SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

Consultation Conclusions on Proposed Amendments to Enforcement-related Provisions of the Securities and Futures Ordinance

August 2023

Contents

Executive summary

1. In June 2022, the Securities and Futures Commission (**SFC**) issued the Consultation Paper on Proposed Amendments to Enforcement-related Provisions of the Securities and Futures Ordinance (**SFO**). The objective of the proposed amendments is to enable the SFC to better protect the interests of the investing public and uphold the reputation of Hong Kong's financial markets through more effective enforcement action.

2. The consultation ended in August 2022. A total of 27 written submissions were received, including from various industry associations, law firms, professional bodies and individuals. A list of respondents (other than those who requested anonymity) is set out in Appendix A.

3. A majority of the respondents raised concerns about the proposed amendments to sections 213 and 103(3)(k) of the SFO. Respondents generally supported the proposed amendments to the insider dealing provisions of the SFO.

4. The key comments and the SFC's responses can be found in the section starting on page 5.

<u>Part 1 – Amendments to section 213 of the SFO to expand the basis on which the SFC may apply for remedial and other orders against a regulated person</u>

5. Many respondents commented on the legal and implementation issues that these proposed amendments would likely cause. Their comments can be divided into five major themes: (i) legal and jurisprudence concerns when a breach of non-statutory SFC codes or guidelines may give rise to legal remedies; (ii) implementation issues arising out of the perceived conflation of the disciplinary regime and section 213; (iii) fairness and proportionality concerns; (iv) the impact of the amendments on the competitiveness and status of Hong Kong as an international financial centre; and (v) the need for a broader and more holistic review of compensation orders as a remedy in Hong Kong.

6. We reiterate that the policy objective of the proposal is to enhance the remedies to protect the investing public in situations where the SFC cannot directly require regulated persons in breach of SFC codes or guidelines to compensate aggrieved clients or for the SFC to seek redress for these investors through section 213 proceedings. However, we acknowledge the complexities raised by the respondents, which warrant our further consideration.

7. Therefore, we believe the preferred course is to put the proposal on hold. We will further assess the adequacy of the current avenues for seeking financial redress by or for aggrieved investors and study a full range of other options to meet our policy objective.

<u>Part 2 – Amendments to exemptions in section 103 of the SFO</u>

8. Many respondents expressed concerns about the proposal to amend the professional investor exemption in section 103(3)(k) of the SFO. These comments can be broadly categorised into two concerns: (i) the necessity of the amendments; and (ii) operational difficulties and the impact of the amendments on business development and marketing processes.

9. We reiterate that the policy objective of the proposal is to enhance investor protection by limiting retail investors' exposure to unauthorised advertisements of investment products intended for professional investors and by reducing the risk of the professional investor exemption being abused by issuers of advertisements. However, we note the practical difficulties in implementing this proposal as highlighted by the respondents and acknowledge that the potential benefits of this proposal need to be considered against these difficulties.

10. After reassessing this proposal, we have decided not to proceed with it in its current form. We remind the industry that anyone who wishes to invoke the professional investor exemption in section 103(3)(k) should be able to demonstrate a clear intention to dispose of the investment product only to professional investors. In our view, to demonstrate this intention, at a minimum, the issuer of an advertisement should ensure it is plainly apparent from the face of the advertisement that the investment product is intended only for disposal to professional investors.

Part 3 – Amendments to the insider dealing provisions of the SFO

11. Most respondents expressed their support for this proposal and we will proceed with the amendments to the insider dealing provisions of the SFO. Several respondents sought clarification of the scope and applicability of the proposed amendments which are set out in detail in paragraphs 58 and 61 below.

12. We note that some respondents requested the publication of the draft language of the amendments in order for them to properly assess and analyse the impact of the amendments. The industry will have the opportunity to review the draft amendments during the legislative process.

Concluding remarks and next steps

13. The SFC will proceed with the proposal to amend the insider dealing provisions of the SFO.

14. We would like to thank all respondents and the industry for their time and effort in providing us with their detailed comments on the proposals in the consultation.

