

Operational Review

We maintain stability, competitiveness and orderliness in the financial markets through our principal areas of work: intermediaries, products, corporates, markets and enforcement.

Intermediaries

We set standards and qualifying criteria for corporations and individuals licensed to operate in our markets under the Securities and Futures Ordinance (SFO). As part of our ongoing supervision, we conduct on-site inspections and off-site monitoring of licensed corporations¹, and explain our regulatory focus and concerns to the industry. We closely monitor market and technological developments and adapt our approach accordingly.

Licensing

As of 31 March 2019, the number of licensed corporations totalled 2,960, up 10% from last year. The number of licensees and registrants increased 5% to 46,678 in the same period. We received 8,942 new licence applications during the year, an increase of 8% from a year earlier. These were both record highs since the implementation of the regulatory regime under the SFO on 1 April 2003.

Revamped licensing process

To enhance efficiency and transparency and to keep ahead of the evolving financial market landscape, we revamped our licensing process and introduced new measures to sharpen our focus on key risks and achieve better regulatory outcomes. In May 2018, we restructured the Licensing Department to improve operational efficiency. In addition, we redesigned our licensing forms to introduce an enhanced risk-based approach. In September 2018, we held three consultation sessions to discuss the revamped licensing process with industry participants, including fund managers, brokers, investment banks and compliance consultants.

Starting 26 November 2018, approval letters to individual licence applicants are only sent electronically, copying their accredited licensed corporations. Also on the same date, the delegation of the SFC Online Portal function was adjusted to allow directors of licensed corporations or registered institutions and persons authorised by their boards to submit corporate notifications and annual returns. Previously, only responsible officers and executive officers were allowed to submit these documents.

¹ Broadly, licensed corporations include securities brokers, futures dealers, leveraged forex traders, fund managers, investment advisers, sponsors and credit rating agencies.

In February 2019, new forms and a new edition of the SFC's Licensing Handbook were released. After a two-month transitional period, both the use of the new forms and the electronic submission of annual returns and notifications via the SFC Online Portal were made compulsory from 11 April 2019. (See sidebar on the licensing reform on page 44.)

Annual licence fees

From 1 April 2019, we resumed the collection of annual licence fees after a seven-year period when these fees were waived. A fee concession of 50% was provided for two years. Annual fees will be fully reinstated from 1 April 2021. We issued a circular in March 2019 to set out the annual fee collection arrangements for the industry.

Prudential risks

Securities margin financing

In April 2019, we concluded a public consultation on proposed guidelines which set out the expected risk management standards for securities margin financing (SMF) activities. The guidelines include qualitative requirements and quantitative benchmarks for margin lending policies and key risk controls. The consultation was launched in August 2018 and followed a 2017 review of SMF activities which indicated dramatic

growth in total margin loans over the last decade, with significant deterioration in the quality of loans and widespread imprudent lending practices among brokers. A report summarising the review findings was also published in August 2018.

OTC derivatives

We launched a two-month consultation in June 2018 on proposals to impose margin requirements for non-centrally cleared over-the-counter (OTC) derivatives. The proposals specify the categories of licensed corporations, counterparties and instruments subject to the requirements for margin exchange, as well as the assets eligible as margin. We plan to publish consultation conclusions later this year.

In December 2018, we released consultation conclusions on proposals to enhance the OTC derivatives regime and address conduct risks posed by dealings with group affiliates and other connected persons. New risk mitigation requirements for non-centrally cleared OTC derivative transactions will take effect on 1 September 2019. Client clearing requirements for OTC derivative transactions will become effective when the new Types 11 and 12 regulated activities come into effect. The effective date for the conduct requirements to address risks posed by group affiliates and other connected persons is 14 June 2019.

Licensees

	Corporations [^]		Representatives		Responsible Officers		Total [^]		
	As at 31.3.2019	As at 31.3.2018	As at 31.3.2019	As at 31.3.2018	As at 31.3.2019	As at 31.3.2018	As at 31.3.2019	As at 31.3.2018	Change
Stock exchange participants	581	563	12,397	12,096	2,155	2,043	15,133	14,702	2.9%
Futures exchange participants	114	115	849	884	199	188	1,162	1,187	-2.1%
Stock exchange and futures exchange participants	81	74	5,002	4,831	576	536	5,659	5,441	4%
Non-stock/non-futures exchange participants	2,184	1,950	16,655	15,784	5,769	5,174	24,608	22,908	7.4%
Total	2,960	2,702	34,903	33,595	8,699	7,941	46,562	44,238	5.3%

[^] These figures exclude 116 registered institutions as at 31 March 2019 and 120 as at 31 March 2018.

Intermediaries

Financial resources rules

In October 2018, we issued consultation conclusions on proposed amendments to the Securities and Futures (Financial Resources) Rules to update the computation basis for the financial resources requirements and ensure the rules are compatible with the latest market developments. The new requirements were enacted on 12 December 2018. Amendments related to a new accounting standard took effect on 1 January 2019 and the remaining amendments came into effect on 1 April 2019.

Strategic licensing review

Our licensing processes are a key element of our gatekeeping function. By collecting more relevant information from applicants upfront, this can help us make decisions faster and identify issues earlier.

During the year, we completed a thorough review to make our licensing functions more transparent, speed up our workflow and improve communication with the industry. To this end, we introduced a three-pronged strategic reform to modernise our licensing processes.

First, we reorganised our licensing functions and re-engineered the operational flow to make it more efficient. After the restructuring, we observed general improvement in overall efficiency in processing individual licensing applications.

Next, we refined our assessment approach by focusing on five key risks of a corporate licence applicant, namely its business, controller, management, financial strength and internal control.



Licensing workshops

Conduct risks

Professional investors

In May 2018, we issued consultation conclusions on proposals to standardise the rules for prescribing professional investors and ensure consistent application of our regulations. The amended rules came into effect on 13 July 2018. We also explained the professional investor regime on the website of the Investor and Financial Education Council².

To demonstrate its financial strength, the applicant must provide a projection of its operating expenses in the first six months after having been licensed.

We also published self-assessment questionnaires for corporate applicants to match SFC-regulated activities with their business profiles as well as to evaluate the soundness of their risk management and internal control measures. These allow us to identify potential regulatory issues at an early stage.

Thirdly, we improved our interaction with licensees and applicants by introducing a series of redesigned licensing forms, along with user-friendly instructions and navigation guides, to collect the information we need to assess an applicant's fitness and properness upfront. To enhance the efficiency and transparency of the application process, we revised some questions set out in the licensing forms and streamlined the information requirements.

We also released a new edition of the Licensing Handbook and updated the licensing section on the SFC website to provide additional guidance on these enhancements as well as recent policy updates.



² Formerly known as the Investor Education Centre.

Alternative liquidity pools

In April 2018, we issued a circular and thematic report to highlight the key areas of concern and good practices noted during a thematic review of alternative liquidity pools (ALPs) which identified a number of deficiencies including in ensuring that ALP users are qualified investors. The report also provides an overview of the ALP landscape in Hong Kong.

Sale of complex products

We issued consultation conclusions in October 2018 on requirements for intermediaries to apply additional protective measures to the sale of complex products in an offline environment. Intermediaries have to ensure the suitability of complex products and provide product information and warning statements to clients when the complex products are sold on an unsolicited basis. Accordingly, identical protective measures will apply to both the online and offline sale of complex products with effect from 6 July 2019. This ensures better investor protection, provides a level playing field for industry participants and avoids potential regulatory gaps.

Disclosure

In May 2018, we concluded a public consultation on proposed disclosure requirements applicable to discretionary accounts to address potential conflicts of interest where product issuers provide incentives

to discretionary account managers. We also published frequently asked questions on the requirements, which became effective in November 2018.

"Nominees" and "warehousing" arrangements

In light of the increasingly prevalent use of "nominees" and "warehousing" arrangements which may play a part in market and corporate misconduct, we issued a circular in October 2018 reminding intermediaries to be vigilant in identifying potential red flags which may suggest the use of these arrangements for illegitimate purposes, make follow-up enquiries with clients and report suspicious transactions promptly to us and other authorities where necessary.

Financial technology

Online client onboarding

We issued a circular in July 2018 to provide guidance to intermediaries on using electronic signatures to onboard individual clients online. The alternative procedures specified in the circular provide safeguards to contain the risks while enabling intermediaries to onboard clients more efficiently and better serve customers without compromising their regulatory responsibilities.

Breaches noted during on-site inspections

	2018/19	2017/18	2016/17
Internal control weaknesses ^a	443	535	598
Breach of Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ^b	275	320	441
Non-compliance with anti-money laundering guidelines	201	175	201
Failure to safekeep client money	28	59	62
Failure to safekeep client securities	32	38	58
Others	257	349	395
Total	1,236	1,476	1,755

^a Comprised deficiencies in management review and supervision, operational controls over the handling of client accounts, segregation of duties, information management and adequacy of audit trail for internal control purposes, among other weaknesses.

^b Commonly related to risk management, record keeping, client agreements, safeguarding of client assets and management responsibilities.

Note: See Table 4 in Breakdown of SFC activity data on page 166 for more details.

Intermediaries

Client orders via instant messaging

We issued a circular in May 2018 to provide guidance on the controls and procedures intermediaries are expected to implement when they receive clients' orders through instant messaging services. They are encouraged to take adequate measures, such as keeping proper records of messages relating to client orders, ensuring all records are accessible for monitoring and audit purposes, validating client identities and maintaining adequate safeguards to prevent unauthorised access and security attacks.



Ms Julia Leung (right), Deputy Chief Executive Officer and Executive Director, Intermediaries, at Freshfields Bruckhaus Deringer's Asia In-House Counsel Forum 2018

Virtual assets

In June 2018, we issued a circular to remind intermediaries to inform us of any plans to provide trading and asset management services involving virtual assets or robo-advisory services. Intermediaries were also advised to discuss their plans with the SFC before they engage in these services.

We published regulatory standards for managers of funds which invest in virtual assets in November 2018. The sale of these unauthorised funds was limited to professional investors. We also developed a conceptual framework for exploring whether we should regulate virtual asset trading platforms in consideration of serious investor protection issues. If implemented, this regulatory approach could provide a path for compliance for those platform operators capable and willing to adhere to a high level of standards and practices, and set them apart from others which do not seek a licence. (See sidebar on page 47.)

In March 2019, we issued a statement clarifying the legal and regulatory requirements applicable to parties engaging in security token offerings. We also reminded investors to be wary of the risks associated with virtual assets, including tokens which are the subject of security token offerings.

Anti-money laundering

In July 2018, we launched a public consultation on proposed amendments to the Guideline on Anti-Money Laundering and Counter-Financing of Terrorism (For Licensed Corporations) as well as the Prevention of Money Laundering and Terrorist Financing Guideline Issued for Associated Entities to align them with the latest international standards and provide additional guidance in light of industry developments. The amended guidelines came into effect on 1 November 2018.

We issued a circular in April 2018 to draw licensed corporations' attention to the findings of the Government's *Hong Kong Money Laundering and Terrorist Financing Risk Assessment Report* and provide guidance on measures that they should take to mitigate any money laundering and terrorist financing risks identified in the report. We conducted three seminars for around 700 industry participants in June 2018 on the implications of the report's findings for licensed corporations.

In August 2018, we issued a circular highlighting deficiencies in anti-money laundering and counter-financing of terrorism (AML/CFT) measures and controls identified during our inspections. The circular provided guidance with practical examples for complying with the legal and regulatory requirements and enhancing AML/CFT policies, procedures and controls.

A mutual evaluation was carried out by the Financial Action Task Force and Asia/Pacific Group on Money Laundering in 2018³. Following completion of its on-site review of Hong Kong last year, we will continue to update our AML guidance notes to align with the latest international standards.

³ See Regulatory engagement on pages 73-76.

Fintech developments

In this fast-moving technological landscape, we take a facilitative approach to innovation when Fintech can be used to provide better customer experience, increase financial inclusion or make markets more efficient and reliable. One example is the growth of online platforms which provide more choices and offer better service and convenience to investors. In this regard, we issued the Guidelines on Online Distribution and Advisory Platforms which came into effect in April 2019.

We also engage with firms, industry organisations, startups and other stakeholders through the SFC Fintech Contact Point, which handled over 200 enquiries during the year.

Where a Fintech activity poses serious risks to investor protection, we take a more cautious stance. Virtual asset activities are associated with risks arising from illiquidity, volatility, opaque pricing, hacking, money laundering and fraud. A prudent approach is therefore required. We announced a conceptual framework for the potential regulation of virtual asset trading platforms in November 2018 and are currently considering our regulatory approach towards virtual assets.

On a day-to-day basis, we closely monitor licensed corporations' risk management practices to determine whether they need to be strengthened in response to technological developments or to address cybersecurity risks, data privacy breaches or other concerns. We mandate two-factor authentication and other baseline requirements for internet brokers and conduct inspections on a sample basis to assess compliance.

We are now considering how to enhance data collection and analysis using supervisory technology. As a trial, we analysed licensed corporations' algorithmic trading and dark pool operations to assess their compliance with business conduct standards. We identified non-compliance and are consulting the industry on standards to prescribe trading data to be submitted to us.

