SFC Enforcement Reporter

A monthly summary of SFC enforcement action

SFC 證監會

April 2005

Highlights

In March 2005, the SFC:

- **successfully prosecuted five companies and four people**
- **disciplined 15 licensees**

Prosecution

Helper of market manipulation sentenced

Ms Wan Wai Chi Katherine was sentenced to perform 120 hours of community services following her earlier conviction for aiding and abetting a person to create a false and misleading appearance of active trading in a stock and to conduct wash-sales with the intention of raising the stock's price. Wan was also ordered to pay the SFC's investigation costs.

(Press releases issued on 24 February 2005 and 14 March 2005)

Market manipulation is serious misconduct which will lead to criminal prosecution. It creates a false perception of the market which misleads investors and could damage their interests. The SFC will take appropriate action to prevent and penalise such conduct. Serious instances are likely to result in custodial sentences.

Mishandling of clients' securities results in prosecution

Victory Securities Company Ltd and its responsible officer Ms Kou Kuen Katerine pleaded guilty to pledging clients' securities without obtaining prior approval from clients in August 2003. The SFC found that Victory had pledged clients' securities to its bank accounts in order to secure overdraft facilities. They were fined a total of $10,000 and ordered to pay the SFC's investigation costs.

(Press release issued on 31 March 2005)

Licensees should obtain prior approval of clients before pledging their shares. Without the approval, licensees will be abusing the trust of their clients and putting client assets at risk. The SFC treats this seriously and licensees committing such misconduct could face prosecution and discipline.

Failures to disclose interests and keep a register of interests result in prosecution

Mr Leung Kin Keung and Mr Lee Wing Ngai pleaded guilty to disclosure of interests breaches. Leung failed to make initial disclosure to Hong Kong Exchanges and Clearing Ltd (HKEx) and Golden 21 Investment Holdings Ltd of his interest in the shares of Golden 21, upon commencement of the Securities and Futures Ordinance (SFO) on 1 April 2003. Lee failed to report within the proper period after his acquisition and disposals of Golden 21 shares. Leung and Lee were fined $4,000 and $22,000 respectively, and ordered to pay the SFC's investigation costs.

(Press release issued on 3 March 2005)

Montgomery Properties Holding Ltd pleaded guilty to failing to, as a principal, ensure that it was immediately notified of the disposals of its shares in Everpride Biopharmaceutical Company Ltd effected by its agent on three occasions. As a result of such failure, Montgomery was unable to disclose its reduction in interests from the three disposals within the prescribed period as required by the SFO. Montgomery was fined $9,000 and ordered to pay the SFC's investigation costs.

(Press release issued on 31 March 2005)

The Court of First Instance dismissed Mr William Mong Man Wai's appeal against his earlier conviction in relation to his failure to notify the Stock Exchange of Hong Kong Ltd and the Bank of East Asia Ltd (BEA), of which he was appointed a non-executive director on 1 June 1995, of his deemed interest arising from a purchase of 2,000,000 BEA shares on or about 17 March 1995 within five days after the appointment.

(Press releases issued on 30 August 2004 and 24 March 2005)

Linefan Technology Holdings Ltd pleaded guilty to failing to keep a register of interests in shares for substantial shareholders and a register of the same for directors and chief executives. Linefan was fined $2,000 and ordered to pay the SFC's investigation costs.

(Press release issued on 10 March 2005)

China Conservational Power Holdings Ltd (then known as Yew Sang Hong (Holdings) Ltd) in August 2002 commenced an investigation under section 18 of the Securities (Disclosure of Interests) Ordinance and requested from its shareholders information in relation to its shareholding. However, it failed to enter the shareholding information received in its register of interests in shares and notify HKEx and the SFC of the information. China Conservational pleaded guilty to the failure. It was fined $9,000 and ordered to pay the SFC's investigation costs.

(Press release issued on 24 March 2005)

Disclosure of interests in listed companies is essential to ensuring market transparency. Keeping an updated register of shareholders' interests helps achieve this end. The SFC will continue to prosecute people who fail to comply with the disclosure requirements.