15. The consultation paper, the responses (other than those from respondents who requested their responses be withheld from publication) and this paper are available on the SFC website at www.sfc.hk.

Comments received and the SFC's responses

Section 1 – Amendments to section 213 of the SFO to expand the basis on which the SFC may apply for remedial and other orders against a regulated person

Question 1:	Do you agree with: (i) the proposal to amend section 213 of the SFO to expand the basis on which the SFC may apply to the Court of First Instance (**CFI**) for remedial and other orders after having exercised any of its powers under section 194 or 196 of the SFO against a regulated person, and; (ii) the proposed consequential amendments to section 213(1), (2), (7) and (11)? Please explain your view.
Question 2:	Do you have any comments on the proposed consequential amendments to section 213(3A) in respect of open-ended fund companies (**OFCs**)? Please explain your view.

16. Many respondents expressed concerns about the amendments to section 213 to expand the basis on which the SFC may apply for remedial or other orders against a regulated person. There are five major themes across the responses: (i) legal and jurisprudence concerns when a breach of non-statutory SFC codes or guidelines may give rise to legal remedies; (ii) implementation issues arising out of the perceived conflation of the disciplinary regime and section 213; (iii) fairness and proportionality concerns; (iv) the impact of the amendments on the competitiveness and status of Hong Kong as an international financial centre; and (v) the need for a broader and more holistic review of compensation orders as a remedy in Hong Kong.

<u>(i) Legal and jurisprudence concerns</u>

Public comments

17. Respondents questioned whether it is right as a matter of jurisprudence to empower the SFC to seek legal remedies in the form of court orders for a breach of codes and guidelines which do not themselves have the force of law, and the formulation of which was not subjected to the same scrutiny as legislation. Some respondents noted that the SFC's codes and guidelines are principle-based and broad, and their primary purpose is to serve as guidance on the practices and standards expected of licensed firms. This contrasts with legislation, which spells out specific acts of misconduct. Therefore, some respondents believe this proposal would introduce significant legal and regulatory uncertainty for regulated persons. A number of respondents also cited section 399(6) which specifies that any failure to comply with the provisions of any codes and guidelines does not provide a right of action, demonstrating the intent of the legislature that breaches of regulatory guidance should be treated differently to breaches of statute.

The SFC's response

18. Whilst we understand the concerns relating to making any breach of codes and guidelines a cause of action under section 213 and the availability of legal remedies for these breaches, we do not believe this proposal would fundamentally alter the status of

the SFC's codes and guidelines issued under the SFO as suggested by some respondents.

19. The current law already allows the SFC to seek section 213 orders for breaches of licensing conditions which do not have the force of law. Furthermore, while codes and guidelines contain general principles with which regulated persons must comply, they also set out specific requirements for regulated persons in the conduct of their business dealings with clients. The proposed introduction of the exercise of disciplinary powers (after a finding of a breach of codes or guidelines is established) as a ground on which the court may exercise its discretion to order remedial measures for aggrieved clients does not fundamentally alter the nature of the available grounds in section 213. The legislative intent of section 213 has always been to allow the court to exercise its discretion and order relief as it considers it necessary to protect investors adversely affected by others' misconduct (in a general sense of that word), whether in the form of a breach of a statutory provision or a condition of a licence. With respect to the apparent contradiction between the proposed amendments to section 213 and the current language of section 399(6), we consider that allowing legal consequences to flow from breaches of codes and guidelines does not mean we are changing the legal status of the codes and guidelines. If we had decided to go ahead with this proposal, consequential amendments would be made to section 399(6) to align the two provisions and avoid inconsistencies between them.

<u>(ii) Implementation and practical issues arising from perceived conflation of the disciplinary regime and section 213</u>

Public comments

20. Many respondents commented on the implementation issues and concerns arising out of the perceived conflation of the disciplinary regime and section 213, when a disciplinary decision becomes a possible ground for the institution of section 213 proceedings. This perception arises because the CFI may review the merits of the SFC's disciplinary decisions in order to discharge its duties under section 213.

