

Process Review Panel for the Securities and Futures Commission Annual Report to the Financial Secretary for 2007

Executive Summary

Introduction

The seventh Annual Report of the Process Review Panel for the Securities and Futures Commission (“PRP”) covers the work of the PRP from 1 January 2007 to 31 December 2007.

Background and Terms of Reference of the PRP

2. The PRP is an independent, non-statutory panel established by the Chief Executive in November 2000 to review and advise the Securities and Futures Commission (“SFC”) upon the adequacy of the SFC’s internal operational procedures governing the action taken and operational decisions made in the performance of its regulatory functions.

3. Under its terms of reference, the PRP may review files of the SFC to verify that the action taken and decisions made in relation to any specific completed case are consistent with the relevant internal procedures and operational guidelines. The PRP is required to submit its reports to the Financial Secretary annually or otherwise on a need basis.

Constitution of the PRP

4. The PRP, chaired by Mr. Anthony Chow Wing Kin, currently comprises ten members, including eight members from the financial sector, academia, the legal and accountancy professions, and two ex officio members including the Chairman of the SFC and the representative of the Secretary for Justice.

Work of the PRP in 2007

5. In 2007, the PRP reviewed completed cases and/or procedures of the SFC in the following areas –

- (a) licensing of intermediaries;

- (b) inspection of intermediaries;
- (c) authorisation of collective investment schemes;
- (d) handling of complaints;
- (e) investigation and disciplinary action; and
- (f) processing of listing applications under the Dual Filing regime.

6. The PRP concluded that the SFC had generally followed its internal procedures in handling cases. The PRP also made a number of recommendations for improvement covering a wide range of the SFC's regulatory activities for improving the transparency, efficiency, consistency of and checks and balances on the SFC's processes. Where the SFC had difficulties to adopt a recommendation, detailed explanations were given.

Engagement with the industry

7. The PRP attaches great importance to views from all users of the market on issues within its terms of reference. The PRP received comments and suggestions from market practitioners and referred these comments and suggestions to the SFC for consideration and response. In response to a request, the PRP reviewed a case of broker misconduct and provided the SFC with its observations.

Observations and recommendations

8. The observations and recommendations made by the PRP are summarised below.

(1) Observations and recommendations that are accepted

(A) Licensing of intermediaries

Item (1)
<p><u>Case findings/market views</u></p> <p>The SFC very often receives applications with incomplete information and supporting documents. The PRP noted that in processing these applications, the SFC had to ask each applicant in writing for supplementing the outstanding documents. In one case, the SFC had to issue three such tailor-made letters until the applicant could provide all the necessary documents.</p>

PRP recommendation/observation

As a way to rationalise the use of SFC's resources, the PRP suggested the SFC consider using standard proforma letter with checkboxes specifying the supporting documents required (Para. 3.3 of Chapter 3).

SFC's response

While the SFC accepted the approach being viable, it had doubts about the benefits in terms of savings in resources and procedural efficiency. The SFC counter-proposed to look into the possibility of using a standard requisition letter for each type of regulated activities, instead of one letter encompassing all types of licence applications. As a pilot scheme, licence applications for hedge fund managers had started using such standard requisition letters. The SFC would review the effectiveness of the scheme and consider enlarging its scope of application.

Item (2)

Case findings/market views

In a case, the applicant was slow in responding to the SFC's requests despite repeated reminders. The applicant had finally withdrawn the application after more than a year of processing.

PRP recommendation/observation

The PRP suggested the SFC consider putting in place a due process to deal with lukewarm response from applicants. The SFC was invited to consider whether an application could be deemed withdrawn if the applicant failed to provide a substantive response after a prolonged period of time (Para. 3.4 of Chapter 3).

SFC's response

The SFC considered the suggestion not viable as it was obliged to follow a statutory procedure in refusing a licence application. The SFC proposed that alternatively, if an applicant failed to provide the required information within a specified period, the SFC would proceed with the refusal process on the grounds that the limited information received was not adequate to prove that the applicant was fit and proper to be licensed.