We update our regulation to cover business models created by new technologies and avoid potential regulatory gaps. We provided tailored guidance on the design and operation of online platforms, including the provision of automated or robo-advice, as well as on opening accounts for individual clients who are not physically present and accepting client orders via instant messaging applications.

Supervisory approach

We adopt a front-loaded and risk-based approach by focusing on the greatest threats and the most significant or systemic risks. We employ a variety of tools to supervise licensed corporations with a focus on their financial risks and how they conduct business.

On-site reviews

On-site reviews, which include prudential visits and routine, special and thematic inspections, are a key supervisory tool for understanding a firm's business operations, risk management and internal controls and gauging its compliance with legal and regulatory requirements. This includes assessing whether it acts with due skill, care and diligence and adopts proper business conduct, procedures and practices. During the year, we conducted 304 risk-based on-site inspections, including thematic inspections on a wide range of issues identified.

In recent years, we have increased the use of thematic inspections as a tool to assess the scale and nature of particular cross-sector risks. These inspections may be triggered by the identification of trends, emerging risks and compliance lapses that require prompt regulatory responses. We highlight to the industry key areas of concern noted during a thematic inspection as well as provide guidance on the standards of conduct and internal controls expected of licensed corporations. As in other inspections, where major breaches or non-compliance are identified, we may conduct enquiries or an enforcement investigation into the case and take disciplinary action.

This year, thematic inspections included AML/CFT, cybersecurity, intermediary misconduct in listed markets and selling practices. Other topics, including brokers' internal controls and supervision of account executives as well as risks relating to remote booking models, were also covered during the year.

Intermediaries

In December 2018, we issued a comprehensive self-assessment checklist along with a thematic review of brokers' internal controls to help them assess their control policies and procedures and improve their supervision of account executives.

Off-site monitoring

We conduct off-site monitoring through regular interaction with licensed corporations to understand their business models and their plans to identify and assess risks. We evaluate their financial soundness mainly through analysis of their regular financial returns. We also utilise intelligence from a variety of sources and follow up on complaints and self-reported breaches. In addition, we examine applications by licensed corporations for subordinated loans and rule modifications or waivers. This helps us form a holistic view of their business profiles.

Data analytics

We are enhancing our analysis of data for regulatory purposes and our capability to monitor current trends, emerging issues and risks using new technologies.

Stress-testing brokers

We launched an automated system in July 2018 to conduct stress tests to identify thinly capitalised brokers following increased extreme price movements and trading suspensions of small-cap stocks held by licensed corporations as securities collateral. We also introduced a stress test system for futures and options brokers in December 2018.

Business and Risk Management Questionnaire

A revamped Business and Risk Management Questionnaire (BRMQ) launched in January 2019 collects information about the business operations of firms and their specific measures to ensure sound risk management and proper internal controls. This will enable us to supervise licensed corporations and associated firms more effectively. For financial years ending on or after 31 March 2019, firms are required to complete and electronically submit the revamped BRMQ within four months after the end of each financial year.

Statistical information and financial position of the Hong Kong securities industry

	As at 31.12.2018	As at 31.12.2017	As at 31.12.2016
Securities dealers and securities margin financiers	1,312	1,222	1,104
Active clients	1,874,289	1,657,931	1,556,695
Total assets (\$ million)	1,226,532	1,337,404	1,078,521

(\$ million)	12 months to 31.12.2018	12 months to 31.12.2017	12 months to 31.12.2016
Total value of transactions ^a	89,678,389	73,901,390	63,495,134
Total operating profit	23,548	23,539	14,131

^a Data extracted from the monthly financial returns submitted under the Securities and Futures (Financial Resources) Rules by corporations licensed for dealing in securities or securities margin financing. Figures reported by an overseas incorporated licensed corporation which carries out its principal business activities outside Hong Kong and operates in Hong Kong as a branch office were excluded.

Note: Also see Table 8 in Breakdown of SFC activity data on page 169 for more details.

Industry guidance

We have broadened how we communicate with and give guidance to the industry. Published circulars are still the principal means through which we set out our regulatory expectations. In addition, in survey results, thematic reports and industry newsletters, we provide anonymised examples to illustrate best practices and our regulatory concerns. We also hold more frequent workshops when we are introducing a significant new regulatory measure.

Compliance Bulletin

We publish a newsletter, the *SFC Compliance Bulletin: Intermediaries*, to provide guidance on the SFC's regulatory and supervisory priorities. Through illustrative case studies, the May 2018 issue highlighted our regulatory focus and areas of concerns when considering licensing applications and provided an update on the implementation of the Manager-In-Charge regime. The November issue focused on the SFC's Fintech initiatives and the use of technology in our supervisory work.

Compliance Forum 2018

The SFC Compliance Forum 2018 was held in June. Over 500 industry participants attended the half-day event to exchange views on the SFC's recent guidance on best execution, client facilitation, sponsors and ALPs as well as the use of innovative technology to deliver financial services and the associated risks. (See Stakeholders on pages 77-81.)

Net asset value of compensation funds

	As at 31.3.2019 (\$ million)	Change	As at 31.3.2018 (\$ million)	Change	As at 31.3.2017 (\$ million)
Unified Exchange Compensation Fund ^a	79.3	4.6%	75.8	4%	72.9
Investor Compensation Fund ^b	2,391.5	1.3%	2,361.2	3.5%	2,280.4
Total	2,470.8	1.4%	2,437	3.5%	2,353.3

^a See pages 150-163 for the financial statements of the Unified Exchange Compensation Fund (UECF). The Investor Compensation Fund (ICF) was established by the SFO on 1 April 2003 to replace the UECF. After settlement of all claims against the UECF and its other liabilities, any remaining balance will be transferred to the ICF.

^b See pages 131-149 for the financial statements of the ICF.

Investor compensation

The enhancements to the investor compensation regime⁴ we proposed in an April 2018 consultation received strong support. Key proposals include increasing the compensation limit from \$150,000 to \$500,000 per investor per default and covering northbound trading under Mainland-Hong Kong Stock Connect. We are working towards issuing the consultation conclusions in the second half of 2019.

The Investor Compensation Company Limited, a wholly-owned SFC subsidiary, received five claims against the Investor Compensation Fund and processed 10 claims during the year.

Investor compensation claims

	2018/19	2017/18	2016/17
Received	5	1	10
Processed	10	6	19
– Compensation payments made	0	3	14
– Rejected	7	3	4
– Withdrawn	2	0	1
– Reconsidered	1	0	0

⁴ Claims against the Investor Compensation Fund may be made for exchange-traded products in the event of broker default.

Products

We formulate policy initiatives to strengthen Hong Kong's position as a full-service international asset and wealth management centre and a preferred fund domicile. On a day-to-day basis, we authorise and regulate investment products offered to the public in Hong Kong, including monitoring their ongoing compliance with our regulatory requirements.

Facilitating market development Authorisations

As of 31 March 2019, a total of 2,797 SFC-authorised collective investment schemes (CIS) were on offer to the public. During the year, we authorised 136 CIS, comprising 134 unit trusts and mutual funds, one investment-linked assurance scheme (ILAS) and one mandatory provident fund (MPF) pooled investment fund.

We authorised 130 unlisted structured investment products for public offering during the year.

ETFs and leveraged and inverse products

As of 31 March 2019, the number of SFC-authorised exchange-traded funds (ETF) listed on The Stock Exchange of Hong Kong Limited was 137, including 22 leveraged and inverse (L&I) products.

To offer more investment choices for investors in Hong Kong, we relaxed the leverage cap for inverse products to a factor of two-times negative (-2x).

In addition, we introduced active ETFs in the revised Code on Unit Trusts and Mutual Funds (UT Code). Unlike a passive ETF, an active ETF does not track an index, but seeks to achieve a stated investment objective by investing in a portfolio of stocks, bonds and other assets. The revised UT Code also allows listed and unlisted share classes to co-exist in a single fund pursuing the same investment strategy, expanding the funds' distribution channels¹.

Authorised CIS

	As at 31.3.2019	As at 31.3.2018	As at 31.3.2017
Unit trusts and mutual funds	2,216	2,215	2,203
ILAS	300	299	300
Pooled retirement funds	34	34	34
MPF schemes	31	31	35
MPF pooled investment funds	191	194	182
Others	25 ^a	26	26
Total	2,797	2,799	2,780

^a Comprising 14 paper gold schemes and 11 real estate investment trusts (REIT).

Unlisted structured investment products

	2018/19	2017/18	2016/17
Unlisted structured investment products ^a	130	114	100
Authorisations granted under the Securities and Futures Ordinance ^b	102	84	84

^a On a "one product per key facts statement" basis, the number of unlisted structured investment products authorised during the period, most of which were equity-linked investments and deposits.

^b Under section 105, offering documents and advertisements of unlisted structured investment products offered to the Hong Kong public.

¹ For example, an unlisted index fund distributed via the secondary market and a passive ETF for distribution in the primary market.



Ms Christina Choi, Executive Director, Investment Products, speaks at an industry conference on asset management

Renminbi products

As of 31 March 2019, there were 64 SFC-authorised unlisted funds² and 34 ETFs³ primarily investing in the onshore Mainland securities market⁴ or offshore renminbi bonds, fixed income instruments or other securities. The number of UCITS⁵ funds offering renminbi share classes increased rapidly after we issued guidance to clarify relevant requirements. This also fostered the development of related products and the introduction of additional renminbi investment options in the Hong Kong market.

SFC-authorised renminbi investment products

	As at 31.3.2019
Unlisted products	
Unlisted funds primarily investing in the onshore Mainland securities markets or offshore renminbi bonds, fixed income instruments or other securities	64
Paper gold schemes with renminbi features	1
Recognised Mainland funds under Mainland-Hong Kong Mutual Recognition of Funds arrangement	50
Unlisted structured investment products with renminbi features ^a	123
Unlisted funds (non-renminbi denominated) with renminbi share classes	195
Listed products	
ETFs primarily investing in the onshore Mainland securities markets or offshore renminbi bonds, fixed income instruments or other securities	34
Renminbi gold ETFs ^b	1
Renminbi REITs	1
ETFs (non-renminbi denominated) with renminbi trading counters	20

^a The number is on a "one product per key facts statement" basis.

^b Only includes gold ETF denominated in renminbi.

² Excluding recognised Mainland funds under Mainland-Hong Kong Mutual Recognition of Funds.

³ Refers to unlisted funds or ETFs which are renminbi denominated.

⁴ Refers to onshore Mainland investment through the Renminbi Qualified Foreign Institutional Investor quota, Stock Connect, Bond Connect and the China Interbank Bond Market.

⁵ Undertakings for collective investment in transferable securities.

Products

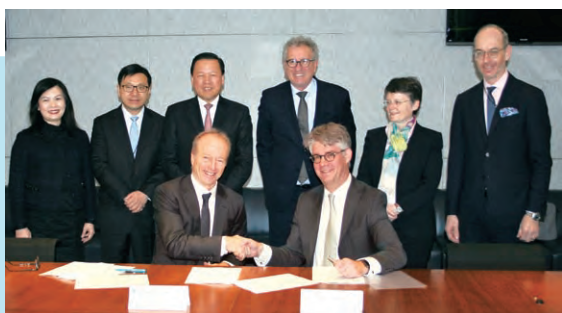
Mutual market access

To broaden the investor base for Hong Kong funds, promote Hong Kong as a competitive asset and wealth management centre and fund domicile and encourage the development of local investment expertise, we are proactive in promoting cross-border offerings of qualified Hong Kong public funds to overseas markets through mutual recognition arrangements.

Following the implementation of the mutual recognition of funds (MRF) arrangements with the Mainland and other markets⁶, we expanded our MRF network to include the UK in October 2018, Luxembourg in January 2019 and the Netherlands in May 2019.

After discussions with overseas regulators, we secured eligibility for SFC-authorised funds structured in the form of open-ended fund companies (OFC) under the MRF agreements with Switzerland, France, the UK and Luxembourg. We are exploring MRF arrangements with other overseas jurisdictions.

The Mainland-Hong Kong MRF regime maintained momentum with an increase in both applications and approvals of Hong Kong MRF funds. During the year, a total of eight funds were approved under the MRF, bringing the total to 69. As of 31 March 2019, the aggregate net subscription for both Mainland and Hong Kong MRF funds was about RMB10 billion.



Signing of MRF agreement with the Luxembourg Commission de Surveillance du Secteur Financier

Open-ended fund companies

The new OFC regime, which enables funds with variable capital to be established in corporate form in Hong Kong, came into effect on 30 July 2018. We worked closely with the Government to complete the legislative process for the subsidiary legislation. We also issued the new OFC code in July 2018 following a public consultation. By providing a corporate fund structure in addition to a unit trust form, the OFC regime broadens the choice of investment vehicles and facilitates the distribution of Hong Kong funds in overseas markets.

Revamped post-authorisation process

We implemented a revamped process to streamline the vetting of scheme changes and related revised documents subject to the SFC's approval in February 2018. Since then, there has been an overall improvement in the quality of applications and shorter processing times with more timely responses from applicants.

Asset and wealth management activities

We released the *Asset and Wealth Management Activities Survey 2017* (previously known as the *Fund Management Activities Survey*) in July 2018. To provide a more comprehensive overview of Hong Kong's asset and wealth management industry, the scope of this annual survey was extended to private banking and private wealth management clients' accounts. According to the survey findings, the asset and wealth management business in Hong Kong amounted to \$24,270 billion as at 31 December 2017⁷. Of this, \$17,511 billion was attributable to asset management and fund advisory business, which recorded a year-on-year increase of 23%.

