

# SFC publicly censures CLSA Limited, CITIC Securities Brokerage (HK) Limited, Beijing Enterprises Holdings Limited and their representatives for breaching the Code on Share Buy-backs

30 Dec 2019

The Securities and Futures Commission (SFC) has publicly censured the following entities and individuals (Note 1) for buy-back transactions in the shares of Beijing Enterprises Holdings Limited conducted in 2016 in breach of the Code on Share Buy-backs.

- CLSA Limited (Note 2)
- Andrew James WALTERS
- Stuart Richard WILSON
  
- CITIC Securities Brokerage (HK) Limited (CSB) (Note 3)
- Ka Yip Eddy LAU
- King Yuen LAU
- Stephanie LI
  
- Beijing Enterprises Holdings Limited (Note 4)
- Woon Cheung Eric TUNG

In February and May 2016, CLSA on behalf of its institutional clients and CSB on behalf of Beijing Enterprises carried out trades which allowed Beijing Enterprises to buy back more than 18 million of its shares. CLSA and CSB executed these trades on The Stock Exchange of Hong Kong Limited as on-market trades but they were in fact pre-arranged and pre-agreed. The transaction price, size, timing and the manner in which the trades were executed were agreed and coordinated beforehand. These trades were in substance off-market share buy-backs which should have obtained approvals from the Executive (Note 5) and Beijing Enterprises' independent shareholders under Rules 1 and 2 of the Code on Share Buy-backs (Note 6).

In effecting the pre-arranged trades, the conduct of CLSA, CSB and their licensed persons fell short of the standards expected of them under the Codes on Takeovers and Mergers and Share Buy-backs, and shareholders of Beijing Enterprises were deprived of the opportunity to vote on an important corporate action.

Each of the parties accepted that they failed to comply with the Code on Share Buy-backs and consented to the disciplinary action taken against them.

The SFC wishes to take this opportunity to remind practitioners and parties who wish to take advantage of the securities markets in Hong Kong that they should conduct themselves in accordance with the Codes on Takeovers and Mergers and Share Buy-backs. If there is any doubt about their application, the Executive should be consulted at the earliest opportunity.

The [Executive Statement](#) can be found in the "[Listings & takeovers – Takeovers & mergers – Decisions & statements – Executive decisions and statements](#)" on the SFC website.

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Notes:

1. Individuals are listed in alphabetical order below their respective employers at the relevant time.

2. CLSA is licensed to carry out Type 1 (dealing in securities), Type 4 (advising on securities) and Type 7 (providing automated trading services) regulated activities under the Securities and Futures Ordinance (SFO). Andrew James WALTERS was a licensed representative (Type 1) and Head of Block Trading, and Stuart Richard WILSON was a licensed representative (Types 1 and 4) and Managing Director - Head of Equity Syndicate, of CLSA at the relevant time.
3. CSB is licensed to carry out Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities under the SFO. Ka Yip Eddy LAU and King Yuen LAU were responsible officers (Type 1), and Stephanie LI was a licensed representative (Types 1 and 4) and Managing Director - High Networth Brokerage, of CSB at the relevant time.
4. The shares of Beijing Enterprises are listed on the Main Board of The Stock Exchange of Hong Kong Limited. Beijing Enterprises is principally engaged in the distribution and sale of piped natural gas. Woon Cheung Eric TUNG was the Assistant President and General Manager of the Finance Department of Beijing Enterprises at the relevant time.
5. The Executive Director of the SFC's Corporate Finance Division or his delegate.
6. Rule 1 of the Code on Share Buy-backs provides that "a company may only engage in the following types of share buy-back:– (a) an on-market share buy-back; (b) an off-market share buy-back approved in accordance with Rule 2...". Rule 2 provides that "off-market share buy-backs must be approved by the Executive before a repurchasing company acquires any shares pursuant to such share buy-back. Such approval will normally be conditional upon the following:– (a) approval of the proposed off-market share buy-back by at least three-fourths of the votes cast on a poll by disinterested shareholders in attendance in person or by proxy at a general meeting of shareholders duly convened and held to consider the proposed transaction". Rule 2 of the Code on Share Buy-backs is derived from, amongst other things, General Principle 1 of the Codes on Takeovers and Mergers and Share Buy-backs and the fundamental requirement that "all shareholders are to be treated even-handedly and all shareholders of the same class are to be treated similarly".