Item (3)

Case findings/market views

In one case, the SFC received applications from an authorised financial institution for registration as a registered institution and for the appointment of executive officers. The SFC sought advice from the Hong Kong Monetary Authority ("HKMA") as to whether the applicants were fit and proper for registration. The applications had taken a fairly long time to be processed, because the applicant had initiated some significant changes in its proposed business activities and in nominations for executive officers and members of management to be involved in the proposed business activities.

PRP recommendation/observation

The PRP invited the SFC to discuss with the HKMA with a view to expediting the processing of applications from authorised financial institutions (Para. 3.5 of Chapter 3).

SFC's response

The SFC advised that the HKMA had started a new practice of updating the SFC on the status of outstanding cases quarterly.

Item (4)

Case findings/market views

In an application for becoming a responsible officer, the SFC noticed that the applicant was under an on-going investigation by the SFC. The case had been put on hold for several months pending outcome of the investigation.

PRP recommendation/observation

The PRP invited the SFC to consider expediting its investigation work (Para. 3.6 of Chapter 3).

SFC's response

The SFC indicated that it had improved its investigation time significantly. The percentage of investigation cases completed within seven months had increased from 36% in 2006 to 71% in 2007.

Items (5), (6), (7) and (8)

Case findings/market views

In processing an application for licence from a person who had been discharged from bankruptcy for three years, the SFC contacted the employer sponsoring the application to ascertain that the company was aware of the solvency background of the applicant. The SFC explained to the employer that based on the Fit and Proper Guidelines, the application was unlikely to be approved. The applicant subsequently withdrew the application.

PRP recommendation/observation

The PRP considered the SFC's five-year rule too stringent, given that a bankruptcy order could be set aside after four years already (Para. 3.9 of Chapter 3).

SFC's response

The SFC explained that the five-year rule was only a guiding reference. In considering an application from a discharged bankrupt, it would take into account factors like circumstances leading to the bankruptcy and the person's current solvency, in addition to the time of discharge from bankruptcy. In fact, between April 2003 and December 2007, the SFC had approved a total of seven applications from persons discharged from bankruptcy within five years, and refused only one.

PRP recommendation/observation

To ensure a right balance between protecting the interest of the investing public and denying the livelihood of an applicant who might have only the skills for a job in the financial industry, the PRP recommended the SFC to issue guidelines on dealing with applications from discharged bankrupts (Para. 3.13 of Chapter 3).

PRP recommendation/observation

The PRP considered it useful to set out the criteria and considerations such as the supporting documents required for assessment (Para. 3.13 of Chapter 3).

SFC's response

The SFC agreed to issuing a set of Frequently Asked Questions to the public and preparing internal guidelines on handling applications from discharged bankrupts.

PRP recommendation/observation

The PRP suggested that a database and statistics on applications with adverse information should be maintained to provide ready reference (Para. 3.13 of Chapter 3).

SFC's response

The SFC explained that it had already set up an electronic database of licensees and individuals about whom the SFC had concerns. Statistics on the number of applications approved, refused or withdrawn could be derived from the existing licensing system.

Item (9)

Case findings/market views

In assessing an application from a person whose bankruptcy order had been annulled only three months before making the application, the SFC requested the applicant to provide additional information relating to the bankruptcy. The applicant replied with only a brief explanation on the circumstances leading to the bankruptcy and that the order was annulled after he had settled all his debts. As the applicant could not produce the relevant bankruptcy papers, the SFC suggested the applicant obtain copies from the government authority or the court. The applicant subsequently withdrew his application.

PRP recommendation/observation

The PRP considered that since the bankruptcy order had already been annulled by the court, the SFC might take a flexible approach and consider other information available such as employer's reference, instead of relying solely on empirical evidence to assess the applicant's solvency position (Para. 3.11 of Chapter 3).

SFC's response

The SFC agreed with the PRP that it was viable to adopt a flexible approach in considering the types of supporting evidence in certain circumstances but the SFC would remain vigilant as to the reliability of the evidence provided.

