

## The SFC's Updated Guidance on the Benefits of Co-operation: A New Approach?

On 12 December 2017, the Securities and Futures Commission (SFC) issued a Guidance Note on Co-operation (the “**Note**”) highlighting the benefits of co-operating in its investigation and enforcement proceedings. The SFC also issued frequently asked questions to help the industry and public to understand the Note which replaces the Hong Kong financial regulator's previous guidance published in March 2006.

In the aftermath of the global financial crisis, the SFC put aside the 2006 guidance and adopted what some critics considered to be an inflexible approach towards the resolution of SFC enforcement actions generally. When settlements were agreed, it was often unclear from the SFC's public announcements what credit, if any, was given for co-operation in the enforcement process.

The Note is designed to encourage early co-operation by articulating what may be the benefits of co-operation and when may be the most opportune times to engage the SFC in settlement discussions. Under appropriate circumstances, the SFC says co-operation may be recognised in the form of reduced sanctions. Hopefully, this signals a more transparent approach by the regulator to co-operation and settlement.

### Something old, something new

The new guidance applies to disciplinary matters involving licensed or registered persons, as did the previous guidance. In addition, the SFC provides guidance on the benefits of co-operating in the early resolution of civil court and Market Misconduct Tribunal (MMT) proceedings for the first time.

### Criminal cases excluded

The Note does not apply to criminal cases because the Department of Justice (DOJ) has unfettered discretion over criminal prosecutions. Any plea

negotiation and agreement in a criminal case will be subject to the terms of the Prosecution Code of the DOJ, and consideration by the presiding magistrate or judge.

### The SFC's policy on private or no-admission settlements

As a general principle, the SFC considers it is not in the public interest to resolve cases privately or on a no admission of liability basis.

### “Co-operation” defined by the SFC

Prompt, voluntary reporting of breaches or failings constitutes co-operation. The SFC expects full and frank disclosure of information when a report is made. This includes sharing the results of any internal investigation and providing the SFC with evidence and information of which it is otherwise unaware.

Unsurprisingly, an admission of liability and the prompt payment of compensation to investors who have suffered losses also constitute co-operation. Finally, the SFC regards prompt rectification and remediation of any breaches or failings as additional indicators of co-operation.

### What isn't co-operation?

The Note states that mere compliance with the requirements of the Securities & Futures Ordinance or other regulatory requirements does *not* represent co-operation in the eyes of the SFC. A party must go beyond what it is required by law in order to be deemed as cooperative. For example, in the context of disciplinary proceedings if a regulated person agrees to jointly appoint a third-party review with the SFC in respect of the breaches or failings and agrees to be bound by the reviewer's findings, then the SFC will recognise that step as co-operation.

## How does the SFC measure co-operation?

The SFC will consider the value of assistance provided in a particular case by referencing a number of factors including the quality, extent and substance of the assistance provided. The nature and seriousness of the breaches or failings, and the conduct of the party after the breaches or failings will be considered as well.

## Waiver of privilege

Concerns have been expressed by the industry in the past that the SFC expects privilege to be waived in the context of internal investigations, and that a refusal to waive privilege may be viewed negatively by the regulator. Therefore, it is good to read in the Note that the SFC acknowledges that a bona fide refusal to waive legal privilege over a document will not be regarded as uncooperative conduct.

## What are the rewards for co-operation?

For disciplinary cases, the SFC has been creative. If a case is resolved before the SFC issues a Notice of Proposed Disciplinary Action (NPDA), a reduction of the sanction imposed by up to 30 percent is possible according to the Note. The potential discount is up to 20 percent if the case is settled after the NPDA is issued but before the regulated person is due to make written representations in response. This discount is reduced to no more than 10 percent if settlement is reached after the regulated person makes representations but before the SFC issues a Decision Notice.

The SFC is unable to offer similar incentives for prompt co-operation in court or MMT cases where the sanctions to be imposed are ultimately determined by the presiding judge or MMT. The Note points out that early resolution of court or MMT cases can result in significant savings of time, cost and manpower to the SFC, which may in turn enable a case to be resolved on the basis of agreed facts. However, as a litigant rather than a decision maker, the SFC cannot fix a scale for a reduction in sanctions. The most it can do is agree to put forward a reduced sanction for the court or MMT's consideration, which the court or MMT may or may not accept.

## Transparency

The Note concludes by saying that in the interests of transparency, the SFC will provide an appropriate level of disclosure regarding co-operation. If the SFC considers it appropriate to impose a reduced sanction, it will inform the regulated person of the original sanction and the final sanction imposed after taking co-operation into account. This will allow the regulated person to measure the tangible benefits of their co-operation. The SFC will also state in its press release and Decision Notice the fact that the regulated person co-operated and give a general description of such co-operation. The enhanced transparency will be welcomed enabling all market users to understand better what benefit, by way of reduction in sanction or otherwise, will stem from co-operation and under what circumstances.

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