

Supervision & Enforcement 5th Pan Asian Regulatory Summit

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Opening

Thank you for the chance to set the scene for this afternoon's panel discussion.

I want to touch on two key areas: firstly, cross-border regulation, especially enforcement and secondly, cross-boundary enforcement in the proposed Shanghai-Hong Kong Stock Connect scheme. Both issues raise important challenges for Hong Kong as a global market. And I will say a few words about sanctions and remedies, given the reference to section 213 of the Securities and Futures Ordinance in your agenda.

The New Black

Following the post-financial crisis, cross-border enforcement became the 'new (and ubiquitous) black'. And the 'new black's' calling card was the multi-lateral MOU (MMOU) between regulators (now with over 100 signatories).

The MMOU is an agreement between regulators who have the means and the will to assist one another to fight financial crime. Entry is not automatic. Members need to prove their worth and capability through a testing screening process. And once accepted as a member, the demands are equally rigorous. As they should be.

The MMOU operates in a simple way. A regulator needing assistance sends a written request to another regulator (the receiving regulator) who is committed to providing the assistance that has been requested.

This simple mechanism – perhaps a little binary - has flourished and created a strong dynamic of mutual dependence between regulators, especially those carrying global burdens.

And by and large, it has created two kinds of regulators: those that could be described as net recipients of requests for assistance i.e. exporters of evidence and those who are net seekers of assistance i.e. net importers of evidence.

International financial centres – like HK, Singapore, London and New York - are more likely to be net recipients of requests for help, reflecting the intensity of activity inside their markets that originates from other parts of the world. This tendency is corroborated by experience.

More parochial or domestic markets, on the other hand, are more likely to require assistance, often from international financial centres, like Hong Kong, reflecting the intensity of financial activity affecting them that originates outside their markets. This is also borne out by experience.



Some Observations

The MMOU has been in existence for 12 years and the bulk of its worth has been realized since 2008. This experience identifies some trends and permits some observations:

- US and Hong Kong have moved away from a net balance of requests for assistance – what I call a ‘balance of trade’ position - to a steady state in which Hong Kong receives more requests from US authorities than it sends. In other words, Hong Kong has become a net exporter of forensic evidence to the US, reflecting perhaps volumes of business in the US with a Hong Kong source or connection or an increased inquisitiveness on the part of US authorities in this part of the world.
- overall, the volume of exchanges with the UK has reduced and the new steady state is, by and large, a ‘balance of trade’ position with overall numbers trending lower than those with the rest of Europe or North America or Asia.
- the volume of requests to and from Hong Kong but within Asia has increased dramatically as a percentage of total requests involving Hong Kong whilst the overall global numbers have increased as well. This appears to reflect a growing connectivity within Asia, especially between Hong Kong and Singapore, Japan, Malaysia, Australia and South Korea.
- the volume of information exchanges within Asia *in toto* are substantially greater than those between Asia and Europe including London – a position that I do not think existed a few years ago – reflecting the previous trend in a different way.

These MMOU numbers, of course, do not reflect our own exchanges with mainland China. These exchanges are governed by a different, bi-lateral arrangement. These numbers have also shot up over the last few years but they remain, for fairly obvious reasons, one directional: Hong Kong is a net requester of assistance and so a net importer of evidence from the Mainland, by some way. I will return to sharing information with our Mainland counterparts in a moment.

Another New Black

Regulators can be a little like magnets with north and south poles that repel or attract. The enforcement arms of regulators tend to be the bits that attract most readily and so the MMOU has been successful in harnessing the natural respect and regard that investigators around the world have for each other’s work and for one another.

The success of the MMOU – and I think, as a first step in giving regulators the chance to attack misconduct that otherwise could not be tackled, the MMOU has been very successful - has given birth to another new black. By creating the capacity for members to investigate on one another’s behalf and to share the product of those investigations, the MMOU has enlivened the long arm of many regulators and law enforcement agencies leading to the development and growth of cross-border enforcement.

While the MMOU has created the means for these long arms to operate, there remain some difficult consequential questions and problems including:



- the risk of inconsistent approaches as to whether multiple penal proceedings in different jurisdictions gives rise to double jeopardy. In some places, for example, double jeopardy will apply to multiple proceedings involving the same circumstances but it will not bar multiple proceedings by different sovereigns; in others, it does and it will.
- the consequential risk as to whether providing assistance to another agency to bring proceedings relating to the same matters that may be the subject of action in the first jurisdiction involves any abuse of process in either place.
- the use of compelled evidence from one jurisdiction in proceedings where such use may be barred either wholly or in proceedings of that kind under the law of the first jurisdiction.
- the absence of any protocol or process for the conduct of joint investigations by agencies from different jurisdictions.

