explosive growth in the level of activity in the derivative warrants market. We looked into allegations about possible market manipulative activities by issuers. While some complaints reflected a lack of understanding by retail investors about the characteristics of warrants, particularly those of an exotic nature, we identified cases where an abnormally high level of day trading activity by individuals did not appear to be driven by profit motives. This called into question whether these trades were to create a false appearance of active trading. In July 2004, the SFC reminded investors to exercise caution in choosing derivative warrants.

We also looked into the Macau concept stocks frenzy in the second half of 2004. We focused on market manipulation and false or misleading company announcements. We initiated 24 inquiries involving 23 listed companies. Most cases are still under consideration.

### ■ Disclosure of Interests

HKEx refers late filings of disclosure of interests to the SFC. From time to time, while conducting other inquiries, we may identify cases of failure to disclose. These breaches are assessed on a case-by-case basis. Where relevant information has been disclosed publicly, the transaction usually will not attract any further SFC action. Minor and first time offenders are usually warned. Serious cases may be prosecuted.

In the second year of implementing the SFO, both listed companies and investors had become more

familiar with the disclosure requirements. The number of late filings dropped from 6,608 in 2003-2004 to 4,185 last year. During the year, disclosure failures that warranted full investigation also dropped from 36 cases to 30 cases.

### Investigations

Last year, we continued 546 investigations from 2003-2004. Another 501 new cases were opened as a result of information from sources including the public, other law enforcement agencies, HKEx and foreign regulators. Out of these 1,047 cases handled, 553 were concluded and the remaining 494 were subject to continuing investigations, hearings or prosecutions.

#### ■ Listed Companies

We reported in 2003-2004 that we were considering seeking orders under section 214 of the SFO (including orders disqualifying directors) in two company investigations. We discontinued one case because of Police action against the company. Our action against the other is imminent. Meanwhile, we are taking legal advice on seeking section 214 orders in a case that came to light last year.

Altogether we investigated 23 cases involving listed companies in 2004-2005, including 11 cases carried forward. Five cases were referred to the Police for further investigation (one of which simultaneously under SFC investigation). As a result of one such referral the Police searched a listed company, Tungda Innovative Lighting Holdings Limited and its senior management, which the media widely reported. Three cases were referred to HKEx, and two were written off.

During the year, we successfully prosecuted a listed company and its director for providing false or misleading announcement to the public (Table 1). We have a similar matter before the Courts and are taking legal advice as to whether we have sufficient evidence to prosecute in another case.

Successful Prosecutions – Provision of False or Misleading Information

1  
Table

Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)	Costs of Investigation Awarded(\$)
1	Cai Yang Bo Huafeng Textile International Group Ltd	22.09.04 22.09.04	1 1	50,000 50,000	28,000
<b>Total: 2 entities</b>		<b>2</b>	<b>2</b>	<b>100,000</b>	<b>28,000</b>

#### ■ Market Misconduct

Our determination to combat market misconduct is evidenced by both the number of matters heard by the Insider Dealing Tribunal (IDT) and the number of successful market manipulation prosecutions during the year.

In addition to the cases we prosecuted, the Police Commercial Crime Bureau was successful in securing a three-month custodial sentence for a person found guilty in the District Court of manipulating Wing Lee Holdings Limited shares. This case was referred by the SFC to the Police.

In the coming year, the ICAC will be prosecuting parties involved in the alleged manipulation of Shanghai Land Holdings Limited shares. Our staff have provided significant assistance in terms of data analysis and will give expert evidence in the trial.

## Enforcement

### Insider Dealing

In 2004-2005, the IDT substantially completed five hearings relating to Firststone International Holdings Limited, Chinney Alliance Holdings Limited, HKCB Bank Holdings Company Limited/Lippo China Resources Limited/Lippo Limited, Gilbert Holdings Limited and Siu Fung Ceramics Holdings Limited. However, the final findings in respect of HKCB Bank/Lippo China Resources/Lippo and Gilbert are awaited and there are outstanding matters to be concluded in respect of Siu Fung Ceramics (Table 2).

In the Firststone inquiry, four persons were found to be insider dealers. They were ordered to pay penalties, disgorge profits and pay costs totalling \$16.1 million. They were banned from being directors of any listed company for two to five years. One of them appealed against the penalty and the date of appeal hearing will be fixed this year.