21. Respondents further elaborated that there would be a risk of parallel proceedings and contradictory outcomes. Several respondents suggested that the amendments to section 213 should address this by outlining how the CFI's review interacts with the role of the Securities and Futures Appeals Tribunal (**SFAT**) and the Court of Appeal in disciplinary proceedings. For example, the SFC should not commence section 213 proceedings until the appeal process by the regulated person to the SFAT or Court of Appeal under the disciplinary regime has been exhausted. Some respondents also suggested adding to section 213(4) a non-exhaustive list of the factors that the CFI should take into account in considering whether an order is desirable and not prejudicial, including any disciplinary action already taken by the SFC such as significant fines or licence suspensions.

The SFC's response

22. We acknowledge the implementation issues and challenges highlighted above. These arise because, if we had decided to go ahead with the proposal, it would have established a new link between the disciplinary regime and section 213, which currently operate independently.

23. Before making a remedial order under section 213(1), the court is required by section 213(4) to ensure it is "desirable" that the order be made and the order "will not unfairly prejudice any person". With the new disciplinary ground as a basis for the CFI to make an order, the CFI may consider it necessary to review the merits of the underlying disciplinary decision to discharge its obligation under section 213(4) in some circumstances, whether or not the disciplinary decision has been reviewed by the SFAT or appropriate appeals courts. Prior to the issue of the consultation paper, we were aware that this might result in parallel proceedings, namely court proceedings under section 213 and SFAT proceedings on a review of disciplinary decisions, with contradictory outcomes. We considered that this issue could be administratively mitigated if the SFC did not commence section 213 proceedings until the appeal process under the disciplinary regime has been exhausted, as also suggested by some respondents. Having said that, in light of the other concerns raised by the industry, we believe this proposal should be deliberated further.

(iii) Fairness and proportionality concerns

Public comments

24. Some respondents were concerned that the expansion of section 213 would result in all forms of disciplinary action taken by the SFC potentially triggering an action under section 213, and they believe this would be unnecessarily broad and would not reflect the varying degrees of severity contained in the types of disciplinary sanctions and the breadth of the SFC's codes and guidelines. They therefore suggested that the SFC specify which types of misconduct would give rise to an application under section 213, as it would be unfair for section 213 orders to be made in all circumstances, for example, in instances of minor misconduct.

25. Other respondents commented that the proposal imposes a heavy responsibility on the court to ensure any section 213 order sought is desirable and fair. Respondents suggested that given the court's lack of familiarity with the huge volume of the SFC's non-statutory requirements set out in an array of codes and guidelines, the court may have to rely heavily on the SFC's interpretation of the codes and guidelines, leading to unfair decisions.

26. Some respondents also commented on the potential extension of the limitation period. At present, the statutory limitation period commences from the date of the loss or breach. Respondents noted that if the SFC's power to apply for orders under section 213 is triggered after the disciplinary action is made, this would postpone the commencement of the limitation period from the date of the loss or breach to the date of the decision. Respondents believe this appears unfair and the extension would significantly increase the potential liability of regulated persons.

27. Respondents also noted that as both the SFC's disciplinary decisions and section 213 orders are sought based on the same misconduct, this could result in regulated persons being fined and then subjected to a compensatory order. Respondents commented that this would impose an unduly harsh burden on regulated persons and that the SFC should consider, for instance, whether pecuniary sanctions under section 194 or 196 of the SFO and remedies under section 213 should be mutually exclusive. Respondents commented that the SFC should also consider whether to suspend any penalty imposed under section 194 or 196 until the section 213 proceedings have been resolved and also take into account the section 213 compensation in determining whether disciplinary fines should be imposed and if so the amount.

The SFC's response

28. We acknowledge the industry's concerns about the need for certainty about the circumstances in which the SFC may seek section 213 orders in the context of this proposal. These concerns will be considered in further detail.

29. In relation to the comment on the court's potential unfamiliarity with the SFC's non-statutory requirements set out in its codes and guidelines, we are confident of the independence and competence of the court in dealing with novel legal and factual issues.

30. We note the comments on the extension of the limitation period and the impact this would have on regulated persons, particularly the contingent liability for longer periods of time and the lack of certainty with respect to the extent of their potential liability. To clarify, postponing the commencement of the limitation period is not the policy objective of this proposal, though it would indeed be the natural result if the proposal goes ahead in its current form. These practical implications will also be considered in further detail.