**The SFC publicly censures CLSA Limited, CITIC Securities Brokerage (HK) Limited, Beijing Enterprises Holdings Limited and their representatives for breaching the Code on Share Buy-backs in respect of share buy-backs conducted by Beijing Enterprises Holdings Limited**

**Introduction**

1. The Securities and Futures Commission (**SFC**) publicly censures the following entities and individuals ("**Individuals**"<sup>1</sup>, and together with the entities, the "**Parties**") in respect of certain buy-back transactions in the shares of Beijing Enterprises Holdings Limited conducted in 2016 in breach of the Code on Share Buy-backs:

CLSA Limited (**CLSA**)  
Andrew James WALTERS (**Mr Walters**)  
Stuart Richard WILSON (**Mr Wilson**)

CITIC Securities Brokerage (HK) Limited (**CSB**)  
Ka Yip Eddy LAU (**Mr Eddy Lau**)  
King Yuen LAU (**Mr KY Lau**)  
Stephanie LI (**Ms Li**)

Beijing Enterprises Holdings Limited (**Beijing Enterprises**)  
Woon Cheung Eric TUNG (**Mr Tung**)

**Background**

2. CLSA is licensed to carry out Type 1 (dealing in securities), Type 4 (advising on securities) and Type 7 (providing automated trading services) regulated activities under the Securities and Futures Ordinance (**SFO**). Mr Walters was a licensed representative (Type 1) and Head of Block Trading, and Mr Wilson was a licensed representative (Types 1 and 4) and Managing Director - Head of Equity Syndicate, of CLSA at the relevant time.
3. CSB is licensed to carry out Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities under the SFO. Mr Eddy Lau and Mr KY Lau were responsible officers (Type 1), and Ms Li was a licensed representative (Types 1 and 4) and Managing Director - High Networth Brokerage, of CSB at the relevant time.
4. CLSA and CSB are subsidiaries of CITIC Securities Company Limited.
5. The shares of Beijing Enterprises (stock code: 392) (**Shares**) are listed on the Main Board of The Stock Exchange of Hong Kong Limited (**Stock Exchange**). Beijing Enterprises is principally engaged in the distribution and sale of piped natural gas. Mr Tung was the Assistant President and General Manager of its Finance Department at the relevant time.

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<sup>1</sup> Individuals are listed in alphabetical order below their respective employers at the relevant time.

## **The buy-backs**

### **17 February 2016 trade (February Trade)**

6. CLSA approached Beijing Enterprises prior to the February Trade and asked if it was interested in acquiring a block of its shares from one of its clients. The February Trade, executed on the Stock Exchange on 17 February 2016, involved the buy-back of 10.362 million Shares at \$34 per share by Beijing Enterprises, which was matched with the sell orders for a total of approximately 10.4 million Shares of an institutional client of CLSA. CLSA acted as broker for the institutional client while CSB acted as broker for Beijing Enterprises.
7. Although the trade was executed on the Stock Exchange, hence was on the face of it on-market, there were in fact communications among various personnel at CLSA, CSB and Beijing Enterprises beforehand. In particular:
  - (a) CLSA's institutional client and Beijing Enterprises, through CLSA and CSB, agreed on the price for and the quantity of the Shares to be bought back;
  - (b) staff of CLSA and CSB discussed the sequencing of the orders to be placed on the Stock Exchange, which allowed CSB to take up 99.5% of the Shares sold by CLSA; and
  - (c) the execution staff at CLSA and CSB coordinated and communicated the timing of execution over unrecorded phone lines when placing the trades.

The above coordination allowed the respective sell and buy orders to be matched almost simultaneously and ensured that Beijing Enterprises bought back the Shares at the agreed price. While the Individuals from CLSA in particular followed existing internal procedures and obtained advice internally, including from a senior execution banker, on the method of execution of the February Trade, the advice received was flawed. No advice was obtained by the employees of CLSA and CSB from their respective compliance or legal departments prior to executing the February Trade to ensure the manner of execution complied with all relevant rules and regulations.