Item (10)Case findings/market views

The PRP noted that an application from a discharged bankrupt was approved by a Senior Manager whereas in another case, an application from a person with conviction record was approved by a Director. The PRP noted that for cases with adverse information, the SFC's procedural manual only required the case officer to discuss the matter with more senior officers but did not specify the level of the decision-makers.

PRP recommendation/observation

Since both bankruptcy and criminal conviction were matters that might impugn the integrity of an applicant, the PRP considered that there should be consistency in the approval process, and invited the SFC to review and designate the approving authority for such cases in the procedural manual (Para. 3.12 of Chapter 3).

SFC's response

The SFC explained that given the vast variation in the nature of adverse information, it was difficult to define the approving authority for each type of cases. Nonetheless, the SFC agreed to consider requiring the decision to be made by an officer not below Senior Manager level and to review the procedural manual to ensure consistency.

(B) Authorisation of collective investment schemes**Item (11)**Case findings/market views

In one case, the processing work took more than nine months because the applicant accorded priorities and resources to the other applications submitted to the SFC concurrently. The applicant could not provide a substantive response to the SFC's comments in time despite the issue of several reminders.

PRP recommendation/observation

The PRP was concerned about whether the applicant had taken advantage of the application system by ensuring that the application, which might have been submitted pre-maturely, would remain valid (Para. 3.21 of Chapter 3).

SFC's response

There was no evidence in this case suggesting an abuse of the system. Notwithstanding, in order to rationalise the use of its resources, the SFC was considering a new approach to deal with lukewarm response from applicants. If an applicant failed to provide a substantive response after a reasonably long time, the SFC might refuse the application on the grounds that it could not be satisfied that the requirements in the relevant code on collective investment scheme had been met. The SFC was reviewing its standard reminder letters to highlight the possibility that an application could be refused.

(C) Handling of complaints

Item (12)
<p><u>Case findings/market views</u></p> <p>An ex-licensee wrote to the Licensing Department asking what he needed to do in order to be licensed again. As he had not received any response from the SFC for more than a month, he made an enquiry to the SFC's office in person. Since he had not made an appointment in advance, the case officer handling his enquiry could not meet him. The case officer called him on the following day and asked him to submit an application for assessment. The person lodged a complaint to the SFC about its failure to acknowledge his enquiry and to meet him when he visited the SFC's office.</p>
<p><u>PRP recommendation/observation</u></p> <p>The PRP considered that public enquires should be handled expeditiously to meet the rising expectation of the public. An acknowledgement was a useful means to notify the person that the matters had been directed to the right place and were receiving attention. It was a good practice to issue an acknowledgement upon receipt of an enquiry instead of making no response for a period of time. The PRP suggested the SFC consider developing clear guidelines and timeframe for handling public enquiries of all sorts, including a timeline for issue of an acknowledgment (Para. 3.24 of Chapter 3).</p>
<p><u>SFC's response</u></p> <p>The SFC agreed that it would be a good practice to issue acknowledgement to enquiries promptly. Subject to the availability of resources, the Licensing Department would formalise its internal practice to bring the response time generally in line with the performance pledge, i.e. making preliminary response within four business days for telephone enquiries, and within two weeks for written enquiries.</p>
Item (13)
<p><u>Case findings/market views</u></p> <p>Arising from the review of two complaint cases, the PRP noted the SFC's advice that there was no written procedures for handling complaints against the Commission itself.</p>
<p><u>PRP recommendation/observation</u></p> <p>The PRP suggested the SFC review its complaint handling procedures and submit its findings to the SFC Audit Committee for consideration from a corporate governance angle (Para. 3.25 of Chapter 3).</p>
<p><u>SFC's response</u></p> <p>The SFC explained that it had always followed a consistent approach in handling complaints, but agreed that it would take steps to formalise the existing practice in writing and submit the proposals to the SFC Audit Committee for consideration in due course.</p>

Item (14)

Case findings/market views

The SFC received, one day before the launching of an initial public offering exercise (“IPO”), a complaint about the proliferation of off-market deals in which investors were assured that they would be allotted with certain number of shares being offered upon paying a premium. Investors entering such deals ran a high risk as the seller might not fulfil the promise to deliver the shares. The complaint was reported to the SFC’s Complaints Control Committee (“the Committee”) and a senior officer of the SFC promptly spoke at a meeting with the media about the risks to investors in entering such off-market deals. The PRP noted that the complaint was actually discussed at the Committee one day after the close of the IPO.