An insider dealer in the Chinney case was ordered to pay penalties etc totalling \$3.8 million and banned for four years. Rulings on the other two concluded cases are expected in the coming year.

In the Siu Fung inquiry, the IDT held that the company's former chairman and four related

persons had engaged in insider dealing. Penalties, profits disgorgement and costs amounting to \$250 million were imposed on four of the insiders.

In 2004-2005, the IDT commenced an additional two inquiries, namely Asian Orient Holdings Limited and Easy Concepts International Holdings Limited. These hearings continue. The hearing of four more inquiries might take place in the coming year.

We investigated 11 cases carried forward and three new cases. We referred two cases to the Financial Secretary for consideration of the appointment of an IDT. We concluded four cases with no further action and investigations continued in the remaining eight cases.

### Market Manipulation

We are encouraged by the successful prosecution of eight people and one company in the Courts for manipulating the shares of MUI Hong Kong Limited (Case 1 in Table 3), Fortuna International Holdings Limited (Case 2), Fujikon Industrial Holdings Limited (Case 3), Tern Properties Co Limited (Case 4), Tradeeasy Holdings Limited (Case 5) and Sino Technology Investment Limited (Case 6). The record nine convictions compared to seven in the previous year.

Penalty Ordered by IDT on Insiders

2  
Table

Case	Insider Dealers	Shares of Listed Company	Date of Judgement	Disgorgement of Profit (\$)	Penalty (\$)	Cost (\$)	Bar from Being a Director
1	Huang Xiao Jiang James	Firststone International Holdings Ltd	08.07.04	3,219,981.71	3,219,981.71	2,161,588.77	5 years
	Chiu Yuen Man*			379,647.89	2,371,341.41	1,080,794.39	3 years
	Chow Kar Chun Eddie			–	1,404,426.95	720,529.59	3 years
	Kwan Lai Sheung			687,846.56	687,846.56	720,529.59	2 years
	<b>4 entities</b>		<b>Total</b>	<b>4,287,476.16</b>	<b>7,683,596.63</b>	<b>4,683,442.34</b>	
2	Lee Siu Fung	Siu Fung Ceramics Holdings Ltd	08.11.04	69,870,530	139,741,060	9,185,356	5 years
	Chan Kwong Tat			–	13,925,337	2,296,339	1 year
	Lisa Lam Lai San*			1,910,297	1,910,297	2,296,339	1 year
	William Lam Chun Ming*			1,910,297	1,910,297	2,296,339	1 year
	Tai Hon Leung Henry*					to be ordered	
	<b>5 entities</b>		<b>Total</b>	<b>73,691,124</b>	<b>157,486,991</b>	<b>16,074,373</b>	
3	Lau Chung Yin	Chinney Alliance Holdings Ltd	24.12.04	1,318,486	700,000	1,800,000	4 years
				<b>1 entity</b>	<b>Total</b>	<b>1,318,486</b>	<b>700,000</b>
<b>Total: 10 entities</b>				<b>79,297,086.16</b>	<b>165,870,587.63</b>	<b>22,557,815.34</b>	

\* Under appeal

## Successful Prosecutions – Market Manipulation

3  
Table

Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)/Penalty	Costs of Investigation Awarded(\$)
1	Chung Man Keung	09.06.04	10	2-month imprisonment suspended for 2 years and a fine of \$20,000	21,959
2	Han Sze Chao Richard	28.07.04	1	25,000	29,276
	Super Glory International Ltd	28.07.04	1	25,000	
3	Wong Pui Ming	01.09.04	1	2-month imprisonment, suspended for 2 years and a fine of \$5,000	10,000
	Ho Sze Man	15.09.04	1	10,000	20,000
	Yuen Kim Shing	15.09.04	1	10,000	20,000
4	Chow Lung On	01.11.04	1	15,000	15,226
5	Leung Tung Wa	15.11.04	1	5,000	44,390
6	Wan Wai Chi	24.02.05	5	120 hours of community service	15,941
<b>Total: 9 entities</b>			<b>22</b>	<b>115,000</b>	<b>176,792</b>

We are confident that a comparable number of cases will be heard in 2005-2006. We have three cases awaiting trial or judgment and another five awaiting legal advice and clearance to prosecute. One of these cases relates to attempted manipulation of the pre-opening price of index futures.