Company prosecuted for unlicensed advising on corporate finance

MCC Capital Consulting Ltd pleaded guilty to holding itself out between February and July 2004 on its website as carrying on a business of advising on corporate finance whilst unlicensed. It was fined $5,000 and ordered to pay the SFC's investigation costs.

(Press release issued on 10 March 2005)

Unlicensed persons cannot perform regulated activities. The SFC will prosecute those who engage in such activities and take disciplinary action against licensees who help them. To protect their interests, investors should check in advance if people they deal with are licensed by the SFC.

Person convicted of short selling

Mr Fung Wing Kwong pleaded guilty to short selling securities on 25 February 2004. He was fined $10,000 and ordered to pay the SFC's investigation costs.

(Press release issued on 10 March 2005)

The SFO prohibits the sale of securities when a person does not have a presently exercisable and unconditional right to sell them. Brokers can help eradicate this illegal practice by putting in place sound internal controls to detect and prevent short selling.

Discipline

Lengthy suspension for conflicts of interest and unsound advice

The SFC suspended the licence of Mr Lo Chiu Wai, a licensed representative of South China Securities Ltd and South China Commodities Ltd, for nine months. In an investigation concerning a placement by Cedar Base Electronic (Group) Ltd (now renamed China Water Affairs Group Ltd) in January 2002, the SFC found that Lo had borrowed $4.5 million from a client and lent it to three other clients to subscribe for Cedar Base shares in the placement. As a result, Lo became interested in the transactions. Lo failed to avoid the conflicts of interest because he did not want to lose a business opportunity. The loans also breached Lo's employers' internal rules. Furthermore, Lo recommended to the three clients to subscribe beyond their means by borrowing substantial loans from him to finance the investment. The SFC took into account Lo's co-operation in settling with the SFC when deciding penalty.

(Press release issued on 29 March 2005)

Licensees must handle conflicts of interest with extreme care. Loans to and from clients clearly give rise to conflicts of interest. Licensees should avoid becoming personally interested in clients' transactions. Client interests are at risk in such situations and the SFC will penalise more heavily if there is evidence of any harm to clients. Equally importantly, advice or recommendations given by licensees to clients must be suitable, based on thorough analysis and having taken into account alternatives. In the case of a leveraged transaction, licensees must also ensure that the client understands the nature and risks of the transaction and has sufficient net worth to be able to assume the risks and bear the potential losses of the transaction.

Suspension for facilitating or accepting suspicious orders

The SFC suspended the licence of Ms Lui Yee Ying, Candy for four months for facilitating suspicious trading activities. Lui was a securities dealer representative of Eureka Securities Ltd in 2002. She signed as a witness on the account opening documents of several clients whom she had not met them. She accepted instructions from a third party to trade in those accounts without the clients' authorisation. Lui was aware that: the pattern of those trades was abnormal but did nothing to stop it even though she realised it was probably manipulative.

(Press release issued on 18 March 2005)

The SFC suspended the licence of Mr Ho Kwan Kit, a licensed representative of Sun Hung Kai Investment Services Ltd and Sun Hung Kai Commodities Ltd, for two months for accepting suspicious orders. Near the market close on 28 February 2003 Ho input in quick succession 10 bid orders for a client, each for one board lot, and each at eight spreads above the previous bid price of a stock. The client had made clear to Ho that her intention was to double the stock's price. The SFC took into account Ho's co-operation in settling with the SFC when deciding penalty.

(Press release issued on 24 March 2005)

Licensed persons are not only accountable to their employers, but should also act with due skill, care and diligence, in the best interests of the clients and the integrity of the market. Signing account opening documents without knowing the clients, allowing a third party to trade in clients' accounts without clients' authorisations, and turning a blind eye to suspicious trades are acts that call into question licensees' ability to perform efficiently and fairly. Licensees failing to have regard for market integrity will face appropriate sanctions.

Stabilizing manager reprimanded and fined for breaching price limits

The SFC reprimanded and fined Daiwa Securities SMBC Hong Kong Ltd $100,000, and reprimanded Mr Koji Yoshihara, one of its licensed representatives at the material time, for breaching the pricing limits as stipulated under Schedule 2 of the Securities and Futures (Price Stabilizing) Rules. Daiwa Securities SMBC breached the Rules 25 times, either by placing buy orders or executing transactions at prices exceeding the maximum price stipulated in the Rules. The SFC took into account that the breaches were inadvertent in nature and the price stabilization performed by Daiwa Securities SMBC had no significant effect on the price of the shares in question. The SFC also took into account Daiwa's voluntary reporting of the breach, subsequent reforms and its co-operation in settling with the SFC.