PRP recommendation/observation

As the Committee met on a weekly basis and might not be able to cope with urgent or time-critical issues, the PRP invited the SFC to advise how it would deal with urgent or time-critical issues within or outside the Committee framework (Para. 3.26 of Chapter 3).

SFC’s response

The SFC explained that where the circumstances justified prompt action, the relevant operational division had the discretion to proceed and then seek retrospective endorsement and advice at the following Committee meeting.

Item (15)

Case findings/market views

An investor complained to the SFC about an investment-linked assurance scheme offered by an insurance company. After inquiring into the case, the SFC concluded that there was no breach of the SFO nor of the Code on Investment-Linked Assurance Schemes, and the complaint was not substantiated. The complainant was not satisfied with the findings and had followed up with several complaints against the SFC for having failed to properly handle his case. The SFC reviewed the procedures for handling the complaint, and concluded that a thorough investigation with extensive consultation had been made and no further action would be taken.

PRP recommendation/observation

Very often, investors could not fully understand the features of an investment product, such as illustrated return as opposed to guaranteed return of investment-linked assurance schemes. This misunderstanding often gave rise to complaints if the actual return from the investment could not meet up with the expectation. The PRP suggested the SFC consider strengthening the investor education programme (Para. 3.28 of Chapter 3).

SFC’s response

The SFC agreed with the PRP that investor education was important. There were extensive publicity about the difference between guaranteed return and illustrated return through its InvestEd website and in printed media. Moreover, the External Relations Department of the SFC had been taking part in the SFC’s Complaints Control Committee meetings where it could have first hand information about market sentiments and areas that might attract complaints. On the basis of these information, the External Relations Department would formulate its focus and strategy in investor education programmes.

(D) Investigation and disciplinary action

Items (16) and (17)
<p><u>Case findings/market views</u></p> <p>The PRP reviewed a case concerning a company dealing in futures contracts, which was associated with an authorised financial institution (a bank). The SFC found that a responsible officer of the futures company had instructed several officers in a branch of the bank to accept instructions from clients to trade in futures contracts and to convey the orders to the dealing room of the futures company for execution. These officers were licensed to deal in securities but not in futures contracts. The persons and the company concerned were prosecuted for performing a regulated function without a licence. The SFC subsequently entered into settlement with the parties in relation to the disciplinary proceedings. Under the settlement terms, the parties pleaded guilty to the summonses and accepted a public reprimand and a heavy fine of close to \$1 million; and the licences of the persons concerned were suspended for a period of time.</p>
<p><u>PRP recommendation/observation</u></p> <p>The PRP invited the SFC to explain the reasons for taking prosecution in addition to a substantial fine (Para. 3.32 of Chapter 3).</p>
<p><u>SFC's response</u></p> <p>The SFC took a serious view in this case having regard to the fact that the misconduct perpetuated for several years. The amount of fine was determined in the light of similar precedent cases and the profits derived from the unlicensed activities. Also, in line with established policy, the amount had been reduced to reflect the cooperation of the parties in the investigation and that prosecution was taken concurrently.</p>
<p><u>PRP recommendation/observation</u></p> <p>The PRP considered that market practitioners might have misunderstood that a licence was required only for a person who input an order into the trading system but not those who convey an order. The PRP suggested the SFC consider taking steps to clear up this misunderstanding and remind market practitioners of the statutory requirement that a licence would be required to convey an order from clients to the dealing room (Para. 3.35 of Chapter 3).</p>
<p><u>SFC's response</u></p> <p>The SFC agreed to take steps together with the HKMA to remind banks and their management staff of their obligation to ensure those who had a role in handling client orders in SFC regulated products were properly licensed.</p>