All these offences took place before the introduction of the SFO. The SFO has introduced harsher penalties. It is also encouraging to note that the Magistrate in the Fujikon case warned one defendant that he would have been jailed if he had not pleaded guilty.

#### Market Misconduct Tribunal

The SFO introduced an alternative civil route, via a Market Misconduct Tribunal (MMT), to deal with all types of market misconduct including insider dealing. Legal advice is being sought on two cases where we think a referral to the MMT is warranted. Investigations have been completed in four others where a referral will also be considered.

Accordingly, we are optimistic that the MMT can commence hearing its first case in the coming year. Nevertheless, we will follow the criminal

route of prosecution where there is sufficient evidence and prosecution is in the public interest.

#### Cold Calling

Cold calling is prohibited so investors are not pressured into trading. Often clients recruited by such means complain of having been obliged to depend upon the advice of the Account Executive who persuaded them, on the basis of incomplete information, to open and lock more contracts than was necessary. We prosecuted three people for hawking of futures contracts (Table 4). Subject to legal advice, there may be six more prosecutions, and disciplinary actions.

## Successful Prosecutions – Hawking of Futures Contracts

4  
Table

Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)	Costs of Investigation Awarded(\$)
1	Shiu Yau Wah	21.04.04	1	5,000	10,000
2	Lam Shuk Kuen Mean	30.09.04	3	7,500	8,158
	Lau Chun Kwok	30.09.04	2	5,000	8,363
<b>Total: 3 entities</b>			<b>6</b>	<b>17,500</b>	<b>26,521</b>

## Enforcement

### ■ FRR Breaches

Four persons and four companies were prosecuted for Financial Resources Rules (FRR) related breaches (Table 5). They provided false or misleading information to the SFC or failed to notify the SFC of liquid capital deficiencies. Two persons were sentenced to suspended imprisonment.

Successful Prosecutions – FRR Breaches					
Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)/Penalty	Costs of Investigation Awarded(\$)
1	Pacific Pearl Securities Ltd	02.04.04	2	12,100	–
	Cheng Kwok Cheung	02.04.04	2	3-month imprisonment, suspended for 2 years	–
	Pacific Pearl Futures Ltd	02.04.04	1	16,000	–
	Yung Ki Cheong	02.04.04	2	2-month imprisonment, suspended for 1 year	81,747
2	Upbest Investment Co Ltd	14.06.04	5	25,000	59,213
	Choy Ye King Andy	14.06.04	3	6,000	–
3	Evergreen Securities Ltd	16.06.04	5	20,000	14,295
	Cheng Hok Wai	16.06.04	5	20,000	–
<b>Total: 8 entities</b>			<b>25</b>	<b>99,100</b>	<b>155,255</b>

### ■ Failing to Assist Investigations

Two persons were convicted of failing to co-operate with SFC investigations (Table 6). People hindering SFC investigations undermine our effort to curb illicit activities that threaten Hong Kong's markets. The SFC will not hesitate to prosecute these offenders.

Successful Prosecutions – Failing to Assist Investigations					
Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)	Costs of Investigation Awarded(\$)
1	Xu Li	08.09.04	4	40,000	3,000
2	Wan Wai Chi Katherine	30.09.04	3	30,000	12,296
<b>Total: 2 entities</b>			<b>7</b>	<b>70,000</b>	<b>15,296</b>

### ■ Unlicensed Activities

During the year, 12 people and two companies were prosecuted for different types of unlicensed activities, including aiding or abetting (Table 7).