Regulatory enhancements

UT Code review

Amendments to the UT Code took effect on 1 January 2019, with a 12-month transition period. A public consultation, concluded in December 2018, proposed amendments based on a holistic review of the UT Code which involved extensive engagement with stakeholders. Changes included strengthening the requirements for key operators and introducing new fund types (see sidebar on page 53).

⁶ Include Australia, Malaysia (for Islamic funds), Taiwan (for ETFs), Switzerland and France.

⁷ Due to the extended scope of the survey, comparative figures are not available.

Updates to fund regulation

As part of a holistic review to update the regulatory regime for public funds, changes were made to the UT Code in three major areas.

Derivative investments

To help investors better differentiate between products, the revised UT Code sets out a clear overall 50% limit for derivative investments by plain vanilla public funds. Funds with derivative investments over this limit are regarded as derivative funds which are subject to enhanced distribution requirements. This measure was refined after consulting a focus group comprising fund managers and industry experts.

To improve transparency, SFC-authorized funds have been listed as derivative funds or non-derivative funds on the SFC website starting from 1 January 2019.

Trustees and custodians

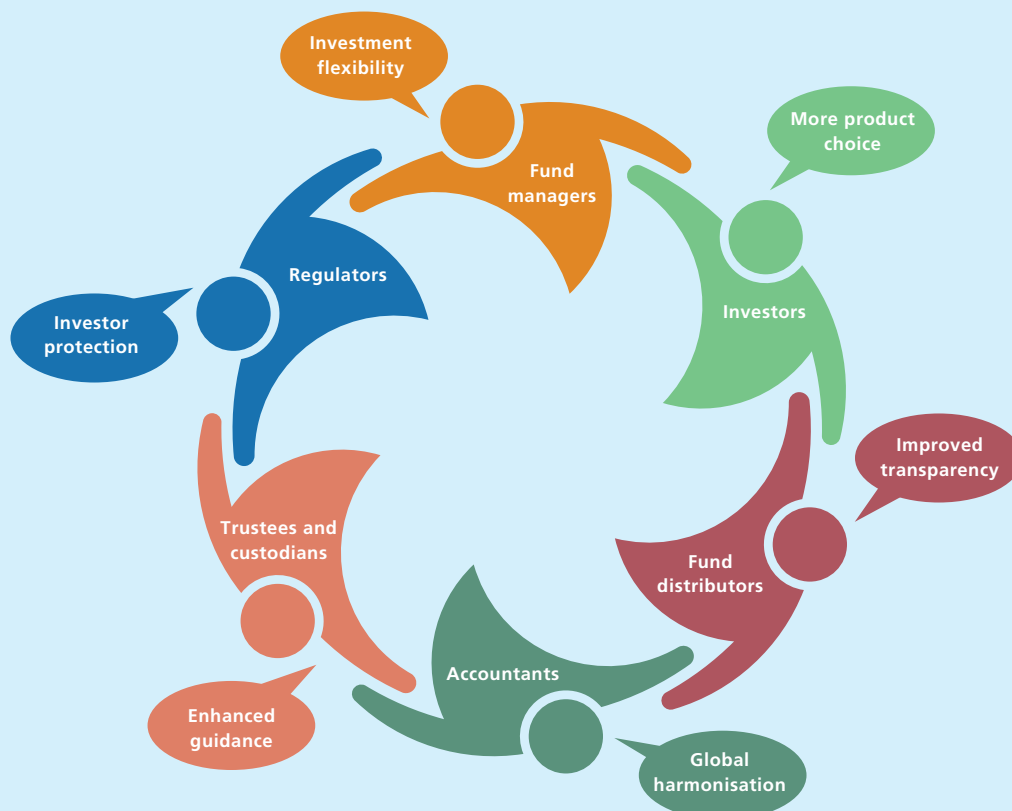
We tightened the obligations and internal controls requirements for trustees and custodians of public funds, which have important obligations to safeguard fund assets and perform independent oversight. We will also explore measures to ensure a robust regulatory regime for the safekeeping and custody of assets by trustees and custodians of public funds.

New product types

The revised UT Code introduces new fund types, such as active ETFs (see page 50), to encourage product development and offer investors wider investment choices.

To facilitate implementation of the revised UT Code, we published new guidance and frequently asked questions on our website and held two briefings for more than 250 industry participants.

Benefits for stakeholders



Products

Asset and wealth management

Revised fund management conduct requirements, which took effect in November 2018, enhance asset management regulation in key areas including securities lending and repurchase agreements, custody of fund assets, liquidity risk management and disclosure of leverage by fund managers.

Enhancements to provide more point-of-sale transparency to better address conflicts of interest when investment products are sold came into effect in August 2018. Important changes include requirements governing the use of the term “independent” by intermediaries and enhanced disclosures of trailer fees, commissions and other monetary benefits. Additional protective measures for the sale of complex products will become effective in July 2019, including the requirement to ensure the suitability of complex products sold on an unsolicited basis, whether distributed through online or offline platforms.

Surveillance and monitoring

We updated the fund data reporting requirements for Hong Kong-domiciled SFC-authorized funds in June 2018 to strengthen our ability to identify potential problem areas and monitor funds’ risk exposures. The requirements cover periodic reporting of key data including the fund’s subscription and redemption flows, liquidity profile, asset allocation and securities financing and borrowing transactions.



Industry briefing

In addition, we monitor the liquidity of funds through reports from asset managers on any unusual or untoward activities, including significant redemptions, suspensions of dealing and liquidity problems, and review abnormal fluctuations of the daily unit prices of Hong Kong-domiciled public funds as compared with their respective peer groups. We regularly monitor ETFs and L&I products through data related to pricing, exposure to counterparties and, for L&I products, daily rebalancing activities.

We also conduct ongoing surveillance of the marketing materials of SFC-authorized funds and fund managers’ websites to monitor their compliance with regulatory requirements. We perform routine surveillance of advertisements and handle complaints about property-related or other suspected arrangements which may be CIS. We looked into 19 suspicious CIS cases during the year.

We handled 13 cases of material non-compliance with regulatory requirements by issuers of SFC-authorized products, which resulted in compensatory payments totalling \$29 million to affected Hong Kong investors.

Corporates

We oversee listing and takeovers matters in Hong Kong, including takeovers and merger activities, vetting of listing applications, disclosure requirements, corporate conduct and the listing-related functions of The Stock Exchange of Hong Kong Limited (SEHK). We review listing and takeovers policies from time to time to keep pace with market changes and facilitate the development of Hong Kong's securities market.

Listing policy

Emerging and innovative companies

Following our approval, SEHK implemented new Listing Rules on 30 April 2018 allowing pre-revenue biotech companies and innovative companies with weighted voting rights (WVR) structures to list in Hong Kong. During the year, we received listing applications from four WVR companies and 13 biotech companies. As at 31 March 2019, two WVR companies and seven biotech companies were listed in Hong Kong.

After the SFC and SEHK signed an addendum to the Memorandum of Understanding Governing Listing Matters in March 2018, a new Listing Policy Panel¹ was established as an advisory, consultative and steering body to discuss listing policy with broader regulatory or market implications. In September, the panel held its inaugural meeting and discussed a proposal to permit corporate WVR beneficiaries.

Review of SEHK's work

In a December report, we reviewed SEHK's performance in its regulation of listing matters during 2016 and 2017. Our review focused on the Listing Department's operational activities, processes and procedures, particularly SEHK's vetting of initial public offering (IPO) applications and suitability for listing, the regulation of reverse takeover transactions, the handling of disclaimer audit opinions and policy on listing enforcement. The report identified specific areas for SEHK to enhance its performance.

Review structure for Listing Committee decisions

Following discussions with us, SEHK issued conclusions to its consultation on the review structure for Listing Committee decisions in January 2019. To promote transparency and accountability in decision-making, significant Listing Committee decisions will be subject to one level of review. A new independent committee, the Listing Review Committee, will be established to replace the existing Listing (Review) Committee and Listing (Disciplinary Review) Committee, while the Listing Appeals Committee will be discontinued. All decisions on non-disciplinary matters made by the new Listing Review Committee will be published. The changes are expected to take effect in mid-2019.

Review of listing regulation

Together with SEHK, we regularly review the effectiveness of listing regulation to maintain market quality and address problematic listed company behaviour. Following a public consultation, SEHK introduced new rules governing capital raisings by listed companies as well as a new delisting framework. It also consulted the public on proposals relating to backdoor listings and continuing listing criteria and a proposal to introduce a suspension requirement for companies with disclaimer or adverse audit opinions on their financial statements.



¹ The Listing Policy Panel consists of 12 members comprising senior representatives of the SFC, the Listing Committee, Hong Kong Exchanges and Clearing Limited and the Takeovers and Mergers Panel.

Corporates

IPO applications

We vet listing applications and raise enquiries to determine whether an application gives rise to any concerns under the Securities and Futures (Stock Market Listing) Rules (SMLR). We may object to a listing of securities based on one or more of the grounds set out in section 6(2)² of the SMLR.

We received 394 listing applications via SEHK during the year, up 28% from 309 last year, including four listing applications from WVR companies and 13 listing applications from biotech companies under the new listing regime for innovative companies. We shared our comments or concerns with SEHK where appropriate.

In line with our front-loaded regulatory approach, we directly sought information or expressed our



Our senior executives at a seminar hosted by the Hong Kong Securities and Investment Institute

New listing applications

concerns in 17 listing applications where we became aware of potentially serious disclosure or public interest issues. In two of these applications, the applicants satisfactorily addressed our concerns and were subsequently listed. As at 31 March 2019, six applications had not proceeded to listing, leaving our concerns unaddressed, and in nine applications, the applicants had yet to satisfactorily address our concerns.

During the year, we issued a “letter of mindedness to object”³ directly in two listing applications. One listing applicant postponed its share offer and was subsequently listed after addressing our concerns.

Corporate conduct

To better identify potential misconduct and irregularities in disclosures, we conduct daily reviews of corporate announcements under statutory corporate conduct and inside information disclosure provisions. During the year, we issued section 179⁴ directions to gather additional information in 73 cases and wrote to listed companies to detail our concerns about 37 transactions. These concerns included, for example, whether a corporate action or transaction is being conducted in a manner which is oppressive or unfairly prejudicial to shareholders.

SFC Regulatory Bulletin

During the year, we published the second and third issues of the *SFC Regulatory Bulletin: Listed Corporations* which used case studies to illustrate how we intervened at an early stage where we had serious concerns about IPO applications or corporate transactions.

	2018/19	2017/18	2016/17
Listing applications received ^a	394	309	245
Listing applications lapsed/withdrawn/rejected during the year	166	88	79
Listing applications returned ^b	0	3	5
New listings ^c	193	203	148

^a Including applications for transfer from GEM to the Main Board (2018/19: 16; 2017/18: 22; 2016/17: 18).

^b Listing applications were returned by SEHK because the application proofs or related documents were not substantially complete. The listing applicants can only submit a new listing application with a new application proof not less than eight weeks after the return.

^c Including successful transfers from GEM to the Main Board (2018/19: 11; 2017/18: 17; 2016/17: 6).

² Under section 6(2) of the SMLR, the SFC may object to a listing if it appears to the SFC that: (a) the listing application does not comply with SEHK's requirements or an applicable provision of law, or does not contain sufficient information to enable an investor to make an informed decision; (b) the application is false or misleading; (c) the applicant has failed to furnish information as may be reasonably required by the SFC under section 6(1) of the SMLR; or (d) it would not be in the interest of the investing public or in the public interest for the securities to be listed.

³ A “letter of mindedness” sets out our substantial concerns along with detailed reasons.

⁴ Section 179 of the Securities and Futures Ordinance gives the SFC the power to compel the production of records and documents from persons related to a listed company.

Takeovers matters

In Hong Kong, takeovers, mergers, privatisations and share buy-backs affecting public companies are regulated by the Codes on Takeovers and Mergers and Share Buy-backs. These codes aim to afford equal treatment of shareholders and ensure a fair and informed market as well as to mandate disclosure of timely and adequate information to enable shareholders to make informed decisions.



Following a three-month consultation on proposed amendments to the Codes on Takeovers and Mergers and Share Buy-backs, we released consultation conclusions in July and the amended codes took effect

on 13 July. Amendments included empowering the Takeovers and Mergers Panel to require compensation be paid to shareholders who have suffered as a result of a breach of these codes and increasing the threshold for independent shareholder approval for a whitewash waiver to 75%.

With effect from April 2018, a new Note was added to section 4.2 to the Introduction to the Codes on Takeovers and Mergers and Share Buy-backs to align them with the new listing regime for companies from emerging and innovative sectors.

Investigations and enquiries remained an important focus of our regulatory functions. We sanctioned two parties during the year.

In June, we publicly censured and imposed a 24-month cold shoulder order against Chan Shing. He triggered a mandatory general offer obligation when he acquired shares of Burwill Holdings Limited on the market in April 2014, but he did not make an offer.