31. As regards the concern that disciplinary fines and section 213 orders would be sought over the same misconduct, we understand that the potentially very significant monetary amounts of section 213 compensation orders may result in such orders being perceived by the industry as punitive in nature. However, the fundamental nature of section 213 orders is restitutionary and compensatory to restore those who suffered harm from a regulated person's misconduct to the position they would have been in had the misconduct not taken place. In contrast to the compensatory nature of section 213 orders, regulatory fines serve to deter future non-compliance. Fines and compensation orders have different purposes, and while they are complementary, one should not be at the cost of the other.

32. We reiterate that the policy objective of this proposal is to enhance investor protection; particularly in instances where misconduct by licensed persons results in financial losses to investors and they need to be compensated. If investors are not compensated or where the channels for seeking compensation are unduly burdensome, their confidence in the financial services industry in Hong Kong will be weakened, which will harm the functioning and reputation of our markets.

(iv) Competitiveness and status of Hong Kong as an international financial centre

Public comments

33. Many respondents expressed concerns relating to the impact of the amendments on the competitiveness and status of Hong Kong as an international finance centre. They commented that the lack of predictability about the total financial impact of an enforcement action may exacerbate the prevailing trend towards relocating staff or business units with regional remits to other Asia-Pacific jurisdictions. Some respondents also commented that the potentially very significant monetary amounts of section 213 compensation orders coupled with disciplinary sanctions may dissuade regulated persons from participating in some types of high-risk regulated activities, such as sponsoring initial public offerings and selling complex investment products, and this may adversely affect the development of Hong Kong's financial markets.

The SFC's response

34. We do not agree that the proposal would harm the competitiveness or status of Hong Kong as an international financial centre. An effective regulatory regime needs to strike a balance between providing a proportionate degree of protection for investors and enabling the industry to conduct business in an environment which is not hampered by unnecessary regulatory barriers to innovation and competition. While there are tensions between these two interests, higher regulatory standards and the active enforcement of those standards help strengthen investor confidence which in turn makes Hong Kong an attractive market for international investors.

(v) A broader and more holistic review of compensation orders as a remedy in Hong Kong

Public comments

35. Several respondents commented that current laws already provide adequate legal rights and remedies for investors, and they questioned whether there was any need for the amendments as the existing framework appears to function well. Other respondents also noted that Part IX of the SFO already provides adequate remedies and safeguards to deal with misconduct and the lack of fitness and properness of regulated persons through disciplinary proceedings. Respondents noted that there are other existing rights of action beyond the SFO, such as consumer protection laws and the option of civil litigation, alongside the Financial Dispute Resolution Scheme and regulated persons' own complaints handling procedures.

36. One respondent further commented that given the far-reaching impact of the amendments, they should be considered more carefully and by a wider range of stakeholders. The respondent considered it might be suitable for the Secretary for Justice or the Chief Justice to refer the proposal to the Law Reform Commission of Hong Kong.

The SFC's response

37. We do not agree that the existing legal framework in Hong Kong already provides adequate protection to ensure aggrieved investors, in particular retail investors, will be compensated for financial losses in all appropriate cases. In response to the comments on the option of civil litigation for investors to pursue directly, we note that retail investors often do not have the resources to litigate directly in courts and there is also no class action mechanism in Hong Kong. Further, in circumstances where multiple regulated persons perpetuated similar misconduct with respect to similar investment products resulting in large numbers of investors suffering losses, it would be more suitable for the SFC to obtain compensation on behalf of the investors.

38. However, we agree that any amendments to enhance the available remedies to protect the investing public will have a far-reaching impact on the industry and the Hong Kong financial markets, and we will take more time to reconsider the proposal, taking into consideration any comments from stakeholders.

(vi) The SFC's concluding remarks

39. The current available remedies for compensating aggrieved investors are not perfect. In situations where there is solely a breach of the SFC's codes or guidelines (but no contravention of a statutory provision), the SFC has no means to require intermediaries to compensate aggrieved clients or investors. The proposal aims to close this regulatory gap.