Successful Prosecutions – Unlicensed Activities					
Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)	Costs of Investigation Awarded(\$)
<b>Unregistered Dealing in Margin Financing</b>					
1	Wong Chung Ling	06.04.04	1	12,000	12,560
<b>1 entity</b>			<b>1</b>	<b>12,000</b>	<b>12,560</b>
<b>Unregistered Dealing in Securities</b>					
1	Cheung Tak Shun Dickson	28.10.04	1	2,500	5,000
2	Chang Kit Sun Lama	12.11.04	1	2,500	10,700
<b>2 entities</b>			<b>2</b>	<b>5,000</b>	<b>15,700</b>
<b>Unregistered Investment or Corporate Finance Advising</b>					
1	CSF Consultancy Ltd	07.05.04	1	4,000	–
	Chan Wing Chuen Freeman	07.05.04	2	10,000	–
2	Chiang Chip Man Andrew	01.09.04	1	5,000	5,000
	Lai Dick Wai	01.09.04	1	5,000	5,000
3	Wong Lee Chun	10.11.04	1	3,000	12,601
4	Tsoi Leung Po	06.01.05	1	2,000	2,540
5	MCC Capital Consulting Ltd	10.03.05	1	5,000	13,131
<b>7 entities</b>			<b>8</b>	<b>34,000</b>	<b>38,272</b>
<b>Unlicensed Forex Trader</b>					
1	Yip Sheung Chi	01.09.04	1	8,000	10,000
2	Tsang Wai Lin	13.12.04	2	60,000	–
<b>2 entities</b>			<b>3</b>	<b>68,000</b>	<b>10,000</b>
<b>Unauthorised Advertisement</b>					
1	Ko Wai Yu	14.10.04	2	10,000	4,500
2	Li Ping Hei Benjamin	10.11.04	1	5,000	12,601
3	Tsoi Leung Po	06.01.05	7	14,000	17,785
<b>3 entities</b>			<b>10</b>	<b>29,000</b>	<b>34,886</b>
<b>Total: 14 entities</b>			<b>24</b>	<b>148,000</b>	<b>111,418</b>

## ■ Disclosure of Interests

In 2004-2005, 17 people and 13 companies were prosecuted for material breaches (Table 8). We issued 154 warning letters for minor and inadvertent breaches.

Successful Prosecutions –  
Disclosure of Interests

8  
Table

Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)	Costs of Investigation Awarded(\$)
1	Value Partner Ltd	07.04.04	4	16,000	29,225
2	Deng Chi Yuan	07.04.04	11	55,000	6,967
3	Leung Kin Man Kenny	23.06.04	2	5,000	10,000
4	Page Louis	23.06.04	2	5,000	6,542
5	Mong Man Wai William	30.08.04	2	5,000	13,578
6	Cheung Choi Chuen	01.09.04	2	7,000	3,500
7	Choo Yeow Ming Summers Overseas Ltd	01.09.04 01.09.04	4 4	4,000 4,000	13,339
8	Ng Kwok Kuen	22.09.04	6	15,000	8,000
9	Yeung Ka Sing Carson	27.09.04	14	43,000	7,398
10	Lee Shi Tat Caric	30.09.04	2	3,000	8,112
11	South China Holdings Ltd	07.10.04	4	8,000	12,991
	South China Industries Ltd	07.10.04	2	4,000	–
	South China Industries (BVI) Ltd	07.10.04	2	4,000	–
	Wah Sing International Holdings Ltd	07.10.04	2	4,000	–
	Man Wah Trading Ltd	07.10.04	4	8,000	–
12	Wong Man Hung Patrick	14.10.04	4	10,000	5,000
13	Lo Wai Shing Felix	28.10.04	1	5,000	38,177
14	Tsui Muk Lan	28.10.04	9	18,000	16,033
15	Sky Victory Ltd	09.11.04	1	2,000	–
	Siu Wai Keung	09.11.04	2	4,000	10,000
16	SinoPac Capital Ltd	25.11.04	6	12,000	10,000
17	Kuk Po Shun	25.11.04	4	10,000	4,500
18	Shu Kwan Long	16.12.04	2	4,000	9,500
19	Modern World Resources Ltd	24.02.05	4	10,000	3,500
20	Leung King Keung	03.03.05	2	4,000	10,821
	Lee Wing Ngai	03.03.05	8	22,000	17,094
21	Linefan Technology Holdings Ltd	10.03.05	2	2,000	4,479
22	China Conservational Power Holdings Ltd	24.03.05	12	9,000	9,765
23	Montgomery Properties Holding Ltd	31.03.05	3	9,000	21,000
<b>Total: 30 entities</b>			<b>127</b>	<b>311,000</b>	<b>279,521</b>

## ■ Others

A licensed corporation and its responsible director were prosecuted for pledging clients' securities without their approval. A person and a company were prosecuted for unauthorised investment promotion and three persons for short selling. Three persons were prosecuted for providing false or misleading representation in applications for SFC licences, and a company for issuing share subscription forms without a prospectus (Table 9).