Liang Guosheng was publicly censured and given a 24-month cold shoulder order in July. Liang triggered a mandatory general offer obligation when he acquired shares of Silver Base Group Holdings Limited on the market in July 2017, but no offer was made.

Takeovers activities

	2018/19	2017/18	2016/17
General and partial offers under Code on Takeovers and Mergers	55	59	73
Privatisations	6	11	13
Whitewash waiver applications	21	41	37
Other applications under Code on Takeovers and Mergers [^]	275	289	365
Off-market and general offer share buy-backs	9	1	4
Other applications under Code on Share Buy-backs [^]	7	0	2
Total	373	401	494

[^] Including stand-alone applications and those made during the course of a Code-related transaction.
Note: Also see Table 3 in Breakdown of SFC activity data on page 165 for more details.

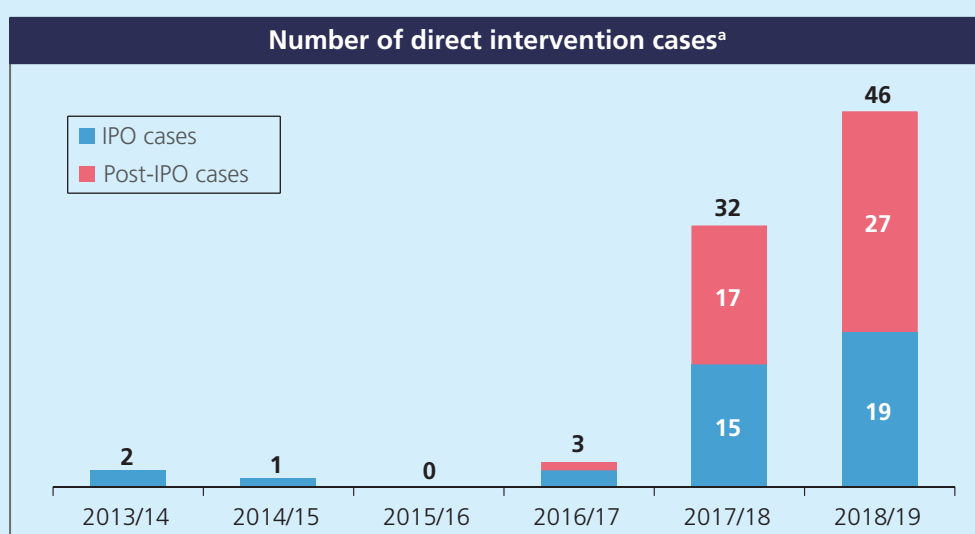
Two years into our front-loaded approach

Our front-loaded regulatory approach emphasises earlier and more targeted intervention to tackle market irregularities and protect the investing public. We closely monitor conduct and directly intervene in the listing market where necessary. We also cooperate with SEHK in joint policy actions. This approach complements our traditional enforcement actions which have been the SFC's primary response towards misconduct.

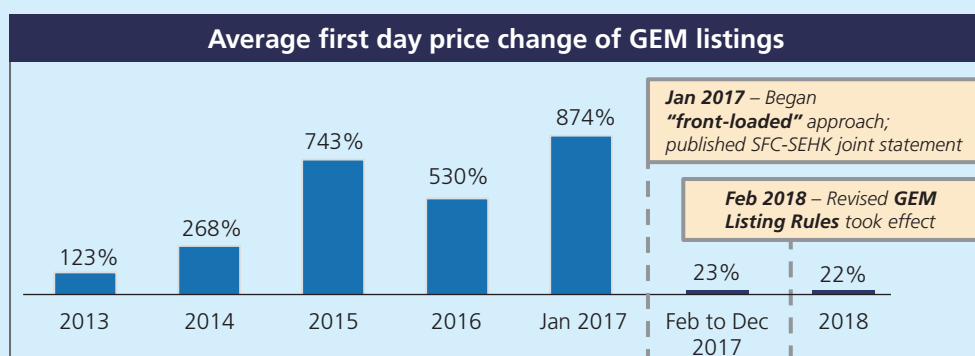
After we adopted this front-loaded approach in early 2017, the number of cases where our direct intervention involved the actual or potential use of our SMLR powers increased significantly.

We target the most serious forms of misconduct. In particular, we are concerned about harmful speculative activities, indications of which may be an exponential increase in market capitalisation over an unusually short period of time, shares trading at an inexplicably high valuation, "shell" related activities or networks of companies with complex patterns of cross-holdings.

Our direct interventions and coordinated policy actions with SEHK made it more difficult for listed companies to be used as vehicles for improper market activities. For example, we were concerned about the share price volatility of newly-listed GEM stocks. On the first day of trading, their share prices increased an average of five times in 2016 and eight times in the first month of 2017.



^a Does not include action listed in Table 7 on page 168.



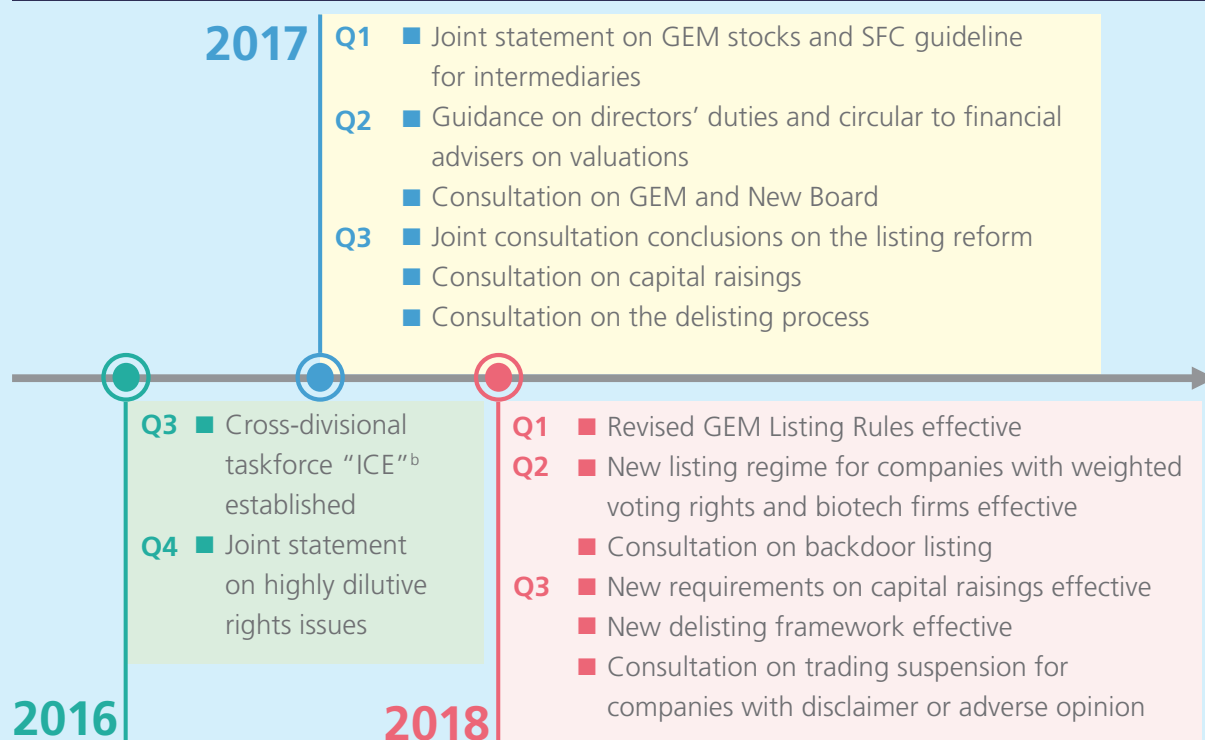
Note: Based on calendar year.

To tackle this, in January 2017 we issued guidance materials with SEHK and explained the requirements for having an adequate spread of shareholders and a fair and orderly market for new listings. We also took regulatory action, conducting investigations and exercising our SMLR powers. As a result, we observed a significant decrease in the volatility of newly-listed GEM stocks.

In recent years, we have seen highly dilutive rights issues and open offers structured or conducted in a manner which appeared to be against the

interests of minority shareholders. After discussions with us, SEHK introduced a series of measures to address this. Coupled with the SFC's front-loaded approach, the result was a substantial drop in the number of these transactions. In addition, there were fewer deeply-discounted share placements, an area where the SFC often directly intervened.

Key milestones



^b The Intermediaries, Corporate Finance and Enforcement divisions.

Green finance

Hong Kong is uniquely situated to contribute to global developments in green finance and the creation of a green financial ecosystem. Building an environmentally-friendly, low-carbon and climate change-resilient economy will be essential for a sustainable future.

During the year, we collaborated with regulators, the industry and other stakeholders to promote our initiatives to help develop Hong Kong as a leading green finance centre. In September 2018, we published our *Strategic Framework for Green Finance*, setting out a five-pronged strategy which goes beyond Hong Kong's current focus on green bonds and is aligned with global market and regulatory developments.

We launched a dedicated section on our website in May 2019 to provide information, including circulars, statistics and resources, related to this strategy as well as other green finance initiatives in Hong Kong.

Corporate disclosure

To allocate capital efficiently, investors must have the best information about the potential financial risks which climate change poses to businesses. As our top priority, we have been working with Hong Kong Exchanges and Clearing Limited (HKEX) to improve listed companies' reporting of environmental information, with an emphasis on climate-related risks and opportunities.

The SFC signed up as a supporter of the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD), which help companies identify and report the potential financial impact of climate-related risks and opportunities on their businesses. HKEX recently updated its guidance on environmental, social and governance (ESG) reporting, taking into account the TCFD recommendations.



Chief Executive Officer Mr Ashley Alder at the European Commission's High-Level Conference on Sustainable Finance

Photo: European Commission

ESG investing

Green asset managers have to do more than simply claim that they take ESG into account. To help us consider ways for asset managers to make clear to investors how environmental and climate-related risks are factored into their investment processes and risk assessments, we conducted a survey of the ESG investment practices of asset managers and asset owners. The results will be considered along with global developments when we formulate new policies.

Green-related investments

We have seen a notable increase in the number of applications we receive for funds with a green or sustainability focus. To foster the development of these fund products in Hong Kong, we issued a circular to provide guidance which will make disclosures by SFC-authorised green funds more transparent and comparable. We will also feature a central database of these funds on the SFC's website to increase their visibility.

In addition, we work closely with HKEX to develop and promote the listing and trading of green financial products including bonds, indices and derivatives. HKEX is also developing a green finance regime which will enable environmentally-aligned companies to obtain sustainable financing at a lower cost.

International cooperation

We actively participate in international initiatives with the aim of building a global, coordinated approach to green finance and promoting Hong Kong as a global green finance hub. Hong Kong is well placed to complement mainland China's comprehensive framework for green finance and to connect green finance flows between the Mainland and the rest of the world. Our strategic framework accords with the Outline Development Plan for the Guangdong-Hong Kong-Macao Greater Bay Area.

We are part of the Network for Greening the Financial System, which aims to strengthen global efforts to enhance the financial system's role in managing risks and mobilising capital for green and low-carbon investments in line with the goals of the Paris Agreement. Within the United Nations Framework Convention on Climate Change, the Paris Agreement, which came into force in 2016, calls for making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.

The SFC also takes part in the International Organization of Securities Commissions' Sustainable Finance Network and the Advisory Group of the United Nations Sustainable Stock Exchanges Initiative. Our Chief Executive Officer Mr Ashley Alder participated in the European Commission's High-Level Conference on Sustainable Finance in March 2019.

In May 2019, we hosted a high-level regulatory meeting in Hong Kong for senior officials from the Mainland, Hong Kong and the European Union to discuss the harmonisation of green finance efforts and standards.



Ms Julia Leung, Deputy Chief Executive Officer and Executive Director of Intermediaries, addresses the Hong Kong Chinese Enterprises Association

Financial education

Raising investor awareness of green finance and related investment matters is another part of our agenda and we work with the Investor and Financial Education Council (IFEC) to achieve this. IFEC launched a dedicated web page on The Chin Family website to introduce green finance to the general public.

Greening the SFC

To support green investments, our Investment Committee enquires in detail how and to what extent the external managers of our financial reserves incorporate ESG principles into their investment and risk analysis processes. Inside the organisation, we step up our green practices and promote awareness of the importance of environmental protection¹.



¹ See Corporate Social Responsibility on pages 84-91.

Markets

To ensure orderly markets, we supervise and monitor exchanges and clearing houses in Hong Kong. We also work to improve market infrastructure and strengthen Hong Kong's role as the premier risk management centre for Mainland risk and a booking hub for Asian derivatives.

Supervision of HKEX

On-site inspection

As part of our regular on-site inspections of the non-listing-related operations of Hong Kong Exchanges and Clearing Limited (HKEX), we completed an inspection of its cash market clearing operations in 2018 and recommended improvements. We began an inspection of its futures exchange trading and clearing operations in 2019.

Recognised clearing houses

We worked with HKEX to implement risk management initiatives to improve the resilience of its clearing houses in Hong Kong and their compliance with international standards. We approved proposals to enhance the admission criteria for clearing participants, the process for managing clearing participants' defaults and recovery plans for dealing with extreme market situations.

Following our approval, HKEX introduced measures to strengthen the clearing guarantee funds, including risk-based contributions from the clearing houses.