40. However, we acknowledge the complexities raised by the respondents. We will further study the concerns raised and, if necessary, consider a broader range of possible options to meet our policy objective of enhancing the prospects of investors getting fair compensation in intermediary misconduct cases.

41. Having considered all the public submissions, and in particular those highlighted above, we believe the preferred course forward is to put this proposal on hold, so that we can thoroughly consider the implementation issues highlighted in this document as well as a full range of other options to achieve this policy objective including strengthening the SFC's disciplinary regime.

Section 2 – Amendments to exemptions in section 103 of the SFO

Question 3:	Do you agree with the proposal to amend the exemption set out in section 103(3)(k) and the consequential amendments to section 103(3)(j)? Please explain your view.

Public comments

42. A majority of respondents raised concerns about the proposal to amend the professional investor exemption set out in section 103(3)(k) and the consequential amendments to section 103(3)(j). While the respondents were generally supportive of the objective underpinning the proposal to enhance investor protection, common concerns related to: (i) whether the amendments are necessary; and (ii) the operational difficulties and the impact on business development and marketing processes.

(i) Necessity of the amendments

43. Many respondents questioned whether the amendments were necessary. They contended that there is no material risk for retail investors to be exposed to unauthorised advertisements of investment products if they are unable to invest in them. Respondents noted that the existing regulatory requirements, such as know-your-client (**KYC**), suitability assessments and risk disclosures, already provide sufficient protection for retail customers. Respondents commented on the lapse of time since the Pacific Sun judgment was handed down, noting that there has not been any enforcement action relating to section 103(3)(k) since then, suggesting that the lack of urgency indicates there is no material issue which necessitates this proposal.

44. Several respondents also noted that the SFC has not sufficiently identified a harm which may be caused to retail investors by firms advertising their products generally, as it should not be the SFC's regulatory objective to protect investors from merely seeing advertisements. The respondents commented that the harm to investors is perceived as opposed to quantified. Further, respondents also commented that the amendments are disproportionate to the harm given the existing disciplinary sanctions for intermediaries and the criminal penalties for breaches of section 103.

45. A few respondents supported these amendments, one of whom noted that following the judgment of the Court of Final Appeal in Pacific Sun, retail investors are in a vulnerable position because the court expanded the scope of the exemption which increased the risk that retail investors may act upon unauthorised advertisements. Therefore, the amendments are necessary to align section 103(3)(k) with the intended legislative purpose and to safeguard retail investors' interests. Another respondent agreed that unauthorised advertisements of investment products should be confined to professional investors who have the experience and knowledge to understand them, particularly as financial products have become more complex and diverse.

(ii) Operational difficulties and impact on business

46. Many respondents highlighted the operational difficulties and impact of the proposal on business development and marketing processes. They considered that this proposal is detached from commercial realities and will unnecessarily disrupt some common

marketing activities. For example, if implemented, this proposal would effectively require intermediaries to only issue unauthorised advertisements to professional investors who have already been identified through the firms' KYC and related procedures. Some respondents pointed out that in reality, professional investors are generally unwilling to provide their KYC information at the preliminary marketing stage, and this proposal would significantly reduce intermediaries' ability to market to prospective investors or may create a disjointed marketing process.

47. A few respondents further commented that this proposal would provide an unfair advantage to more sizeable financial institutions who already have a large existing client base to which they can market new products without having to conduct KYC. Many respondents believe this would make it more difficult to solicit new investors without providing any additional investor protection benefits.

48. Several respondents also commented that the amendments would unduly restrict online marketing efforts. They believe the amendments would jeopardise Hong Kong's competitiveness and status as an international financial centre, which may divert sales activities to other markets.

The SFC's response

49. The policy objective behind this proposal is to enhance investor protection by ensuring that retail investors will not be exposed to unauthorised advertisements of investment products intended only for professional investors and to reduce the risk of the professional investor exemption being abused by advertisers. The proposal seeks to reflect the original intent of section 103, which is to protect investors at the point when marketing materials are issued. Investment products aimed at professional investors are likely to be too complex or risky for the investing public and there have been considerable developments in the financial landscape which have made investment products more diverse and their distribution more accessible.