Item (18)
<p><u>PRP recommendation/observation</u></p> <p>In 2006, the SFC had agreed to develop a policy that would guide its staff in deciding when to take or recommend criminal proceedings in lieu of or in addition to disciplinary proceedings. The PRP invited the SFC to advise on the progress (Para. 3.33 of Chapter 3).</p>

SFC's response

The SFC advised that in general, it would consider taking disciplinary action against a licensee following a successful prosecution. In developing a formal policy in this regard, the SFC had sought advice from counsel in the United Kingdom on the issues of double jeopardy and proportionality. The counsel advice confirmed that there was no double jeopardy between criminal and disciplinary proceedings, but the SFC had to give due regard to the proportionality of the total penalty especially in imposing a fine after a criminal conviction. The SFC advised that officers dealing with enforcement matters had already been briefed and given training on the legal advice and the implications from a management perspective. The SFC aimed to address the issues in a formal policy document in due course.

Items (19) and (20)

Case findings/market views

In a case, a property developer and its agent placed advertisements on newspapers to promote investment in a property in the Mainland. On the basis of the features of the sales package, the SFC considered that the investment product was a collective investment scheme and the issue of promotional materials required the SFC's authorisation under section 103 of the SFO. As no authorisation had been granted, the companies and the persons concerned were prosecuted for issue of unauthorised promotional materials on collective investment scheme. The PRP noted that the companies had placed advertisements on the newspapers again during the investigation. The SFC explained that it could not stop the companies from issue of promotional materials before a case of misconduct was established.

PRP recommendation/observation

In order to better protect investors, the PRP suggested the SFC consider reminding the subject under investigation about the SFC's regulatory concerns at the beginning of an investigation and that engagement in suspected activities during an investigation could be taken as an aggravating factor in determining the penalty in the event that a breach was substantiated.

Moreover, in line with the drive to promote compliance culture, the PRP suggested that efforts be made to raise awareness of both market practitioners and the public of the statutory requirement to obtain prior approval from the SFC for publicising promotional materials on collective investment schemes (Para. 3.37 of Chapter 3).

SFC's response

The SFC explained that it had already taken suitable steps to remind persons involved in an investigation about the regulatory concerns at the commencement of a formal investigation. It was a statutory requirement for the SFC to issue a notice to persons involved in an investigation and such notice would set out the scope of the investigation. The SFC would also interview the person concerned to explain the regulatory concerns and the reasons why he/she was identified as a person under investigation. In regard to protection to investor, the SFC said that in cases where a conduct could cause material harm to investors, the SFC could apply to the court for an injunction to restrain an activity before conclusion of an investigation. Regarding the suggestion that engagement in suspected misconduct during an investigation be taken as an aggravating factor, the SFC said that in determining the disciplinary sanctions, it would take into account the particular facts and circumstances of a case, including the failure to observe the SFC's advice on its regulatory concerns.

Regarding the publicity on the requirement to obtain authorisation for promotional materials, the SFC advised that it had issued a press release immediately upon successful prosecution in this case. Moreover, upon the commencement of the SFO in April 2003, the SFC had already reminded property developers and agents about the statutory requirement through press release.

Items (21) and (22)

Case findings/market views

The SFC's investigation revealed that two directors of a listed company had disposed of substantial number of shares but they filed the disclosure notices to The Stock Exchange of Hong Kong Limited ("SEHK") only five months later. The SFC prosecuted one director and gave a warning letter to the other.

PRP recommendation/observation

The PRP invited the SFC to clarify the rationale for imposing different penalties for the same misconduct (Para. 3.40 of Chapter 3).