New products

We approved five derivative products proposed by HKEX to meet the trading and hedging needs of market participants.

New derivative products approved

	Trading commencement date
MSCI Asia ex Japan Index Futures	11 June 2018
Hang Seng Index (Gross Total Return Index) Futures Hang Seng Index (Net Total Return Index) Futures Hang Seng China Enterprises Index (Gross Total Return Index) Futures Hang Seng China Enterprises Index (Net Total Return Index) Futures	5 November 2018

Mutual market access

Stock Connect

In April 2018, the SFC and the China Securities Regulatory Commission (CSRC) jointly announced a fourfold increase in the daily quotas for Mainland-Hong Kong Stock Connect to RMB52 billion for each of the northbound links and RMB42 billion for each of the southbound links. The new quotas took effect on 1 May 2018.

Stock Connect covered 1,321 Mainland stocks (580 companies listed in Shanghai and 741 companies listed in Shenzhen) and 479 Hong Kong stocks as of end-March 2019, representing 88% of market capitalisation in Hong Kong, 84% in Shanghai and 73% in Shenzhen.

As of end-March 2019, southbound trading reached a cumulative net inflow of RMB700.5 billion and international investors bought in RMB767.1 billion worth of A-shares through northbound trading.

During the year, Stock Connect accounted for a steady share of Hong Kong's market turnover. On average, daily southbound trading was around 6% of total trading, similar to the proportion in 2017. Northbound trading increased to 3% of the Mainland's total market turnover, compared to 1% in 2017.

We worked with the CSRC to implement an investor identification regime for northbound trading under Stock Connect on 26 September 2018. This facilitates market surveillance of northbound trades by the Mainland exchanges and regulators. We target to introduce a similar model for southbound trading in mid-2019.

Bond Connect

After a consultation with the SFC, Bond Connect Company Limited¹ introduced the Primary Market Information Platform in February 2019. As the first English-language portal disseminating information about the Mainland primary bond market, the platform provides timely and reliable information to global investors about new bond issues.

Bond Connect experienced strong growth during the year. Total funds flowing into the Mainland interbank bond market through Bond Connect reached RMB222 billion in 2018, up from RMB132 billion in 2017. Average daily trading increased to RMB3.6 billion in 2018 from RMB2.2 billion in 2017.

OTC derivatives

In line with the G20's commitment to reform the over-the-counter (OTC) derivatives market, an OTC derivatives regime is being implemented in phases in Hong Kong. In June 2018, we concluded a joint consultation with the Hong Kong Monetary Authority on mandating the use of Legal Entity Identifiers² for

the reporting obligation and expanding the clearing obligation. We also adopted the proposed process to determine for which products it may be appropriate to introduce a platform trading obligation.

We use the data reported to the Hong Kong Trade Repository to monitor OTC equity derivatives of securities listed in Hong Kong. This allows us to assess more effectively the systemic risks to the Hong Kong securities market arising from both the on-exchange and off-exchange derivatives markets. As of end-March 2019, the estimated notional value of the OTC equity derivatives of securities listed in Hong Kong was comparable to that of exchange-traded counterparts. This was in line with major overseas markets.

Uncertificated securities market

In January 2019, we launched a consultation jointly with HKEX and the Federation of Share Registrars Limited proposing a revised operational model for implementing an uncertificated, or paperless, securities market in Hong Kong (see sidebar below).

Going paperless

The SFC is working to introduce a paperless securities market in Hong Kong.

In January 2019, we issued a consultation paper jointly with HKEX and the Federation of Share Registrars Limited to seek the public's views on a proposed operational model which would enable investors to hold and transfer securities in their own names without share certificates or other paper documents.

Investors would enjoy a direct relationship with the listed company and better legal protection. Listed companies would have more transparency when it comes to the genuine owners of their shares.

^a Securities held through the HKEX system will be registered in the name of HKSCC Nominees Limited.

The existing nominee structure within the clearing and settlement infrastructure would be preserved^a, which means that investors who want to hold a beneficial interest in securities through brokers and banks may continue to do so.

The digitisation of securities holdings and removal of paper and manual processes will help make post-trade settlement and servicing more efficient. This makes our markets more dynamic and globally competitive.

After the enactment of legislation, implementation is expected to be conducted in phases from 2022.

¹ Bond Connect Company Limited is an authorised automated trading services provider facilitating the operation of Bond Connect.

² A unique 20-digit, alpha-numeric code which identifies entities in a financial transaction.

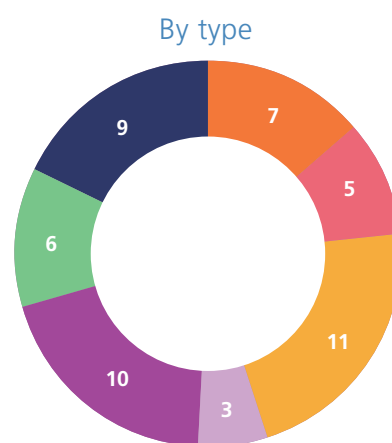
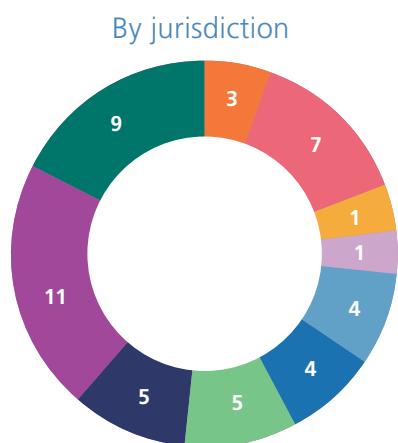
Markets

Automated trading services

Under the Securities and Futures Ordinance (SFO), two regimes regulate automated trading services (ATS) providers. Typically, those that offer facilities similar to those of a traditional exchange or a clearing house are authorised under Part III of the SFO. Intermediaries which provide traditional dealer functions along with ATS as an added facility (eg, operating a dark pool or a pre-IPO trading platform) are expected to be licensed under Part V of the SFO.

Over the past year, we approved eight applications from overseas regulated exchanges and bond trading platforms. Trades conducted on authorised trading venues were mainly in benchmark index futures and options, commodity futures, bonds, equities and exchange-traded funds offered by overseas exchanges. The average daily trading volume of futures contracts originating from Hong Kong was about 348,000 contracts for the 12 months ended 31 March 2019.

ATS providers under Part III



Note: One ATS provider is both a financial futures exchange and a central counterparty.

ATS providers

	As at 31.3.2019	As at 31.3.2018	As at 31.3.2017
Under Part III	50	57	49
Under Part V	24	24	24

Short position reporting

	As at 31.3.2019	As at 31.3.2018	As at 31.3.2017
Market value of short positions as a percentage of market capitalisation of reported securities	1.5%	1.5%	1.4%

Enforcement

We take firm and prompt action to combat crime and misconduct in the securities and futures markets, focusing on high-impact cases which pose the greatest risks to the investing public. Through proactive enforcement, we send strong deterrent messages whilst ensuring fairness and integrity.

Our tools under the SFO

We use the full spectrum of sanctions and remedies available to us under the Securities and Futures Ordinance (SFO), including through criminal, administrative, compensatory and disciplinary actions.

We have broad powers to hold directors and individuals responsible for misconduct committed by the companies they manage. We can discipline licensed intermediaries through reprimands, fines¹ and suspensions or revocations of licences, and apply to the court for injunctive and remedial orders against wrongdoers in favour of victims.

In dealing with market misconduct, such as insider dealing and market manipulation, we can also institute criminal prosecutions and bring cases directly to the Market Misconduct Tribunal (MMT).

During the year, we commenced 238 investigations and laid 42 criminal charges against four individuals and one corporation and secured convictions against four persons and one corporation.

We obtained disqualification and restorative orders against one person and seven corporations. Civil actions seeking financial redress and other remedial orders against 101 persons and corporations in 23 cases are pending before the court.

Disciplinary action was taken against 14 persons and 21 corporations. In addition, we commenced three cases before the MMT against three corporations and nine persons for suspected market misconduct or late disclosure of inside information.

We also issued 234 compliance advice letters to address areas of regulatory concern and raise standards of conduct and compliance in the industry.

Market surveillance

On a daily basis, we monitor trading on The Stock Exchange of Hong Kong Limited (SEHK) and the Hong Kong Futures Exchange Limited and conduct preliminary inquiries to detect possible market manipulation or insider dealing. We also engage with firms to review how they perform their monitoring and surveillance.

Our work in figures



[^] These requests were made to intermediaries as a result of our surveillance of untoward price movements and turnover.

¹ Fines paid by intermediaries in disciplinary actions go into the general revenue of the Government.

Enforcement

Through an organisation-wide Market Intelligence Programme, we use the latest technologies to identify conduct risks in our markets, including potential misconduct by interconnected parties. Data collected from our operations and public sources is analysed to isolate patterns and connections between individuals, companies and transactions which may indicate conduct risks.

Our surveillance of untoward price and turnover movements resulted in 9,074 requests for trading and account records from intermediaries. We also received 192 notifications from intermediaries² regarding suspicious equity and derivative trading.

We posted 10 announcements on our website reminding the investing public to exercise caution when trading in shares of listed companies where a small number of shareholders hold a high concentration of shares.

IPO sponsor failures

Initial public offering (IPO) sponsor misconduct is a top enforcement priority. Our enforcement actions help improve the standards of sponsors' due diligence and ensure they perform their gatekeeping role properly and diligently. During the year, we disciplined seven sponsor firms and three sponsor principals and imposed fines totalling \$867.7 million.

- We reprimanded and fined UBS AG and UBS Securities Hong Kong Limited a total of \$375 million for failing to discharge their obligations as a joint sponsor of China Forestry Holdings Company Limited³, Tianhe Chemicals Group Limited⁴ and another listing application⁵. We also partially suspended UBS Securities' licence to advise on corporate finance for one year, during which it cannot act as a Hong Kong IPO sponsor.
- We also suspended the licence of Cen Tian⁶ for two years for failing to discharge his supervisory duties as a sponsor principal in China Forestry's listing application.

- We reprimanded and fined Standard Chartered Securities (Hong Kong) Limited \$59.7 million for failing to discharge its obligations as a joint sponsor of China Forestry's listing application. It failed to conduct reasonable due diligence of core aspects of China Forestry's business, including its forestry assets.
- We banned Joseph Hsu Kar Hing, a former Standard Chartered responsible officer, from re-entering the industry for three years for failing to discharge his duties as a sponsor principal and a responsible officer.
- We reprimanded and fined Morgan Stanley Asia Limited \$224 million and Merrill Lynch Far East Limited \$128 million for failing to discharge their obligations as joint sponsors of Tianhe's listing application. They failed to follow the guidelines for due diligence interviews, allowed Tianhe to control the due diligence process and failed to take appropriate steps to address red flags.
- We reprimanded and fined Citigroup Global Markets Asia Limited \$57 million for failing to conduct adequate and reasonable due diligence on Real Gold Mining Limited's customers and properly supervise its listing application.
- We reprimanded and fined CCB International Capital Limited \$24 million for failing to discharge its duties as the sole sponsor in the listing application of Fujian Dongya Aquatic Products Co., Ltd. CCB failed to conduct reasonable due diligence and keep a proper audit trail of its work.
- We suspended the licence of Wu Yinong, a former responsible officer of China Merchants Securities (HK) Co., Limited, for 18 months for failing to discharge his duties as a sponsor principal in a listing application.

² Intermediaries are required to report clients' suspected market misconduct to the SFC under the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

³ Trading in China Forestry shares was suspended in January 2011. The company was wound up and the listing of its shares was cancelled in February 2017.

⁴ Tianhe was listed on the Main Board in June 2014 and trading in its shares was suspended in March 2015. The SFC directed SEHK to suspend all dealings in the shares of Tianhe in May 2017.

⁵ Details will not be disclosed until the SFC's disciplinary proceedings against other parties involved in this listing application are concluded.

⁶ A former sponsor principal and executive of UBS AG and a licensed representative of UBS Securities Hong Kong.

Safeguarding evidence

Our Evidence Management System team, part of our Enforcement Division, is entrusted with the management and safekeeping of materials related to about one thousand active SFC cases.

To collect evidence in our investigations against market misconduct, we searched more than 300 corporate and residential premises in about 50 operations over the last two years. About 5,000 items of evidence, including a large number of mobile phones, computers and other digital electronic devices, were seized.

Inside our exhibit rooms, rows of shelves are lined with thousands of items sealed in plastic, from paper documents to computer consoles. Many will be used as evidence in court.

Items are transferred between the exhibit rooms and the SFC's headquarters. When a case is closed, exhibits are returned to their owners or moved to a warehouse for storage. Inventory controls ensure that everything is accounted for.

"We made sure that nothing was lost when moving office five times over the past eight years," related Edmund Lee, Senior Administrator. During this time, the exhibit rooms expanded from 500 square feet to more than 3,000 square feet as a result of our increased caseload.

With advances in technology, the SFC has moved away from paper-based systems to keep in step with new trends in digital evidence management. "One of our greatest satisfactions was getting the

evidence management system up and running from scratch," Teresa Ho, Officer, said. Every exhibit is digitally scanned and labelled with a barcode for easy access and tracking.