50. While the regulatory safeguards relating to suitability ought to prevent retail investors from investing in unsuitable products, we are very concerned about the protection of retail investors in an era of increasingly complex and accessible investment products. Our concern is partly prompted by multiple instances of products intended for professional investors (eg, Chapter 37 bonds) being sold to retail investors in breach of suitability rules.

51. However, we acknowledge that the potential benefits of this proposal need to be considered against the impact it may have on the prevailing investment product marketing processes which developed following the Pacific Sun judgment. In particular, we note two practical difficulties highlighted by respondents: (i) where potential clients may be unwilling to provide detailed KYC information in the pre-marketing process; and (ii) the development of multi-media, multi-jurisdictional online distribution of investment products and how investors access these distribution platforms.

52. Having considered respondents' views and concerns, we will not proceed with the proposal in its current form. We will continue to monitor the need to introduce new policies over the longer term. If necessary, we will consult the industry again.

53. We would like to remind the industry that anyone (whether a licensed intermediary or not) invoking the professional investor exemption in section 103(3)(k) must be able to demonstrate a clear intention to dispose of the investment product only to professional

investors. We take a strong view against anyone who misuses this exemption to push unsuitable investment products to retail investors.

54. To demonstrate and evidence a genuine intention to dispose of an investment product only to professional investors, the issuer of an advertisement should, at a minimum, ensure it is plainly apparent from the face of the advertisement that the underlying investment product is intended only for disposal to professional investors.

55. In this regard, we consider that the clear display of an appropriate message or warning on all advertising materials would go a long way to helping an issuer of an advertisement establish this intention. Anyone who issues advertisements will need to determine how best to present this message or warning and put in place related processes and safeguards to ensure the investment products will not be sold to retail investors. The SFC is considering providing further guidance to the market on this matter.

56. As no legislative amendments will be made to section 103(3)(k), there will not be any consequential amendments to section 103(3)(j) relating to investment products sold or intended to be sold only to persons outside Hong Kong.

Section 3 – Amendments to insider dealing provisions of the SFO

Question 4:	Do you agree with the proposal to expand the scope of insider dealing provisions of the SFO to cover insider dealing perpetrated *in Hong Kong* with respect to *overseas-listed securities or their derivatives*? Please explain your view.
Question 5:	Do you agree with the proposal to expand the scope of insider dealing provisions of the SFO to cover insider dealing perpetrated *outside of Hong Kong*, if it involves any *Hong Kong-listed securities or their derivatives*? Please explain your view.

Public comments

57. Most respondents agreed with the proposed amendments to expand the scope of insider dealing provisions of the SFO. Respondents considered that it would strengthen investor protection, protect the integrity and reputation of our markets, as well as bring the SFO insider dealing regime in line with other major common law jurisdictions. However, one respondent commented that overseas regulatory or law enforcement authorities, as opposed to the SFC, should have the principal responsibility for pursuing insider dealing on their markets when it is perpetrated in Hong Kong.

58. Several respondents requested clarification of the scope and application of the proposed amendments.

(a) In relation to bringing overseas-listed securities and their derivatives into the regime, one respondent asked whether insider dealing would be determined by reference to Hong Kong law or the laws of the overseas jurisdiction. They also asked if there would be a requirement that the misconduct should also have been unlawful in the overseas jurisdiction and whether the SFC would consider publishing a list of selected overseas markets for the purpose of implementing this proposal.

(b) One respondent asked whether the proposal would apply to over-the-counter (**OTC**) transactions in overseas-listed debt securities. Another respondent asked if "derivatives" as covered in the proposal refer to the narrow definition of unfunded OTC derivatives or a broader class of products such as funded structured products with embedded derivatives.

(c) One respondent asked whether a transition period would be provided to enable firms to update their internal compliance policies and manuals.

(d) One respondent asked whether a regulated person is required to report breaches in relation to overseas-listed securities under the proposal and how such reports should be made. The respondent noted that data transfer restrictions may apply where the SFC requests information and the information is located overseas.

