

# Cross-Border Regulatory Co-operation

In a world of fast moving global markets and rapid technological advances, it is essential for regulators to be in close contact with their counterparts in other jurisdictions. During the year the SFC had wide ranging discussions with other regulators. Areas covered included improving regulation on the Growth Enterprise Market (GEM), investigating market manipulation and policing Internet trading. The SFC now has 32 co-operation arrangements and 11 informal arrangements with regulatory bodies around the world. Discussions are taking place about establishing formal co-operation arrangements with two additional jurisdictions, one in Europe and one in Asia.

As well as sharing information, the SFC takes an active part in the International Organization of Securities Commissions (IOSCO) and, in particular, the work of the IOSCO Asia Pacific Regional Committee (APRC). The APRC's annual meeting in Seoul, South Korea on 20-21 October 1999 covered recent developments in members' markets as well as enforcement-related issues.

The first training course for securities regulators organized by the Enforcement Institute of the APRC was held in Seoul in November 1999. Members of the SFC's Enforcement Division made presentations on market surveillance, investigation of insider dealing and market manipulation, and the conduct of disciplinary proceedings. The SFC also welcomed delegations from the Shanghai and the Shenzhen Stock Exchanges and demonstrated



Visit to NYSE

its computerized surveillance system to a delegation from the Malaysian Securities Commission.

## Ongoing Co-operation

With the expected listing of mainland companies on the GEM, the China Securities Regulatory Commission (CSRC) and the SFC, on 14 October 1999, signed Letters of Exchange regarding regulatory co-operation between the CSRC and the SFC. The letters re-affirmed the relevant provisions of the Memorandum of Regulatory Co-operation (MORC) entered into on 19 June 1993 and established additional arrangements for the GEM. These include providing assistance on supervision, inspection and investigation in order to better enforce the regulation of the GEM.

To assist overseas regulators that meet statutory criteria, the SFC has powers to disclose confidential information and provide investigatory assistance. In turn, the SFC seeks information and assistance from overseas regulatory authorities. A breakdown of such requests is summarized below.

Table 1

Requests for Regulatory Co-operation		
	Incoming	Outgoing
Enforcement-related requests for information	40	3
Enforcement-related requests for investigatory assistance	18	14
Licensing-related requests for information	257	776
<b>Total</b>	<b>315</b>	<b>793</b>

An example of successful regulatory co-operation was the action taken by the US Securities and Exchange Commission (US SEC) against a Hong Kong resident suspected of insider dealing on 21-22 June 1999 in the shares of Omnipoint Corporation, a company listed on the New York Stock Exchange (NYSE). On 2 July 1999, the SFC received a request from US SEC for help in obtaining records from a local brokerage. The assistance given enabled the US SEC to commence civil proceedings against the Hong Kong resident who, on 26 July 1999, settled

the civil action without admitting or denying the allegation. The settlement included the payment by the Hong Kong resident of some US\$2 million, being the disgorgement of profits and a pecuniary penalty.

### **Joint Inspections**

Intermediaries Supervision Department inspection staff joined with examiners from the US SEC and the UK Financial Services Authority to conduct a co-ordinated inspection of a US-based fund management group in November 1999. This is the third of its kind since the programme was launched in 1997. Findings were collated to identify any deficiencies in the areas of management control, risk management and information technology systems from a global perspective and to identify gaps in regulatory compliance.

Following the 1998 inspections by the Intermediaries Supervision Department of Taiwan branches of securities dealers registered in Hong Kong, representatives from the Taiwan Securities and Futures Commission visited selected securities dealers with Taiwanese ownership in September 1999. The Intermediaries Supervision Department accompanied them on these visits.

### **Work with IOSCO**

The SFC is a member of the IOSCO Technical Committee and an active participant in its working groups and task forces.

### **IOSCO Objectives and Principles of Securities Regulation**

The SFC chairs the IOSCO Committee responsible for continuing work on the implementation of the IOSCO Objectives and Principles of Securities Regulation.

The Committee's two-part mandate requires that it:

- ◆ develops implementation and assessment methodologies for the IOSCO Objectives and Principles; and
- ◆ offers assistance to the international financial institutions in their use of the financial Objectives and Principles.