In short the MMOU has been highly successful at creating the mechanism for bi-lateral exchanges of information that would otherwise not be available to regulators. It has done so in a way that has been essential in creating a *quid pro quo* dynamic of mutual dependence between regulators. In other words, to receive information from another jurisdiction, you need to rely upon the performance of another regulator who is depending on you to perform the same obligation for it in return.

But the MMOU does not address all the consequential issues of coordination and decision-making when cross-border misconduct is actionable in one or more places.

Stock Connect

This brings me to Shanghai-Hong Kong Stock Connect.

For those who may not be aware, this is the scheme announced earlier this year, as a pilot, to permit trading via Hong Kong on the Shanghai Stock Exchange and for Mainland traders to trade directly on the Stock Exchange of Hong Kong. Together with the China Securities Regulatory Commission (CSRC), the Shanghai Stock Exchange, China Clear and the Hong Kong Stock Exchange, the SFC has completed all the regulatory work necessary to enable Stock Connect, as it is known, to commence. The SFC is now in a state of operational readiness.

As mentioned, Hong Kong is a net importer of evidence and information from the Mainland. But this will change under Stock Connect - both regulators will become mutually dependent on one another as the flow, for the first time, will become two-way, which in turn, will help to guarantee performance.

The new working arrangements will be governed by what we call the enhanced MOU which is now published on our website.

One of the most important features of the enhanced MOU is that it does not only commit the SFC and the CSRC to provide assistance to one another, it also provides a framework for coordinated activity and decision-making, addressing some of the consequential risks that are not currently addressed in the MMOU. The enhanced MOU is a concerted game plan for joint work, setting a new benchmark for regulatory cooperation, covering not only investigations but also consequential enforcement proceedings, including:



- obligations for unilateral sharing of alerts about potential or suspected wrongdoing in either the Hong Kong or Shanghai stock markets;
- a mechanism for joint investigations to avoid duplicated work and maximum efficiency; and
- complementary enforcement action:
 - where there is wrongdoing in both jurisdictions (avoiding double jeopardy and abuse of process risks); and
 - to protect the investing public of both the Mainland and Hong Kong, including actions that may be necessary to provide financial redress or compensation to affected investors.

In this way, the enhanced MOU not only provides for the kind of two way exchanges of information that occur under the MMOU, it also provides a stronger platform for the initiation of action by one or both regulators and for coordination and joint effort and for decision-making in relation to consequential action. These are unique and novel developments firsts for a regulatory MOU of this kind.

Underscoring the provision of alerts is a mechanism for the flow of client and order data for surveillance purposes to the SFC's market surveillance team and vice versa. Again, this is a unique development which will ensure there is transparency to the investment flows in both Hong Kong and Shanghai markets.

Through these initiatives, we have broken new ground and established innovative and robust mechanisms to work together for the protection of both Hong Kong and Shanghai markets under this unique and exciting project, the Shanghai-Hong Kong Stock Connect.

Sanctions and Remedies

Vindicating public rights and obligations as well as dealing with the consequences of breaches remains at the heart of our enforcement strategy.

What this means in practice is that deterrent outcomes remain a priority for us here in Hong Kong and, I think, for most regulators. But in equal measure, so does effective action dealing with the consequences of misconduct. And if we are known for anything here in Hong Kong, it has been our approach in taking up the attack on consequences, especially in cases where those consequences are perhaps not ones that victims are best able to identify or address themselves.

I know there is a view in some other markets that redress for misconduct should be the market's responsibility and not the regulators. But the brutal reality is that the unravelling of most white collar crime is simply beyond the means of most investors, especially retail investors and their advisers.

This year we have initiated one case that took seven years to investigate. The time taken has nothing to do with any lack of diligence or effort on our part but more to do with the diffusion of places around the world we have had to engage in order to gather the evidence. Investigation can be a difficult task joining disparate and sometimes hard to find dots. We have now frozen assets worth more than \$1 billion in this case and we are seeking



restitutionary relief for thousands of victims on top of separate proceedings in which we are seeing sanctions against the alleged wrongdoers themselves. In essence, we are using combination of deterrent sanctions and the spectrum of equitable remedies to provide equity in our market.

On that note, I hope I have set the scene for our panel discussion.

Thank you.