(Press release issued on 2 March 2005)

The Price Stabilization Rules legitimise certain dealing activity that would otherwise be considered manipulative. Intermediaries appointed by or representing the offerors of securities should ensure that they strictly follow the Rules if they intend to make use of this concession.

Financial Resources Rules breaches result in reprimands and fines

The SFC reprimanded Guangdong Securities Ltd (GSL) and one of its responsible officers, Mr Yang Jian, for failing to maintain the required liquid capital for one day. GSL was also fined $100,000. In early 2004, GSL received and executed considerable size buy orders from a private fund managed by it. GSL failed to check and ensure the adequacy of liquid capital before executing the orders. It then discovered the liquid capital deficiency and reported the breach to the SFC and took remedial action. The SFC found that GSL had failed to implement adequate internal controls, hence contributing to the FRR breach. In particular, GSL had failed to put in place an adequate system to ensure its FRR compliance; and ensure effective communication and coordination among departments. At all material times, Yang was the responsible officer of GSL responsible for FRR compliance and hence he bore responsibility for GSL's failures. The SFC took into account their co-operation in settling with the SFC in deciding penalty.

(Press release issued on 23 March 2005)

The SFC reprimanded Evergreen Securities Ltd and its responsible officers, Mr Cheng Hok Wai and Mr Cheng Ho Yan Erik, for breaches of the FRR. Cheng Hok Wai was also fined $50,000. Evergreen was convicted in June 2004 of breaching the FRR. It failed to notify the SFC as soon as reasonably practicable after its liquid capital fell below the required liquid capital in three periods in June to August 2003. The breaches were the result of Cheng Hok Wai's instructions to transfer Evergreen's funds to his private company in order to reduce that company's interest costs. Cheng Hok Wai was convicted of consenting to or connivance in Evergreen's failures. Cheng Ho Yan Erik was aware of the transfers but took no action to ensure Evergreen's compliance with the FRR. They also knew about an earlier SFC warning, that it viewed FRR breaches very seriously, issued previously when Evergreen's liquid capital fell below the required liquid capital before. The SFC took into account their co-operation in settling with the SFC and pleading guilty in the earlier criminal prosecution, and the level of criminal penalty, in deciding penalty.

(Press release issued on 23 March 2005)

Compliance with the FRR is vital to ensure licensees have adequate financial resources to meet their ongoing obligations and provide a buffer against insolvency. A responsible licensee should pay proper heed to SFC warnings. Having been alerted by the SFC to a breach or other deficiencies, a licensee should endeavour to take proper investigative, preventive and/or remedial measures as necessary. If he ignores it, the SFC will view further breaches more seriously.

Licensees disciplined for failings relating to client accounts

The SFC suspended Ms Tong Lee Mei Wah Lolitta, a licensed representative of Prudence Securities Company Ltd, for four months for conducting unauthorised trades. The SFC found that Tong had failed to obtain prior written authorisation from the client to authorise the client's husband and Tong to place discretionary orders in the client's account. The SFC also found that Tong had failed to exercise due care, skill and diligence when conducting discretionary trades for the client, resulting in substantial losses in the client's account.

(Press release issued on 9 March 2005)

The SFC suspended the licence of Mr Weng Yi Jiong for one month. He allowed unauthorised operation of a client account by a third party and failed to establish and record the true and full identity of the third party. The SFC took into account, among other things, Weng had co-operated with the SFC and obtained a duly signed third party authorisation form and a copy of the identification document of the third party afterwards.

(Press release issued on 7 March 2005)

The SFC reprimanded Mr Wong Yu Chiu, a responsible officer of Interchina Securities Ltd, and fined him $50,000. Wong had failed to explain the account opening documents and risk disclosure statement to his client and signed as witness to his client's signature in the account opening documents without actually witnessing his client signing the same. He also failed to act with due care in handling an order of the client which resulted in short selling of shares in the client's account, and failed to maintain a complete audit trail to record clients' trading. Furthermore, he used his personal cheques to settle the client's transactions notwithstanding that he instructed his subordinates not to do so. The SFC took into account Wong's co-operation in settling with the SFC in deciding penalty.