The team also oversees four forensic labs to reproduce digital evidence from computers, mobile phones and other devices seized by SFC investigators. "The digitalisation of exhibits certainly helps," added Johnny Ho, Manager. "But it still takes great attention to detail and meticulousness to do our job right."

"The team is vested with the responsibility of preserving the chain of evidence, so even if search operations finish late, the team would stay well into the night to handle the new items seized and ensure they are under safe custody," said Irene Tse, Senior Administrator. "This reflects the team's professional commitment which is the SFC's core value."



From left: Teresa Ho, Edmund Lee, Johnny Ho, Irene Tse

Enforcement



Mr Thomas Atkinson, Executive Director, Enforcement, speaks at 2018 Refinitiv Pan Asian Regulatory Summit

Corporate fraud and misbehaviour Director misconduct

We commenced MMT proceedings against Li Kwok Cheong and Li Han Chun, respectively former chairman and chief executive officer of China Forestry, for suspected disclosure of false or misleading information in the company's IPO prospectus and subsequent financial reports, inducing transactions in the company's shares. We also commenced MMT proceedings against Li Han Chun and his investment vehicle Top Wisdom Overseas Holdings Limited for suspected insider dealing in the company's shares.

We commenced civil proceedings under section 214 of the SFO to seek disqualification orders against the following senior executives of listed companies:

- Duncan Chiu and Derek Chiu, two former directors, and Michael Lui Hung Kwong, former senior officer, of Far East Holdings International Limited. This followed an investigation into Far East's transfers of \$61 million from the company's bank accounts to the personal bank accounts of the then chairman Deacon Chiu Te Ken⁷ purportedly for the subscription of IPO shares on behalf of Far East. The SFC alleged, among other things, that Duncan and Derek Chiu, together with Lui, conducted the company's business or affairs in a manner involving defalcation, misfeasance or other misconduct.

- Joseph Lau Chi Yuen, the former chairman and executive director of Luxey International (Holdings) Limited, and Chung Man Wai, the company's former chief executive officer and executive director, for allegedly conducting the company's business or affairs in a manner involving fraud, misfeasance or other misconduct. The SFC alleged that Lau might have obtained a profit in a very substantial acquisition by Luxey.

The Eastern Magistrates' Court convicted and fined DBA Telecommunication (Asia) Holdings Limited and its former director Chan Wai Chuen for making a false or misleading statement in its results announcement published in 2013.

Failure to disclose inside information

We commenced proceedings in the MMT against the following companies and persons for allegedly failing to disclose inside information as soon as reasonably practicable:

- Fujikon Industrial Holdings Limited and two of its directors⁸.
- Magic Holdings International Limited and its nine directors⁹.
- Health and Happiness (H&H) International Holdings Limited¹⁰ and Luo Fei, its chairman, chief executive officer and executive director.
- CMBC Capital Holdings Limited¹¹ and its six former directors and senior executives¹².



Evidence Management System team

⁷ The late father of Duncan and Derek Chiu.

⁸ Yeung Chi Hung and Chow Lai Fung.

⁹ Stephen Tang Siu Kun, She Yu Yuan, Luo Yao Wen, Cheng Wing Hong, Sun Yan, Chen Dar Cin, Yan Kam Tong, Yang Rude and Dong Yin Mao.

¹⁰ Formerly known as Biostime International Holdings Ltd.

¹¹ Formerly known as Mission Capital Holdings Limited.

¹² Philip Suen Yick Lun (former chief executive officer and company secretary), Paul Suen Cho Hung (former chairman), Lau King Hang (former executive director) and three former independent non-executive directors, Huang Zhencheng, Weng Yixiang and Wong Kwok Tai.

Insider dealing and market manipulation

- The Court of Final Appeal (CFA) allowed the SFC's appeal against the MMT's findings that two former executives of Asia Telemedia Limited¹³, Charles Yiu Hoi Ying and Marian Wong Nam, had not engaged in insider dealing. The CFA set aside the orders made by the Court of Appeal (CA) and the MMT and remitted the matter back to the MMT to deal with sanctions.
- The CFA dismissed the appeal of Eric Lee Kwok Wa, a solicitor, and his sisters, Patsy Lee Siu Ying and Stella Lee Siu Fan against the judgment of the CA, thereby affirming the original determination that they had engaged in fraudulent or deceptive conduct in transactions involving the shares of Taiwan-listed Hsinchu International Bank Company Limited.
- The CA allowed our appeal against the decision of the MMT that Cheng Chak Ngok, former executive director, chief financial officer and company secretary of ENN Energy Holdings Limited, had not engaged in insider dealing in the shares of China Gas Holdings Limited in 2011, and ordered that the issue of dealing be remitted to the MMT for a re-trial.
- The Eastern Magistrates' Court convicted Au-Yeung Siu Pang, a former group finance manager of China CBM Group Company Limited, for two insider dealing offences. Au-Yeung was sentenced to four months of imprisonment and a fine of \$120,000.
- The MMT found that Samantha Keung Wai Fun, former CEO of China AU Group Holdings Limited¹⁴, and her acquaintances Wu Hsiu Jung and Chen Kuo Chen engaged in false trading in the shares of China AU. The MMT imposed cold shoulder orders and cease and desist orders against Keung, Wu and Chen. Keung was also subject to a disqualification order.

Intermediary misconduct

During the year, we disciplined 21 corporations, four responsible officers and 10 licensed representatives, resulting in total fines of \$940 million¹⁵. Key disciplinary actions included:

Deficient selling practices

- We reprimanded and fined BOCI Securities Limited \$10 million over its internal system and control failures. It failed to comply with regulatory requirements concerning client profiling, product due diligence and suitability assessment in its sale and distribution of investment products.
- We reprimanded and fined HSBC Broking Securities (Asia) Limited \$9.6 million for systemic deficiencies in selling bonds listed under Chapter 37 of the Main Board Listing Rules. HSBC failed to conduct proper and adequate product due diligence and have an effective system in place to assess its clients' risk profiles to ensure the suitability of the recommendations or solicitations it made to them.
- We reprimanded and fined Noah Holdings (Hong Kong) Limited \$5 million for internal system and control failures in its sale and distribution of investment products.

Anti-money laundering related breaches

- We reprimanded and fined Guosen Securities (HK) Brokerage \$15.2 million for failing to comply with anti-money laundering and counter-terrorist financing regulatory requirements when handling third party fund deposits and related internal control deficiencies.



¹³ Now known as Yunfeng Financial Group Limited.

¹⁴ Now known as SkyNet Group Limited.

¹⁵ Includes \$867.7 million in fines for sponsor failures. See page 66.

Enforcement

Other disciplinary actions

Reprimanded and fined for internal control failures

Company	Breaches	Fine	Date
Hang Seng Investment Management Limited	Deficient internal controls and procedures for the cash management of SFC-authorized funds	\$3 million	31.5.2018
CN Capital Management Limited	Failure to maintain satisfactory internal controls for employee account dealing	\$1 million	24.4.2018
Instinet Pacific Limited	Deficient internal controls for its electronic and algorithmic trading systems and alternative liquidity pool	\$17.3 million	13.4.2018

Disciplined for mis-handling client money

Company/Name	Breaches	Action	Date
Kong Kar Bong	Misappropriated client money and forged an account statement	Banned from re-entering the industry for 10 years	11.12.2018
Lok Wai Fong	Unauthorised transfer of client money and failure to act on client instructions	Banned from re-entering the industry for life	8.10.2018
HPI Forex Limited	Failure to maintain client money in a segregated client account in Hong Kong and use of client money to conduct proprietary transactions overseas	Reprimanded and fined \$2 million	22.8.2018
Cham Nga Yin	Misappropriated client money	Banned from re-entering the industry for life	9.8.2018

Reprimanded and fined for other regulatory breaches

Company	Breaches	Fine	Date
FWD Life Insurance Company (Bermuda) Limited	Failure to comply with the key personnel requirements under the SFC Code on MPF Products and the Fund Manager Code of Conduct	\$2.4 million	8.1.2019
Ardon Maroon Fund Management (Hong Kong) Limited	Cross-trade failures in managing the Ardon Maroon Asia Master Fund	\$800,000	27.12.2018
SFM HK Management Limited	Failures in the short selling of Great Wall Motor Company Limited shares on behalf of a fund it managed	\$1.5 million	6.12.2018
Huatai Financial Holdings (Hong Kong) Limited	Failures in its short selling of Great Wall Motor Company Limited shares	\$800,000	17.9.2018
Citigroup Global Markets Asia Limited	Failures in the operation of its alternative liquidity pool	\$4 million	10.7.2018

Note: See Table 6 in Breakdown of SFC activity data on page 167 for details of the less significant disciplinary actions.

Other notable cases

- The CFA dismissed the appeal by Moody's Investors Service Hong Kong Limited of our disciplinary action concerning a special comment report published by Moody's in 2011.
- The CA dismissed the appeal by Andrew Left of Citron Research against the determination of the MMT on points of law under the SFO. This came after the rejection of a separate application for leave to appeal by Left against the determination of the MMT on questions of fact following the MMT's findings of misconduct in his publication of a research report on Evergrande Real Estate Group Limited in 2012.
- The CFI ordered three unlicensed entities¹⁶ to compensate 14 investors the sum of about \$600,000. These entities solicited investors to open trading accounts and invest in securities and futures products. However, no trades were executed and investors were not able to recover their money.
- Hui Kwok Piu was convicted and fined \$231,000 for illegal short selling in the shares of Coslight Technology International Group Limited.
- We suspended the trading in the shares of China Ding Yi Feng Holdings Ltd and issued restriction notices to nine brokers¹⁷ prohibiting them from disposing of or dealing with assets held in client accounts related to suspected market manipulation in its shares. We are not investigating these brokers, which have cooperated with our ongoing investigation, and the restriction notices do not affect their operations or their other clients.

Putting the pieces together

The Case Intake Team plays a key role in ensuring we address serious threats to Hong Kong's financial markets. Set up in 2016 as part of a strategic review of the Enforcement Division, the team helps us focus on enforcement priorities and increase efficiency.

"When a case is referred to the team, we look at the facts and circumstances and weigh its importance according to our regulatory priorities, whether there is enough information and whether the problem is part of a larger issue," explained Anna Woo, Associate Director, Enforcement, who heads the team. If the senior management considers an investigation is warranted, it allocates the case to one of our specialised enforcement teams.

The team also reviews public complaints and Anna represents the Enforcement Division in our Complaints Control Committee^a. For her work in this role she received The Ombudsman's Awards 2018 for Officers of Public Organisations.

^a See Stakeholders on pages 77-81.

Cooperation and communication among team members and other colleagues have been key to her team's achievements, Anna added. "We strive to handle cases consistently and transparently and uphold the 'One SFC' approach."



Anna Woo (centre), Celeste Chong (left) and Avon Leung of the Case Intake Team

You have to look at each case with an open mind – it is like putting a puzzle together.

Anna Woo

¹⁶ Cardell Limited or Cardell Company Limited, Waldmann Asset Management and Doyle Hutton Associates.

¹⁷ The nine brokers are Futu Securities International (Hong Kong) Limited, GF Securities (Hong Kong) Brokerage Limited, Guotai Junan Securities (Hong Kong) Limited, Haitong International Securities Company Limited, Orient Securities (Hong Kong) Limited, SBI China Capital Financial Services Limited, Shenwan Hongyuan Securities (H.K.) Limited, Sun Hung Kai Investment Services Limited and Yunfeng Securities Limited.

Enforcement

Updated fining guidelines

We updated our Disciplinary Fining Guidelines in August 2018 to codify the fining principles confirmed by the Securities and Futures Appeals Tribunal in our disciplinary proceedings against HSBC Private Bank (Suisse) SA.

Under these principles, multiple culpable acts or omissions constituting misconduct may attract multiple penalties even if they are of the same generic nature. We may use the number of persons affected by the misconduct as the multiplier in assessing the appropriate penalty. The approach will depend on the facts of each case and we will look at the totality of the penalties to ensure they are not disproportionate to the gravity of the conduct in question.

Reporting misconduct

In October 2018, we conducted a campaign to raise public awareness about listed company fraud and market misconduct, as well as the importance of reporting misconduct to the SFC. We updated our "Have you seen these people?" webpage to encourage the public to help us locate individuals sought in enforcement-related inquiries or investigation.

Enforcement activities

	2018/19	2017/18	2016/17
S179 ^a inquiries commenced	26	24	27
S181 ^b inquiries commenced (number of letters sent)	294 (9,074)	261 (8,461)	301 (8,960)
S182 ^c directions issued	231	274	407
Investigations started	238	280	414
Investigations completed	243	254	591
Individuals/corporations charged in criminal proceedings	5	14	10
Criminal charges laid ^d	42	54	46
Notices of Proposed Disciplinary Action ^e issued	22	29	49
Notices of Decisions ^f issued	34	32	56
Individuals/corporations subject to ongoing civil proceedings	101	97	126
Compliance advice letters issued	234	277	548
Cases with search warrants executed	30	22	34

^a Section 179 of the SFO gives the SFC the power to compel the production of records and documents from persons related to a listed company in relation to fraud or other misconduct.

^b Section 181 of the SFO gives the SFC the power to require information from intermediaries about trading transactions, including the identity information of the ultimate clients, the particulars and instructions relating to the transactions.