The SFC's response

59. Having considered the responses, we will proceed with the proposal outlined in the consultation paper. Regarding the comment that overseas regulatory authorities have the principal responsibility for pursuing insider dealing perpetrated in Hong Kong with respect to overseas-listed securities or their derivatives, we acknowledge that the SFC may provide intelligence to securities regulators in other jurisdictions under our arrangements for cross-boundary regulatory cooperation. However, this is not always an effective way to deal with this type of insider dealing, particularly when much of the evidence required to substantiate the misconduct is in Hong Kong.

60. It is therefore important that the SFC obtains the powers to tackle this type of insider dealing, otherwise the persons responsible may escape liability altogether, and this may damage the reputation of Hong Kong's financial markets.

61. We set out below our clarification of the scope and application of the proposed amendments.

(a) In respect of the proposed expansion of the insider dealing regime to include overseas-listed securities or their derivatives, the amended provisions will stipulate that the misconduct would also need to be unlawful in the relevant overseas jurisdiction. It was noted in the Consultation Paper that a new subsection would be added to section 282 (civil regime) and section 306 (criminal regime) to that effect. Given that the purpose of the proposal is to enable us to take action against cross-border insider dealing, it would not be in line with our policy objective to narrow the scope by prescribing a list of selected overseas markets to which the amended provisions will apply.

(b) Our proposal does not seek to change the applicability of the insider dealing regime with regard to OTC transactions in listed debt securities. It is the territorial scope which is being changed. Our intention is to expand our capability to take action against insider dealing in overseas-listed securities or their derivatives perpetrated in Hong Kong in order to better protect the reputation of the Hong Kong markets. In other words, following the implementation of the proposed amendments, the insider dealing regime would apply to OTC transactions in overseas-listed debt securities, as it currently applies to OTC transactions in Hong Kong-listed debt securities, unless one of the statutory defences applies. Our proposal also does not change the definition of "derivatives" contained within sections 245 and 285 of the SFO—the change in its application relates only to the territorial scope but not to the scope of the instruments. The current scope of the definition remains unchanged.

(c) Once the legislative amendments have been published, firms will have sufficient time to update their internal compliance policies and manuals, and thus a transition period will not be required.

(d) With regard to the reporting of breaches under the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of Conduct), as the amendments are made to some market misconduct provisions within Parts XIII and XIV of the SFO, any notification requirements set out within the Code of Conduct will also apply. Firms should

submit a report when they become aware of any suspected breaches and use their best endeavours to obtain the data to submit in their report to us.

Conclusions and way forward

62. The SFC would like to thank all respondents for their time and effort in reviewing the proposals and for their detailed and thoughtful comments.

63. The SFC will proceed with the proposal to amend the insider dealing provisions of the SFO. The industry will have the opportunity to review the draft amendments during the legislative process.

64. In relation to the proposals to amend sections 213 and 103(3)(k) of the SFO, we will continue to monitor market developments and consider a range of other options to enhance investor protection as necessary.

Appendix A – List of respondents

(In alphabetical order)

1. Asia Securities Industry & Financial Markets Association
2. Clifford Chance
3. CompliancePlus Consulting Limited
4. Deacons
5. Donald Lai
6. Freshfields Bruckhaus Deringer
7. Hong Kong Institute of Certified Public Accountants
8. Hong Kong Investment Funds Association
9. Hong Kong Securities Association
10. Hong Kong Securities & Futures Professionals Association
11. Hong Kong Venture Capital and Private Equity Association
12. Martin Rogers
13. Mayer Brown
14. Private Wealth Management Association (PWMA)
15. Simmons & Simmons
16. SWCS Corporate Services Group (Hong Kong) Limited
17. The Alternative Investment Management Association
18. The Hong Kong Chartered Governance Institute
19. The Law Society of Hong Kong
20. The Institute of Financial Planners of Hong Kong
21. Timothy Loh LLP
22. Virtu ITG Hong Kong Limited
23. Submissions of two respondents are published on a “no-name” basis upon request
24. Submissions of three respondents are withheld from publication upon request