Successful Prosecutions – Others

9  
Table

Case	Defendants	Date of Conviction	No. of Summonses Involved	Fine (\$)/ Penalty	Costs of Investigation Awarded(\$)
<b>Pledging Clients' Securities without Obtaining Clients' Prior Approval</b>					
1	Victory Securities Co Ltd	31.03.05	2	5,000	5,547
2	Kou Kuen Katherine	31.03.05	2	5,000	5,546
<b>2 entities</b>			<b>4</b>	<b>10,000</b>	<b>11,093</b>
<b>Breach of Protection of Investors Ordinance</b>					
1	CSF Consultancy Ltd	07.05.04	1	6,000	–
	Chan Wing Chuen Freeman	07.05.04	1	80 hours of community service	–
<b>2 entities</b>			<b>2</b>	<b>6,000</b>	
<b>Short Selling</b>					
1	Wong Chi Wai	25.08.04	9	54,000	10,560
2	Suen Chi Keung	15.09.04	15	75,000	12,917
3	Fung Wing Kwong	10.03.05	2	10,000	9,152
<b>3 entities</b>			<b>26</b>	<b>139,000</b>	<b>32,629</b>
<b>Provision of False or Misleading Representations in application for an SFC license</b>					
1	Wong Chi Cheong	12.05.04	1	5,000	5,000
2	Yuen Pak Kan	03.02.05	1	10,000	9,000
3	He Zhao Danny	03.02.05	1	10,000	10,000
<b>3 entities</b>			<b>3</b>	<b>25,000</b>	<b>24,000</b>
<b>Issue Application Forms for Shares in a Company without a Prospectus</b>					
1	Delta Asia Securities Ltd	03.02.05	1	15,000	8,000
<b>1 entity</b>			<b>1</b>	<b>15,000</b>	<b>8,000</b>
<b>Total: 11 entities</b>			<b>36</b>	<b>195,000</b>	<b>75,722</b>

## Enforcement

During the year, the SFC successfully prosecuted 76 entities in total. There were six acquittals after trial.

### Discipline

Intermediaries play a crucial role in Hong Kong's financial markets. It is essential that they are honest, efficient and financially sound. We take tough disciplinary actions against those who put their clients' interests and market integrity at risk.

#### ■ Disciplinary Priorities

Last year we made sponsors, investment advisers, fund managers and serious conflicts of interest our priorities. We achieved notable results in each area with some record outcomes.

Sponsors of listed companies are gatekeepers who help ensure that only suitable companies are listed and that the disclosure of information to investors is adequate. Recent failures by listed companies focused public attention on the role of sponsors.

During the year, the SFC concluded action against ICEA Capital Limited, the sponsor of Euro Asia Agricultural (Holdings) Company Limited. In a landmark settlement, ICEA paid \$30 million without admission of liability, and agreed to an internal control review.

In the first joint disciplinary action with HKEx against a sponsor, the SFC settled an action against Oriental Patron Asia Limited and Mr Rabo Leung Chin Sing with each agreeing not to act as sponsors for five and nine months respectively.

Two more cases against sponsors, including one significant action, will likely be concluded in 2005-2006.

Investment advisers play an increasingly important role in helping investors manage their wealth. However, recent events suggest that some are not discharging their role competently.

We settled disciplinary action against Towry Law (Asia) HK Limited with Towry Law promising to make record \$255 million ex-gratia payments to clients whom they had advised to invest in two failed hedge funds. We also reprimanded Towry Law. We concluded a settlement with another investment adviser for mis-selling mutual funds, which resulted in a three-year suspension effective on 15 April 2005.

Fund managers help channel investors' savings, providing diversified investment opportunities as an alternative to direct investment in equities and other products. They are entrusted with vast sums of money. We have increasingly focused on fund managers' compliance failings in line with global attention on the issue.