SFC's response

The SFC explained that late reporting of notifiable interests were handled according to the procedural manual, which set out the factors governing the decision as to whether prosecution vis-à-vis warning letters should be taken for a breach of the disclosure requirement. The factors taken into account in the decision included value of the disposal, length of delay in making a report, location of the suspect and strength of evidence. In general, prosecution would be taken for cases with a disposal value and length of delay exceeding certain pre-determined thresholds whereas warning letters would be issued for cases not meeting the thresholds.

PRP recommendation/observation

Starting from July 2007, the SFC issued compliance advice letters for cases that warranted warning previously. In other words, a breach of the disclosure requirement would result in either prosecution or compliance advice letters. Noting that a compliance advice letter would be much more lenient compared to prosecution, the PRP invited the SFC to consider whether the thresholds should be reviewed (Para. 3.42 of Chapter 3).

SFC's response

The SFC said that the existing system provided a suitable safeguard to ensure market integrity. A change in the thresholds could mean more prosecutions. An increase solely arising from a change from warning letters to compliance advice letters was not justified.

(E) Expediting the return of clients' assets arising from broker misconduct cases

Item (23)
<p><u>Case findings/market views</u></p> <p>Some market practitioners pointed out that when a broker firm was found to have misappropriated clients' assets and when administrators or liquidators were appointed to deal with clients' assets, these assets were often locked up in custodian accounts. It usually took a very long time before the clients affected could recover their shares or money. The market practitioners suggested the SFC expedite the process for returning assets to clients so as to minimise the potential loss to clients (Para. 4.5 of Chapter 4)</p>
<p><u>SFC's response</u></p> <p>The SFC explained that when a broker firm holding clients' assets was liquidated, the SFC might apply to the court to appoint administrators to deal with clients' assets including adjudicating claims and ultimately returning assets to clients. In this respect, the SFC maintained only an overview of the progress of the administration. In general, administrators could return assets to clients in a few months' time. For more complicated cases, the speed at which the administrators could complete the tasks would depend on factors such as the number of clients involved and the reliability of the books and records kept by the brokers concerned.</p>

(F) Developing a communication protocol with the SEHK in the vetting of announcements and circulars

Item (24)
<p><u>Case findings/market views</u></p> <p>There are occasions when the SFC and the SEHK are required to vet announcements and circulars that fall into the ambits of both the Codes on Takeovers and Mergers and Share Repurchases ("Takeovers Codes") and the Listing Rules, which are administered respectively by the SFC and the SEHK. There was a comment from market practitioners that listed issuers and/or their professional advisers had difficulties in finalising the documents when the two regulators held different views. It was suggested that a clear communication protocol be established between the SFC and the SEHK for the vetting of announcements and circulars that required clearance from both regulators (Para. 4.7 of Chapter 4).</p>
<p><u>SFC's response</u></p> <p>The liaison and co-ordination practices between the two regulators were well established and there were no major problems in the past. As a general practice, the Takeovers Executive would copy its comments on draft documents to the Listing Division. In cases where there were different views between the Takeovers Executive and the Listing Division, the Takeovers Executive would discuss the matter with the parties concerned and, if necessary, the Listing Division. A pragmatic approach would be taken after careful consideration of the underlying rationale for the requirements of each of the Listing Rules and Takeovers Codes in order to resolve the issues speedily and effectively.</p>

(G) Improvement to SFC website to facilitate retrieval of practice notes

Item (25)
<p><u>Case findings/market views</u></p> <p>The SFC has been publishing the quarterly Takeovers Bulletin on its website since May 2007. The Takeovers Bulletin serves as periodic newsletters from the Takeovers Executive to market practitioners. It contains short informative articles, practice notes and information relating to takeovers in Hong Kong providing guidelines on how the Takeovers Executive normally interprets and applies certain provisions of the Codes. As the volume of information in the SFC website is building up, it is difficult to search for information. Some market practitioners suggested that a user friendly search function be established on the SFC website to enable users to search for practice notes and panel decisions by various searching strings such as date, topic or rule number (Para. 4.9 of Chapter 4).</p>
<p><u>SFC's response</u></p> <p>A search function had already been provided on the SFC website and users might input keywords to search for the relevant rules or topics. In addition, the SFC set up in April 2008 a new dedicated page called "Practice Notes" under the section of "Takeovers and Mergers" to provide quick reference to the relevant details such as issue time and the related rules of each practice notes.</p>