^c Section 182 of the SFO gives the SFC the power to investigate SFO offences, market misconduct, fraud, misfeasance and disciplinary misconduct.

^d The SFC brought a total of 42 criminal charges against four individuals and one corporation.

^e A notice issued by the SFC to regulated persons that it proposes to exercise its disciplinary powers, on grounds that they appear to be guilty of misconduct or not fit and proper.

^f A notice that sets out the SFC's decision and its reasons to take disciplinary action against regulated persons.

Note: Also see Table 7 in Breakdown of SFC activity data on page 168 for more details.

Regulatory engagement

We actively participate in international policymaking through our involvement in global standard setting bodies. We collaborate with Mainland authorities on regulatory and market development initiatives and maintain close contact with our local regulatory counterparts.

International IOSCO

We play an active role in the International Organization of Securities Commissions (IOSCO), which develops, implements and promotes adherence to internationally-recognised standards for securities regulation. We work closely with the IOSCO Secretariat to develop policy initiatives, facilitate collaboration between IOSCO and the G20's Financial Stability Board (FSB) and promote interaction between members from emerging and developed economies.

Since his re-appointment as Chairman of the IOSCO Board in May 2018, our Chief Executive Officer Mr Ashley Alder pushed forward IOSCO's response to the European Union (EU) data privacy regulation and initiatives related to sustainable finance, cyber resilience, structural vulnerabilities in asset management, market fragmentation and financial technologies (Fintech), including risks associated with crypto-assets.

In May 2018, the SFC became one of the first signatories to the IOSCO Enhanced Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (EMMoU) for cross-border enforcement cooperation. The EMMoU provides signatories with additional tools to combat financial misconduct in the global financial markets.

With other members of IOSCO, the FSB, the Committee on Payments and Market Infrastructures (CPMI) and the Basel Committee on Banking Supervision, we participated in the Derivatives Assessment Team study of the impact of the G20 financial regulatory reforms on the incentives to centrally clear over-the-counter (OTC) derivatives.

Mr Alder co-chairs the CPMI-IOSCO Steering Group which coordinates the regulatory policy work addressing risks in derivatives markets following the



IOSCO Board meeting in Madrid, Spain

Photo: IOSCO General Secretariat

global financial crisis, including the supervision of central counterparties and the monitoring of the implementation of the Principles for Financial Market Infrastructures (FMI)¹. The SFC hosted the October 2018 CPMI-IOSCO Steering Group meeting.

Mr Alder participated in the second EU-Asia Pacific Forum in October 2018. Securities regulators representing the EU and the IOSCO Asia-Pacific Regional Committee discussed the implementation of EU regulations which have an impact on Hong Kong and the region, crypto-assets, sustainable finance and other capital market developments.

We participate in all eight IOSCO policy committees as well as the Committee on Emerging Risks, Assessment Committee, Fintech Network, Sustainable Finance Network and key task forces and working groups.

- As a member of IOSCO's Committee on Investment Management, we chaired the Committee's workstream studying the major risks associated with exchange-traded funds (ETFs) and contributed to a consultation paper on measuring leverage in investment funds.
- We participated in the Committee on Derivatives which published an Update to Survey on the Principles for the Regulation and Supervision of Commodity Derivatives Markets in October 2018 and a report on commodity storage and delivery infrastructures in February 2019.

¹ International standards for financial market infrastructures issued by IOSCO and the CPMI to strengthen financial stability.

Regulatory engagement

FSB

As Chairman of the IOSCO Board, Mr Alder is a member of the FSB's Plenary and its Steering Committee, which focus on monitoring the progress of the G20 reforms and financial vulnerabilities in the global financial system. Mr Alder also participates in the FSB Standing Committee on Supervisory and Regulatory Cooperation.

We are a member of the FSB Standing Committee on Standards Implementation and contribute to its Implementation Monitoring Network, which considers the effects of the G20 reforms and conducts thematic monitoring and peer reviews.

We are also a member of the FSB Regional Consultative Group for Asia, to which we contribute views on regulatory policies, and the FSB Cross-Border Crisis Management Group, which monitors the implementation of resolution regimes for FMIs such as central counterparties.

We worked with the Hong Kong Monetary Authority (HKMA), the Insurance Authority (IA) and the Financial Services and the Treasury Bureau (FSTB) on the FSB's annual exercise to monitor the implementation of the G20 reforms.

We participated in the FSB's OTC Derivatives Working Group which published the *OTC Derivatives Market Reforms – 13th Progress Report on Implementation* in November 2018.

Financial Action Task Force

We contributed to the *Risk-based Approach Guidance for the Securities Sector* published by the Financial Action Task Force (FATF) in October 2018.

Last year, we worked closely with the FSTB, fellow financial regulators and law enforcement agencies to complete a comprehensive self-assessment of the effectiveness of Hong Kong's anti-money laundering and counter-financing of terrorism regime and its compliance with the FATF recommendations as part of the FATF's mutual evaluation² of Hong Kong. An on-site review was carried out by the FATF assessment team in November 2018.



SFC Chairman Mr Tim Lui (left) meets CSRC Chairman Mr Yi Huiman in Beijing

Other engagement

During the year, we maintained regular dialogue with overseas regulators to share intelligence and updates on the supervision of global financial institutions. In March 2018, we co-hosted the third Asia-Pacific Regional Supervisory College with the Australian Securities and Investments Commission in Australia. We hosted a supervisory college in Hong Kong jointly with the US Federal Reserve Bank in October 2018 and also took part in other supervisory colleges held in Japan, Switzerland and the UK.

We participated in the Global Financial Innovation Network and became a member of its Coordination Group which sets its overall direction and strategy. The network, which is led by the UK Financial Conduct Authority and consists of financial regulators and related organisations, aims to create a global regulatory sandbox for firms to conduct cross-border testing of Fintech.

Mainland China

To advance Hong Kong's unique position as the international financial centre connecting Mainland and international capital flows, we take an active part in Mainland-Hong Kong cooperation programmes and hold regular high-level discussions with the China Securities Regulatory Commission (CSRC) on supervision, enforcement and market development initiatives. We also organise high-level meetings with other Mainland authorities to exchange regulatory information and strengthen cooperation.

² See footnote 1 on page 7.



High-level meeting with the CSRC in December 2018

In March 2019, our Chairman Mr Tim Lui met with the CSRC Chairman Mr Yi Huiman to discuss cooperation between the Hong Kong and Mainland capital markets.

In December 2018, the fourth half-yearly SFC-CSRC high-level meeting was held to discuss major initiatives, including supervisory and enforcement cooperation, investor identification for southbound trading under Stock Connect, ETF Connect, enhancements to Mainland-Hong Kong Mutual Recognition of Funds and full circulation of H shares. We also held two regular high-level enforcement meetings to exchange views on cross-border enforcement cooperation, market surveillance workflows and the progress of high-priority investigations.

We support the Government of the Hong Kong Special Administrative Region (HKSAR) in strengthening cooperative relationships with Mainland authorities to develop Hong Kong's financial services sector and access to Mainland markets. We actively participated in the research and policy formulation for the Outline Development Plan for the Guangdong-Hong Kong-Macao Greater Bay Area announced in February 2019. We will work closely with Mainland authorities to implement the initiatives set out in the plan, including further enhancements to the Mainland-Hong Kong mutual market access schemes.

We met with the State Administration of Foreign Exchange and received delegates from the People's Bank of China to discuss the development of offshore renminbi business in Hong Kong and other cooperation initiatives. We also engaged with Mainland exchanges and clearing houses to discuss their operations in Hong Kong and the opening-up of the Mainland futures market.

To strengthen cooperation with our fellow regulators and facilitate knowledge sharing, we co-organised a joint enforcement training programme with the CSRC on digital forensics in Shenzhen in November 2018. Over 120 enforcement officers from both organisations participated. Experts from the Economic Crime Investigation Department of the Ministry of Public Security, the Hong Kong Police and the Independent Commission Against Corruption (ICAC) also provided their insights on current trends.

Our in-house legal team maintains regular contact with the CSRC and conducts joint seminars to share experience on legal topics. The third annual seminar took place in Shenzhen in March 2019.



SFC-CSRC joint enforcement training in Shenzhen

Regulatory engagement

Local

We maintain close contact with the HKSAR Government and local counterparts to keep abreast of emerging issues and regulatory developments. We attended a meeting with the HKMA, IA and China Banking and Insurance Regulatory Commission (CBIRC) in January 2019 where we agreed to strengthen cooperation in monitoring the cross-boundary and cross-sectoral activities of regulated financial institutions.

During the year, we held workshops and training sessions with the ICAC to share best practices in investigation techniques, digital forensics and market surveillance as well as handling corporate fraud, market misconduct and disciplinary cases. The ICAC provided their training facilities for our staff to conduct mock searches and court proceedings. We partnered with the ICAC and the Police to conduct multiple large-scale search operations. We also hosted investigation workshops for officers from the ICAC, the Police and the HKMA.

Bilateral agreements

In June 2018, we signed an MoU with the German Federal Financial Supervisory Authority providing for consultation, cooperation and exchange of information in the supervision of cross-border regulated financial



Mock court hearing at ICAC training facilities

institutions in Hong Kong and Germany. We also entered into a cooperation agreement with the Abu Dhabi Global Market Financial Services Regulatory Authority to establish a framework for cooperation on Fintech.

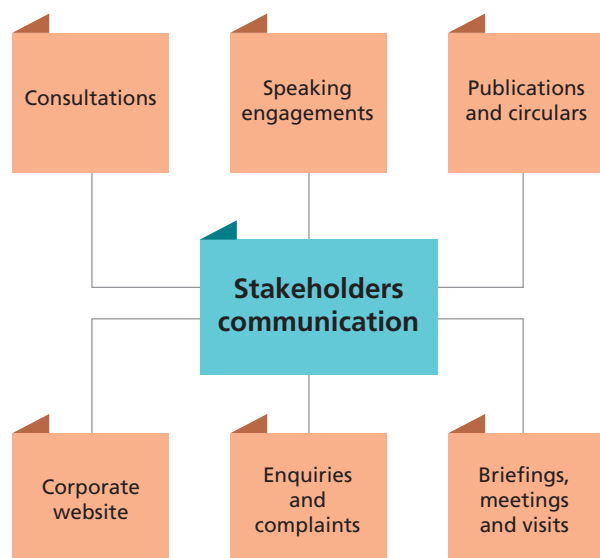
We entered into an MoU for supervisory cooperation with the CBIRC in June 2018 and with the CSRC in November 2018. The MoUs facilitate cooperation and exchanges of information in the supervision of regulated financial institutions in the Mainland and Hong Kong.

Requests for regulatory cooperation

	2018/19		2017/18		2016/17	
	Received	Made	Received	Made	Received	Made
Enforcement-related requests for assistance	113	99	136	104	155	112
Licensing-related requests for assistance	121	597	112	1,178	125	1,101

Stakeholders

To promote transparency, we strive to help stakeholders understand our work and provide them with up-to-date regulatory information through timely, concerted outreach. We engage with a wide range of stakeholders using multiple channels.



Industry

In June, we organised the SFC Compliance Forum 2018 (see sidebar on page 79), a half-day event to exchange views with the industry on current regulatory concerns. More than 500 participants from the financial industry attended.

Publications and other communications

	2018/19	2017/18	2016/17
Press releases	128	138	134
Consultation papers	5	11	4
Consultation conclusions	11	8	2
Industry-related publications	15	15	13
Codes and guidelines ^a	14	10	4
Circulars to industry	90	83	74
Corporate website average daily page views ^b	64,947	67,664	59,952
General enquiries	6,709	7,494	6,532

^a Includes updates to previous versions.

^b The average number of webpages browsed per day during the reporting period.

We maintain an open and productive dialogue with industry associations, professional bodies and other market participants. To keep industry participants informed about regulatory developments, we regularly organise meetings and briefings and from time to time contribute articles to industry association newsletters.

This year, we organised five workshops on our enhanced licensing process and three seminars on anti-money laundering for more than 2,000 participants. Our industry briefing on the Guidelines on Online Distribution and Advisory Platforms was attended by about 200 participants from industry associations and regulatory counterparts. Together with the Hong Kong Chinese Enterprises Association, we organised a workshop to brief Mainland-based firms on the latest regulatory requirements for intermediaries and listed companies in September 2018.

During the year, our senior executives took part in 85 speaking engagements on various topics within our remit. We supported 10 seminars or events organised by industry bodies.

The SFC was one of the regulatory partners supporting the Hong Kong FinTech Week 2018 Main Conference on 31 October and 1 November. Our senior executives discussed regulatory issues related to financial technology (Fintech) development and we displayed information about the SFC's Fintech initiatives at a booth on-site.

Stakeholders

When we propose rules under the Securities and Futures Ordinance, we carry out a public consultation even if it is not a statutory requirement to do so. Before implementation, we consult the public on proposed non-statutory codes and guidelines, as well as amendments to them. We issue consultation papers comprising detailed proposals and as part of the consultation process hold both formal and informal discussions to hear stakeholders' views.

After completing our analysis, we issue a consultation conclusions paper summarising the main comments received and setting out our conclusions. We published five consultation papers and 11 consultation conclusions in the year.