We reprimanded Asia Insurance (Pensions Fund) Limited and Bank Consortium Trust Company Limited for failures to abide by fund investment restrictions and to monitor compliance with those restrictions, respectively. We suspended the licence of a responsible officer of Asia Insurance, Mr Wong Kok Ho, for four weeks.

We also settled allegations against fund manager First State Investments (Hong Kong) Limited of compliance failings that might have facilitated late

trading. First State agreed to make ex-gratia payments to the funds concerned and waived fees without admission of liability. These were relatively technical breaches and we warned the industry that we would take harsher action in more serious cases.

Licensees occupy a position of trust with their clients. We expect them to avoid conflicts of interest and put the interests of their clients first in the event of a conflict. Some licensees ignored these cardinal rules.

We settled with Ms Irene So Wai Yin, who surrendered her licence for five years. She had failed to disclose enough information to clients when borrowing from them for her firm's parent company, which was in financial trouble. We suspended the licence of Mr Eric Wong Wing Fai for 18 months for front-running research reports he issued. This was the first such enforcement action in Hong Kong. We will take action in a similar case this year.

We have sought to use our resources more efficiently by exercising regulatory balance, taking a tougher approach towards more serious cases and a flexible approach towards less serious ones.

We have done this in three ways. First, we have been more flexible in settlements (see discussion later in this chapter). Second, we issued private warnings, where we thought that the public interest did not demand formal punishment, so we could show a degree of leniency while still sending a message that conduct was wrong. Lastly, we have begun to meet with licensees in appropriate cases where penalties are fairly standard, before

we decide to take formal disciplinary action. We hope to dispose of these cases more quickly by encouraging rational settlement negotiations where the parameters for settlement are more predictable for us and defendants.

### ■ Workload and Penalty Trends

Even in the face of a record number of appeals and some very complex cases, we maintained the existing case load.

In 2004-2005, we conducted 209 disciplinary inquiries. Of these, we concluded 99 cases, disciplined 78 entities. We entered into settlements without formal sanctions with 10 licensees, of which four were settled with voluntary payments. We also took disciplinary actions against 28 licensees which were eventually concluded with no formal sanction imposed, although 15 of them received private warnings.

In addition, we started disciplinary action against four deemed licensees who left their firms before the action ended. Under the SFO transitional provisions, these people lost their licences and we have no jurisdiction over them. However, they must answer our concerns and satisfy us that they are fit and proper if they re-apply for a licence.

We continued the previous year's trend to impose higher penalties, and we increasingly used the new sanctions available under the SFO, in particular fines. We suspended more licensees and suspensions were generally longer.

We revoked two licensees, one of them we also banned him for 10 years. We banned another licensee for life. We accepted the surrender of a

## Enforcement

licence and an undertaking not to re-apply for five years. We suspended 37 licences. We reprimanded and fined nine licensees amounts between \$14,000 and \$375,000. We reprimanded 29 licensees and privately warned 48, including the 15 mentioned above and those whom we warned without initiating formal disciplinary inquiries. Table 10 highlights the most significant actions.

We will keep the level of penalties under review to ensure that they secure appropriate regulatory outcomes by remaining proportionate, protective and dissuasive.

### ■ Appeals

During the year, the Securities and Futures Appeals Tribunal (SFAT) received a record 18 appeals against SFC disciplinary actions and five appeals were carried forward from last year. The SFAT heard eight of these cases. Two appeals were withdrawn by the appellant and seven appeals were settled before a full hearing.

Of the eight cases decided by the SFAT, it dismissed three appeals. In five appeals, the SFAT accepted our findings of fact but reduced the penalties, substantially in three appeals and only slightly in the other two.

At the end of the year, we awaited the decision in one appeal and five appeals were awaiting full hearing, though four of these appeals were related and to be heard together. Among the appeal settlements, two were effective on 15 April 2005.

In total, the SFAT upheld our decision to discipline eight licensees. The withdrawal of two appeals and settlement of seven with acceptable settlements suggest that we are getting our disciplinary decisions generally right. Out of the 15 appeals decided or settled, there were substantial

penalty reductions in only three cases. As the majority of appeals were decided by the presiding judge and independent lay members, the results indicate a satisfactory degree of outside acceptance of our findings of fact and penalties.