(H) SFC's policy on issue of compliance advice letter

Item (26)
<p><u>PRP recommendation/observation</u></p> <p>The PRP commented that it was imperative for the SFC to convey a clear message to the industry and to the recipients of compliance advice letters about the implication of the letter, such as its impact on the person's compliance record and whether the person was obliged to disclose it to an employer (Para. 4.16 of Chapter 4).</p>
<p><u>SFC's response</u></p> <p>The compliance advice letters would become a factor that the SFC would take into account when deciding whether to take formal action against a regulated person only when the person committed a similar breach in future. Nonetheless, the SFC would not take into account the events leading to the issue of the compliance advice letter in a formal disciplinary action, or in deciding the appropriate penalty for that breach. Since compliance advice letters were private, recipients of the letters would not need to disclose them to anyone unless they wished. The above features of the compliance advice letter were also explained in the body of the letter.</p>

Item (27)PRP recommendation/observation

The PRP invited the SFC to consider updating its procedural manual and providing training to its staff on the procedural changes (Para. 4.16 of Chapter 4).

SFC's response

The SFC would update its procedural manual and would provide training to its staff on the procedural changes.

(2) *Observations and recommendations that have not been accepted in full*

(A) Licensing of intermediaries

Item (1)Case findings/market views

In an application for becoming a responsible officer, the SFC noticed that the applicant was under an on-going investigation by the SFC. The case had been put on hold for several months pending outcome of the investigation.

PRP recommendation/observation

In view of the significant role of a responsible officer, the PRP suggested the SFC consider apprising the employer of the investigation. The employer should also be reminded not to allow the applicant to conduct any regulated activities until the application had been approved (Para. 3.6 of Chapter 3).

SFC's response

The SFC explained that it could not disclose information relating to an investigation to an employer under the secrecy provisions in the SFO. Moreover, as the investigation was still on-going and the SFC had yet to establish a case of misconduct, disclosure of such information could adversely affect the interest of the applicant. On the suggestion of reminding the employer of the statutory requirement that a person should not conduct regulated activity unless he/she was holding a valid licence, the SFC considered it not necessary since market practitioners should be aware of this.

Item (2)Case findings/market views

In the absence of adverse information in the application form, the SFC had granted a provisional licence to an applicant but was advised later that the applicant had a disciplinary record with an overseas regulatory authority.

PRP recommendation/observation

A provisional licence did not have an expiry date and it would lapse either upon issue of a full licence or refusal of the application. Since the statutory process to refuse a licence application might take a long time, it was possible that a provisional licence might remain valid for some time even if the SFC was minded to refuse the application on the basis of new evidence brought to light subsequently. In order to ensure better protection to the investing public, the PRP invited the SFC to consider introducing a validity period for a provisional licence (Para. 3.17 of Chapter 3).

SFC's response

The SFC explained that it could not implement the suggestion without introducing legislative amendments. Notwithstanding, the SFC said that it was only permitted to issue a provisional licence when, on the basis of the information then available to it, it was satisfied that the applicant was fit and proper. Therefore, this requirement was already a safeguard to investor protection. In addition, the SFC might revoke a provisional licence in exceptional circumstances having regard to the interest of the investing public. The SFC considered that the current system provided an appropriate balance between the interest of the investing public and the licence applicants.

Way forward

9. Looking ahead, the PRP will follow up a number of recommendations made in 2007 in relation to the SFC's internal procedures. The areas include handling of licence applications with incomplete information and enquiries on licensing issues, handling of complaints against the SFC, and the development of a compliance culture to raise awareness of the SFC's regulatory concerns. The PRP will continue its work on the review of completed cases, maintaining dialogue with market players, and engaging the industry to listen to their concerns. The PRP welcomes views from the general public with a view to identifying any areas of improvement to the SFC's procedures and processes.