(Press release issued on 22 March 2005)

Licensees must obtain written authorisation from a client before accepting a third party's instructions to operate the client's account or placing discretionary orders in the client's account. This protects the client from unauthorised trades and prevents the client from disclaiming third party trades at a later date. Also, licensees have a very important duty to know their clients. When handling a transaction, they must satisfy themselves about the identity of those who originate instructions in relation to the transaction and record the information. Furthermore, licensees are required to act with due skill, care and diligence in *the best interests of their clients when conducting business activities. In particular, they should ensure that clients are provided with adequate information regarding their rights and risk exposure when they open accounts with brokers.*

Don't conduct unlicensed regulated activities

The SFC suspended the licence of Mr Yeung Hok Huen, Runter for one month for conducting unlicensed regulated activities. In October 2003, Yeung joined RBC Investment Services (Asia) Ltd. He disobeyed an instruction of RBC which asked him not to engage in regulated activities until he was licensed to act for RBC. Assisted by a colleague, Yeung opened securities accounts for clients, accepted and confirmed client orders, and made stock recommendations while he waited for SFC's approval of his accreditation. RBC conducted an internal investigation and disciplined Yeung and his colleague. RBC also submitted a report to the SFC in accordance with the law. The SFC proposed to reprimand and fine Yeung. However, Yeung asked the SFC to suspend him instead of imposing a fine because he could not afford to pay. The SFC agreed to substitute the proposed fine with a proportionate suspension, taking into account his personal circumstances.

(Press release issued on 29 March 2005)

When a licensed representative changes employer, he has to obtain approval from the SFC before he can carry on regulated activities for that new employer. Knowingly ignoring an employer's instructions and policy is an aggravating factor. The SFC took into account RBC's internal discipline of Yeung in deciding on sanction. It also commends RBC's prompt report to the SFC and appropriate actions as an example for other licensees.

Poor standards and short selling result in reprimand and fine

The SFC reprimanded and imposed a disciplinary fine of $14,000 on Mr Ng Mau Chung for poor standards and short selling. On 20 June 2003, Ng, a licensed representative of Kaiser Securities Ltd and Kaiser Futures Ltd at the material time, placed an order to sell 12 million MAE shares when he only had nine million shares on hand. Ng discovered his mistake and immediately rectified the matter by buying the number of shares short sold. On the same day, Ng carelessly placed a wrong order for a client by selling instead of buying 12 million MAE shares. He placed orders for two other clients without checking the stock balance of their accounts. He reported the error trades to Kaiser Securities Ltd's responsible officer on the same day. The SFC considered Ng's short sales were unintentional and due to carelessness. No loss or damage was suffered by clients, the public, or market users.

(Press release issued on 16 March 2005)

It is essential that account executives take all necessary precautions to check the stock balances and accuracy of the orders before placing them.

General Enforcement Statistics

In the financial year from 1 April 2004 to 31 March 2005, the SFC has successfully prosecuted 76 entities. Summonses were withdrawn against eight entities and a further six entities were acquitted after trial. There were also three entities which the SFC offered no evidence. In 2004-2005, the SFC took action against a total of 88 licensees. Among them, we disciplined 78 licensees for various regulatory breaches. The SFC entered into settlements without formal sanctions with 10 licensees, of which four were settled with voluntary payments. The SFC also took disciplinary actions against 28 licensees which were eventually concluded with no formal sanction imposed, although 15 of them received private warnings. Disciplinary proceedings were also commenced and discontinued against four deemed licensees who left their firms before the conclusion of the action. (A person's deemed licence is effectively revoked on the day the person leaves his or her firm. Under the transitional arrangements, which came into force on 1 April 2003, the SFC has no jurisdiction to continue with disciplinary proceedings against such a person. However, the person would be required to answer the SFC's concerns about him or her if he or she re-applies for a licence or other regulatory approval.)

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