The SFAT was designed to decide appeals quickly and is doing so. Its predecessor, the Securities and Futures Appeals Panel, never heard this number of appeals or decided them so fast. Given the SFAT's speed of decision and the simplicity of procedures, it is proving an inexpensive means of challenging decisions, with individuals appearing unrepresented in a number of appeals, but still capably arguing their cases with the SFAT's assistance.

The SFAT gives useful guidance on how it decides appeals. In two appeals, it stated that the SFC had flexibility to adjust penalties to suit changing circumstances and should not be bound by previous penalties which were too low by present standards. The SFAT also confirmed that SFC disciplinary decisions should have a deterrent effect and that it would give less weight to mitigating factors than was the case in criminal sentencing. Lastly, the SFAT indicated that repeat offenders should be punished more harshly.

During the year, some commentators expressed doubt over the SFAT's function as an effective check and balance on SFC's disciplinary powers, in part because they suggested that the SFAT only reviewed the SFC's procedure and not the merits of cases. They suggested a need for greater industry participation in the disciplinary process.

A review of the SFAT's decisions should dispel these notions. The SFAT is reviewing the merits of decisions. It has, on one occasion, held a full *de novo* hearing (i.e. it heard the case anew). It is also

## Significant Actions

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Table

Case	Registrants	Date of Action	Misconduct	Action/ Settlement/ SFAT Decision
1	Raphael Blot	13.05.04	Alleged use of schemes to circumvent the then placing requirements of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Ltd.	SFC originally decided to suspend Blot for six months. Blot appealed to the SFAT and was granted leave for judicial review. The proceedings were withdrawn as part of a settlement that Blot consented to pay the SFC, on a without admission of liability basis, \$750,000. The SFC withdrew its decision to suspend Blot.
2	Chow Yuk Wah	21.05.04	Pledging clients' shares to a bank for personal loan without clients' consent; sold the shares and misappropriated the sales proceeds.	Revocation.
3	Wong Wing Fai Eric	02.08.04	Failure to avoid a conflict of interests and breaching staff dealing policy.	SFAT upheld the SFC's decision for a 18-month suspension.
4	Towry Law (Asia) HK Ltd	17.08.04	Failed to conduct sufficient due diligence into the two hedge funds managed by third parties; sold the two funds to clients whose investment objectives and risk tolerance did not match with the two funds; failed to conduct proper enquiries into circumstances surrounding the two funds which indicated problems; failed to advise clients when the funds had problems.	Severe reprimand and Towry Law, without admission of liability, agreed to make ex-gratia payments to clients amounted to 80% – 90% of the capital invested, which totalling \$255 million.
5	Cheung Kwok Chiu Kris	10.11.04	Without exercising due skill, care and diligence, mishandled clients' assets and lied to the SFC.	Ban for life from the industry.
6	Oriental Patron Asia Ltd	17.12.04	Withholding material information from HKEx when acting as sponsor to a listing applicant to the Growth Enterprise Market; failed to properly guide and advise the listing applicant with due care and skill.	Removed from HKEx's approved list of sponsors under the GEM subject to certain exceptions and agreed not to act as a sponsor under the Main Board for five months.*
7	Leung Chin Sing Rabo (Principal Supervisor of Oriental Patron)	17.12.04	ditto	Voluntarily withdrew from acting as a Principal Supervisor of Oriental Patron and agreed not to perform or carry out any activities in relation to any GEM or Main Board listing applicant or listed issuer for nine months.*
8	Tong On Jimmy	23.12.04	Charged as much as \$33 million worth of cash clients' securities to a bank as security for an overdraft facility; gave the SFC documents containing inaccurate information during investigation.	SFC originally decided to revoke Tong. Tong appealed to the SFAT. The proceedings were withdrawn as part of a settlement that Tong ceased business, surrendered his license and undertook never to re-apply for a license.
9	ICEA Capital Ltd	27.01.05	Allegedly not exercising due skill, care and diligence in the course of performing its duties as the sponsor for the listing of Euro Asia Agricultural (Holdings) Co Ltd.	A payment of \$30 million without admission of liability.
10	Lau Hing Hung Joie	28.01.05	Impersonating a client to open an account; conducted trading without the client's knowledge and consent; lied to the SFC.	SFAT upheld the SFC's decision for revocation and a 10-year ban from the industry.
11	So Wai Ying Irene	01.03.05	Failing to avoid a conflict of interests and did not act in the best interests of her clients.	SFC originally decided to revoke So. So appealed to the SFAT. The proceedings were withdrawn as part of a settlement that So surrendered her license and undertook not to re-apply for five years.

