

REGULATORY NEWSLETTER

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Enforcement News

SFC reprimands and fines Instinet Pacific Limited \$17.3 million for failures concerning its electronic and algorithmic trading systems and alternative liquidity pool

13 Apr 2018

<http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/enforcement-news/doc?refNo=18PR40>

The SFC has reprimanded and fined Instinet Pacific Limited (IPL) \$17.3 million after resolving concerns over IPL's breaches of the Code of Conduct in relation to its electronic and algorithmic trading systems and alternative liquidity pool (ALP).

In Nov 2016, the SFC and IPL jointly engaged independent reviewers to review IPL's electronic and algorithmic trading systems and ALP. The findings revealed that IPL failed to ensure i) reasonable controls were in place to prevent algorithmic trading system from generating and passing erroneous and disorderly orders to the market, ii) non-proprietary orders received execution priority over proprietary orders in its ALP and iii) compliance with documentary requirement of the Code of Conduct.

SFC reprimands and fines CN Capital Management Limited and responsible officers \$1.2 million over regulatory breaches

24 Apr 2018

<http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/enforcement-news/doc?refNo=18PR42>



Circular Updates

Circular to all Licensed Corporations on Alternative Liquidity Pools

9 Apr 2018

<http://www.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=18EC25>

The SFC conducted a thematic review between 2016 and 2017 to assess compliance with the regulatory requirements for Alternative Liquidity Pools (ALPs) by LCs and to gather information on the latest market developments. The SFC identified a number of deficiencies related to ensuring that ALP users are qualified investors, disclosing information to ALP users, routing orders to third-party ALPs and posting orders to both the ALP and the exchange.

The SFC highlight the following key area of concern:

- ALP operator who route orders to third-party ALPs should i) disclose this in their ALP Guidelines along with the opt-out options for the third-party ALPs and ii) Bring their own ALP Guidelines and the third-party ALP Guidelines to the attention of users to ensure they are fully informed as to the manner in which the third-party ALPs operate

The SFC has reprimanded CN Capital Management Limited (CN Capital) and fined it \$1,000,000 for failing to maintain an effective compliance function and satisfactory internal controls concerning employee account dealing.

The SFC has also reprimanded its responsible officers, Mr George Chan Yee Lee and Mr Stephen Ng Wing Leung and fined them \$100,000 each for failing to comply with the employee account dealing requirements under the Fund Manager Code of Conduct, that they must give their clients priority and avoid conflicts of interest when transacting for themselves.

The investigation between Jan 2011 and Oct 2016 revealed that (i) no CN Capital staff members disclosed their personal investment holdings in writing, (ii) Chan and Ng conducted personal trades and held their personal investments for less than 30 days without written pre-clearance and (iii) personal trades of Chan and Ng were conducted in the same stock and on the same day as the transactions conducted for the fund managed by CN Capital.

- Simultaneous posting of an order to both the ALP and the exchange for more crossing opportunities may alter the order priority in the ALP
- Sufficiently comprehensive information in their ALP Guidelines which includes, but is not limited to, details of the order posting feature and the associated order prioritization should be provided to users
- Design and perform specific testing scenarios to ensure their ALPs operate as disclosed in their ALP Guidelines

[The Report on the Thematic Review of Alternative Liquidity Pools in Hong Kong](#) provides an overview of the ALP landscape in Hong Kong, outlines the areas covered by the thematic review and summarizes the findings and a number of good practices identified. LCs may consider implementing similar controls and mechanism to enhance their AIP control frameworks.