Our publications aim to update the industry on our regulatory work, topical issues and other developments. This year, we published 15 thematic publications, including periodic newsletters, market reviews and surveys.

Circulars and frequently-asked questions are posted on the SFC website to help the industry better understand our regulatory requirements. This year, we issued 90 circulars on a wide range of matters, including virtual assets, securities margin financing, online client onboarding, valuation of fund assets, our review of licensed firms' internal controls and updates on anti-money laundering and counter-terrorist financing.



Government

We attend Legislative Council (LegCo) meetings, including meetings of the Panel on Financial Affairs and relevant Bills Committees, to provide legislators with details of our policy initiatives, explain the rationale behind our work and answer questions. We also respond to enquiries and complaints referred to us or raised by LegCo members and other government agencies.

Through regular meetings and reports, we maintain close liaison with the Financial Services and the Treasury Bureau and provide updates on our regulatory initiatives. We also provide assistance and information to other government bureaux and departments on various issues.



Mr Ashley Alder, Chief Executive Officer, at Hong Kong FinTech Week 2018



Information booth

Regulatory counterparts

We play an active role in international regulatory cooperation through our participation in both the International Organization of Securities Commissions and the Financial Stability Board¹.

To enhance regulatory cooperation, we maintain close contact with local, Mainland and overseas regulatory counterparts. During the year, we signed six memoranda of understanding (MoU) with other regulatory authorities and held more than 30 MoU meetings. In addition, we received visitors and delegates from Mainland and overseas authorities.

SFC Compliance Forum 2018

On 21 June, we hosted the SFC Compliance Forum 2018 to exchange views with the industry on current regulatory issues. Our senior executives, along with representatives from our regulatory counterparts, the financial industry and academia, discussed a range of topics at the half-day event attended by more than 500 participants.

Ms Julia Leung, our Deputy Chief Executive Officer and Executive Director of Intermediaries, delivered opening remarks, cautioning that while the use of technology and big data may bring opportunities and enhance efficiency, the financial industry should not overlook the associated risks. The SFC also explores ways to use technology in its regulatory work to identify and assess risks, she added.

The plenary panel, moderated by Ms Leung, discussed the industry's use of innovative technologies such as artificial intelligence, machine learning, blockchain, cloud services and big data, as well as the related risks and how they intersect with the SFC's regulatory framework.



Ms Julia Leung, Deputy Chief Executive Officer and Executive Director of Intermediaries

One breakout session discussed best execution, client facilitation and alternative liquidity pools in light of the SFC's risk-based thematic reviews, and another focused on our thematic inspection of the work of initial public offering sponsors and the specific challenges they face.



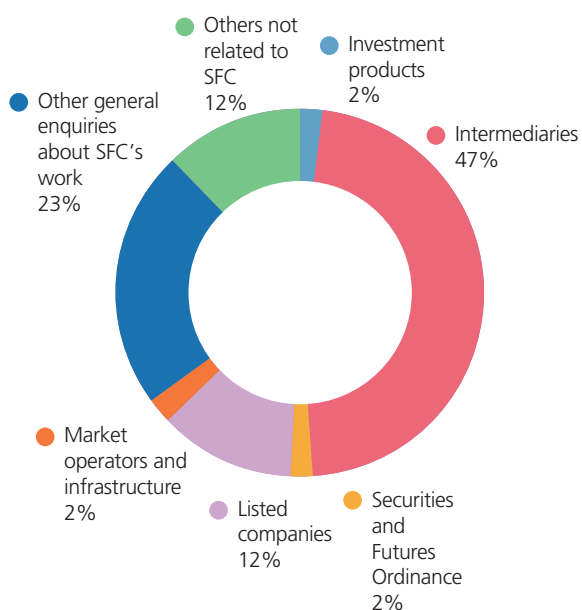
¹ See Regulatory engagement on pages 73-76.

Stakeholders

The public

We address public concerns and enquiries regarding the securities and futures markets. During the year, we received a total of 6,709 general enquiries by phone or in writing.

General enquiries



We handled 6,034 complaints during the year. Complaints against intermediaries and market activities are first reviewed by our Complaints Control Committee, comprising senior executives from across the organisation, and are allocated to responsible divisions for assessment where appropriate.



SFC Chairman Mr Tim Lui (second from the left) at HKEX's ceremony to mark the Lunar New Year's first trading day

A total of 1,596 cases² were allocated for further review and 624 were referred to HKEX³ or other financial regulators and law enforcement agencies.

To increase public understanding of Hong Kong's financial regulatory framework and our role in it, we received visitors from local and overseas institutions and our senior executives delivered key messages in media interviews. We issued 128 press releases to inform the public of the latest regulatory actions and other SFC news.

We published our *Annual Report 2017-18* and three quarterly reports to help stakeholders understand our work. Our reporting efforts were recognised with a Gold Award in the Hong Kong Management Association's Best Annual Reports Awards 2018, and a Gold Award, public sector category, in the Hong Kong Institute of Certified Public Accountants' 2018 Best Corporate Governance Awards.

The public can easily obtain up-to-date information about our work and regulations on our corporate website. This year, we redesigned our homepage and made several sections more easily accessible via mobile and tablet devices as well as by the visually impaired.

² One case may comprise multiple complaints.

³ Hong Kong Exchanges and Clearing Limited.

Complaints against intermediaries and market activities

	2018/19	2017/18	2016/17
Conduct of licensees	453	357	411
Conduct of registered institutions	16	22	39
Listing-related matters and disclosure of interests	3,485	779	739
Market misconduct ^a	364	322	221
Product disclosure	8	12	8
Unlicensed activities	164	141	116
Breach of offers of investments	30	48	141
Boiler rooms and suspicious websites	378	319	330
Scams and frauds ^b	285	186	132
Other financial activities not regulated by SFC ^c	851	503	185
Total	6,034	2,689	2,322

^a Primarily, alleged market manipulation and insider dealing.

^b Such as identity fraud and impersonation.

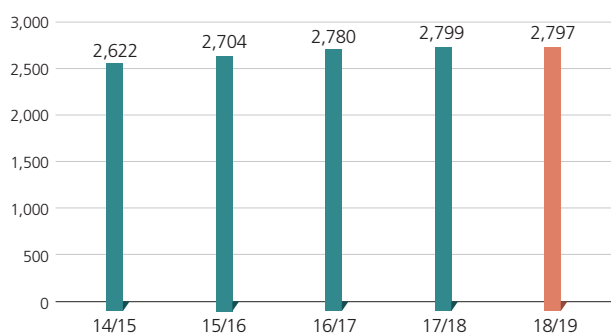
^c For example, bullion trading, banking complaints.



SFC activity data

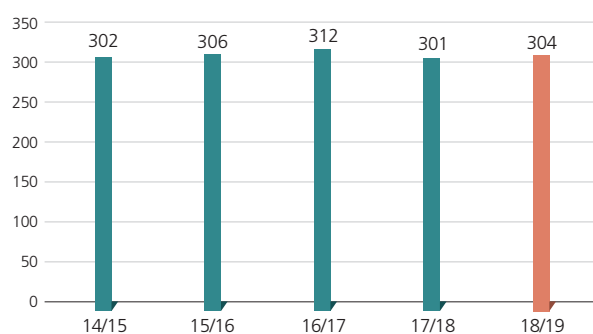
These charts are intended to show at a glance some top-line data on our activities. See Breakdown of SFC activity data on pages 164-169 for more details.

Authorised collective investment schemes

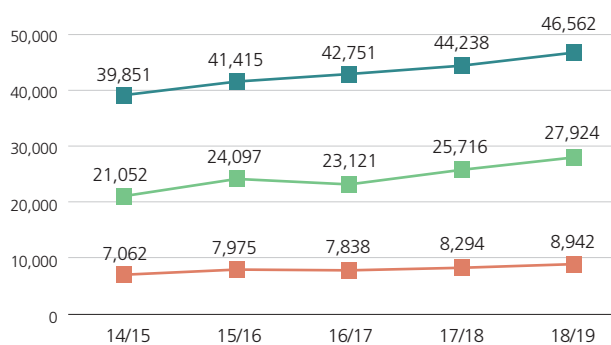


Note: Figures represent a snapshot view as at each financial year-end.

On-site inspections of intermediaries

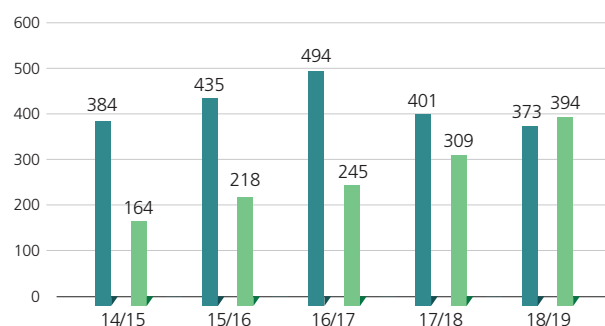


Licensing



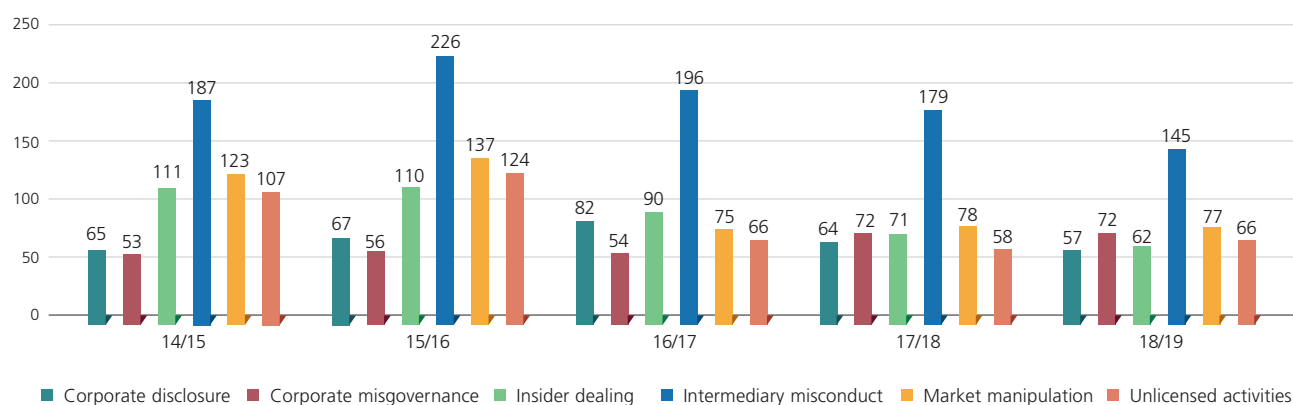
■ Total number of SFC licensees as at each financial year-end
 ■ Applications to conduct new regulated activity
 ■ Applications for SFC licences

Takeovers and listing applications

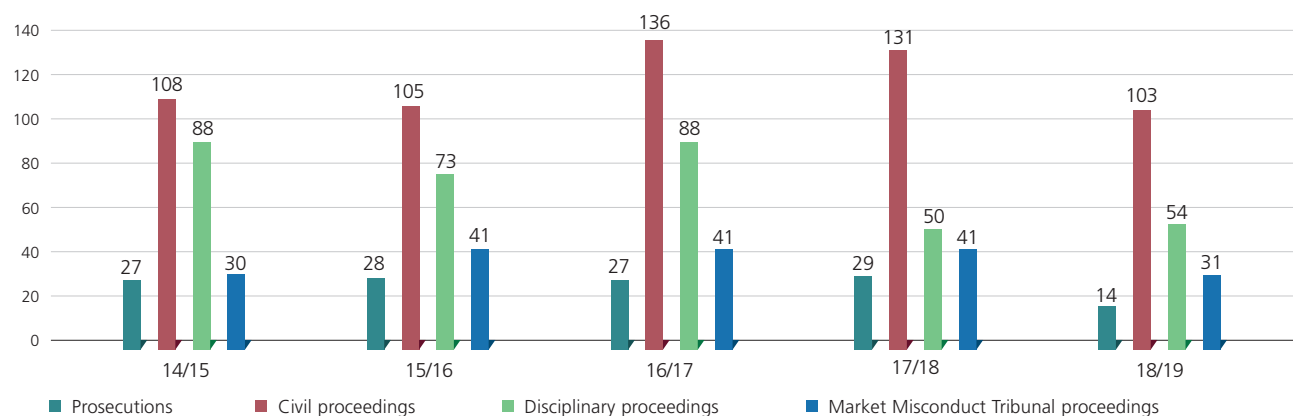


■ Takeovers and share buy-backs transactions handled
 ■ Listing applications received

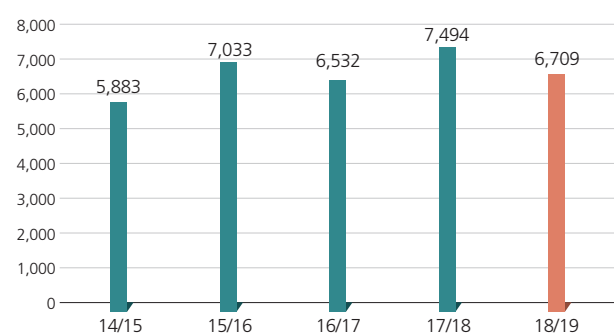
Investigations



Persons/corporations subject to enforcement action



General enquiries



Complaints against intermediaries and market activities