Committee membership includes 20 other IOSCO members drawn from all regions and from both developed and emerging markets. The World Bank, IMF, OECD and the regional development banks are also members of the Committee.

### **Internet Task Force**

IOSCO has established a special task force to consider the regulatory implications of the provision of financial services and the offering of investments over the Internet. Hong Kong is a member of the Task Force. The Task Force will examine the balance between facilitation of business via the Internet and effective regulation. We also expect to share with other regulators strategies for facilitating issues through the Internet without compromising investor protection.

### **Multinational Disclosure and Accounting**

For most of the 1990s the principal goal of Working Party 1 (WP1) has been the establishment of a body of financial accounting standards that IOSCO can endorse as suitable for international equity offerings. By 31 December 1999 the International Accounting Standards Committee (IASC) had issued new or revised accounting standards on all topics previously identified by WP1 as necessary for a comprehensive financial reporting framework. WP1's work of reviewing the IASC's standards is nearly complete and it is hoped that IOSCO's Technical Committee will be able to endorse the use of these standards for cross-border listings at the time of its annual meeting in May.

### **Regulation of Secondary Markets**

This was a year of achievements for Working Party 2 (WP2) and the SFC continued its periodic reporting to WP2 on the preparatory work done by and the readiness of the Hong Kong market in relation to the Y2K rollover.

WP2 submitted a paper to the Hedge Fund Task Force established by the IOSCO Technical Committee for its consideration regarding the advisability and feasibility of imposing requirements directly on the highly-leveraged institutions to disclose information relating to their activities.

WP2 also produced guidelines to assist and encourage member jurisdictions to implement and maintain effective market oversight programmes.

A survey was conducted to identify any need to revise the existing IOSCO Principles for Screen Based Derivatives Markets in the light of the growth of cross-border trading and remote access.

A paper entitled “*Securities Lending Transactions: Market Development and Implications*” was produced in July 1999 with the joint efforts of the Committee Payment and Settlement Systems (CPSS) and WP2 (SFC staff represented in the drafting team). The paper discussed the implications of securities lending activities for market participants and regulators. Another task force between the two groups was formed in late 1999 to revise recommendations issued by the Group of Thirty in 1989 on international standards for clearing and settlement. The revision is expected to be completed by December 2000.

### **Regulation of Market Intermediaries**

During the year Working Party 3 (WP3) started to analyze operational and credit risks and to assess the feasibility of developing appropriate capital treatment of such risks. In addition, WP3 studied the Basle consultative paper on the new capital adequacy framework for banks and its comments were incorporated in the overall IOSCO’s response.

### **Enforcement and Exchange of Information**

During the year Working Party 4 (WP4) concluded a report on market manipulation and how to identify and prove it. It is intended that the report be published subject to the approval by the Technical Committee.

WP4’s report on co-operation between regulators and law enforcement authorities was endorsed by the Technical Committee in October 1999 for internal use by members. This provides details of members’ experiences of co-operation with law enforcement authorities in their respective jurisdictions.

Upon the conclusion of these two reports, WP4 was given the new mandate for examining the issues associated with joint or parallel investigations. Under the mandate, a survey will be conducted to identify potential issues that may arise in parallel or joint investigations and to identify methods to synchronize enforcement action.

A revamp of the SFC’s daily monitoring of the Internet market took place following discussions in WP4. These covered members’ approaches and experience on the surveillance of the Internet as well as the investigation and prosecution of illegal activities perpetrated through the Internet.

### **Investment Management**

Following on work from last year, the discussion paper on “*Regulatory Approaches to the Valuation of Collective Investment Schemes (CIS) and Pricing of CIS Interests*” prepared by the Commission was published by IOSCO in May 1999. During the year Working Party 5 (WP5) also considered two discussion papers arising from the survey on “*Conflicts of Interests of CIS Operators*” and “*Delegation of Functions by CIS Operators*” respectively. The “*Conflicts of Interests of CIS Operators*” paper was finalized at the WP5 meeting in February in London with a view to seeking the Technical Committee’s approval for publication.

With the growing role of education in improving investor protection and given the increasing popularity of collective investment scheme as an investment vehicle for retail investors, WP5 had sought the agreement of the Technical Committee to a mandate to explore the use of investor education programmes to pursue regulatory objectives.