\* Joint action between the HKEx and the SFC

## Enforcement

willing to interfere with SFC penalties and findings. In most cases, the SFAT sits with market representation; it can sit with the judge alone only if the appellant agrees. The SFAT is acting as an effective check and balance on the SFC, as intended.

To further enhance transparency, in September 2004, we issued a plain language booklet on the disciplinary process. The booklet, *Disciplinary Proceedings at a Glance*, is given to defendants and is also available on our website and at the SFC.

### ■ Settlements

During the year, we settled with four licensees with voluntary payments to the Government in exchange for suspensions. The amounts were \$40,000, \$195,000, \$750,000 and \$30 million. In two of these settlements, the licensee did not admit fault.

Separately, we settled with two licensees making ex-gratia payments to investors affected by their alleged conduct without the licensees admitting fault.

Settlements are common in many markets. However, there was local concern about the practice.

It is worth noting that we have always settled disciplinary actions. We have settled without admissions of fault before and also settled with non-statutory disciplinary outcomes, such as compensation, surrender of licences, undertakings not to engage in certain conduct or promises to keep certain undertakings. None of these settlements were controversial.

The SFO made two relevant changes to our disciplinary powers. It gave us the power to fine and an express power to settle, including by taking any appropriate actions as long as we believe it is in the public interest to do so. There may be cases where suspension is too harsh while a reprimand is too light. In many of the cases before the SFO, we had to propose a suspension or other penalty, even though we think a fine would have been ideal.

We have used the new powers to give penalty flexibility to defendants in pre-SFO cases where a fine would have been preferred to suspension. We settled and they made voluntary payments. These settlements bridge the gap between the old law and the SFO, nothing more.

We must satisfy ourselves that it is in the public interest before we settle. Only senior SFC officers can decide to settle and they must do so in accordance with internal procedures. We will not settle with a payment if dishonesty is involved or we consider the licensee poses a continuing risk to the public such that a suspension is more appropriate.

In all cases, the payment that we have agreed upon is proportionate to the initially proposed suspension taking into account the circumstances of the case. We only agree to monetary penalties if we believe they achieve the same protective and deterrent effect as the result we would be able to achieve in the event of the licensees appealing against our proposed actions. The practice will become less common as the number of transitional pre-SFO cases dwindles.

## Co-operation with Other Law Enforcement Agencies and Regulators

We maintain close contact with other local enforcement agencies and our Mainland and overseas counterparts to tackle international financial crime and misconduct.

During the year, we referred 31 cases to the Police for further action. We continued to work closely with the Commercial Crime Bureau and the ICAC in cases involving corporate fraud,

corruption and market manipulation. Furthermore, two officers from the ICAC were seconded to the Division for three months to exchange expertise and share experiences. Similar secondment will take place in the coming year.

We also place emphasis on international regulatory co-operation such as information sharing and cross-border investigation. The SFC has 34 bilateral or multilateral co-operation arrangements with regulatory bodies around the world. We are one of the signatories to the IOSCO Multilateral Memorandum of Understanding (MMOU).

## Regulation of Mainland Corporations



In recent years, there has been an influx of Mainland corporations seeking to list on the Hong Kong market. This has required us to step up our working relationship with the CSRC to deal with cross-border enforcement issues involving Hong Kong listed companies based in the Mainland. The CSRC has been willing to help us to the extent it can.

However, the SFC cannot exercise its statutory power under the SFO over entities or individuals in the Mainland. We are forced to rely on voluntary co-operation from witnesses, suspects and companies located in the Mainland. This represents a significant impediment to effective enforcement of the law.

The SFC has drawn this issue to the attention of the CSRC and the HKSAR Government. In addition, we are working closely with HKEx in tackling the problem by strengthening the regulation of listing and sponsors, and promoting disclosure and transparency.