### **11 May 2016 trade (May Trade, and together with the February Trade, "February and May Trades")**

8. The May Trade, executed on the Stock Exchange on 11 May 2016, involved the buy-back of 7.953 million Shares at \$38 per share by Beijing Enterprises from another institutional client of CLSA. Again, CLSA acted as broker for its institutional client while CSB acted as broker for Beijing Enterprises.
9. The May Trade was executed on the Stock Exchange in a similar manner as the February Trade and involved primarily the same personnel from CLSA, CSB and Beijing Enterprises.
10. On 13 May 2016, following enquiries made by the Stock Exchange, the compliance department of CLSA and CSB informed the SFC of the February and May Trades and that these transactions involved at least 11 employees.
11. The Individuals were directly involved in the February and May Trades and knew about the coordinated manner in which they were to be carried out.

## **Relevant provisions of the Codes on Takeovers and Mergers and Share Buy-backs (Codes)**

12. Share buy-back is defined in the Codes as *“a buy-back of shares, or an offer to buy back, redeem or otherwise acquire shares of an offeror made by an offeror, including a privatisation, scheme of arrangement or other form of reorganisation that consists in whole or in part of such an offer.”*
13. Off-market share buy-back is defined as *“a share buy-back that is not a share buy-back by general offer, an exempt share buy-back or an on-market share buy-back.”*
14. On-market share buy-back is defined as *“a share buy-back made by:- (1) a company having a listing on the Stock Exchange through the facilities of the Stock Exchange in accordance with the Listing Rules; ...”*.
15. Rule 1 of the Code on Share Buy-backs provides that: *“[a] company may only engage in the following types of share buy-back:-
  - (a) an on-market share buy-back;
  - (b) an off-market share buy-back approved in accordance with Rule 2;
  - (c) an exempt share buy-back; and
  - (d) a share buy-back by general offer in accordance with the General Principles and Rules of the Codes.”*
16. Rule 2 of the Code on Share Buy-backs provides that *“[o]ff-market share buy-backs must be approved by the Executive<sup>2</sup> before a repurchasing company acquires any shares pursuant to such share buy-back. Such approval will normally be conditional upon the following:-
  - (a) approval of the proposed off-market share buy-back by at least three-fourths of the votes cast on a poll by disinterested shareholders in attendance in person or by proxy at a general meeting of shareholders duly convened and held to consider the proposed transaction...”*

### **The SFC’s comments**

17. Rule 2 of the Code on Share Buy-backs is derived from, among other things, General Principle 1 of the Codes and the fundamental requirement that *“[a]ll shareholders are to be treated even-handedly and all shareholders of the same class are to be treated similarly.”* General Principle 1 of the Codes lies at the heart of the Codes and is fundamental to its operation. An on-market share buy-back should not have implications under General Principle 1 as all shareholders have access to on-market trading and are therefore provided with an equal opportunity to participate in the buy-back. In an off-market share buy-back, however, the offer to buy back shares is only available to a limited number of shareholders. In this sense, the offer is not available to all shareholders and hence shareholders are not treated equally. This is reflected by the high voting

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<sup>2</sup> The Executive refers to the Executive Director of the SFC’s Corporate Finance Division or his delegate.

threshold (75% of the disinterested shares) for shareholder approval of off-market share buy-backs.

18. Although the February and May Trades were executed on the Stock Exchange, they were in fact pre-arranged and were in substance off-market share buy-backs. Therefore, the February and May Trades should have complied with the relevant requirements under Rule 2 of the Code on Share Buy-backs (ie, approvals from the Executive and Beijing Enterprises' independent shareholders should have been obtained). The SFC considers the breaches of the Code on Share Buy-backs in this case to be serious and to merit the present disciplinary sanction.
19. Beijing Enterprises, in conducting the February and May Trades, clearly breached Rules 1 and 2 of the Code on Share Buy-backs. Shareholders of Beijing Enterprises were deprived of the opportunity to vote on an important corporate action. Mr Tung, on behalf of Beijing Enterprises, gave instructions to CLSA and CSB in respect of the February and May Trades.
20. Section 1.7 of the Introduction to the Codes emphasises the importance of the role and responsibility of financial and professional advisers: they should use all reasonable efforts to ensure that their clients understand and abide by the requirements of the Codes. It also provides that they must have the competence, professional expertise and adequate resources to fulfil their role and discharge their responsibility under the Codes.
21. CLSA and CSB, through their employees, played an active role in coordinating and arranging the February and May Trades. At the relevant time, CLSA and CSB did not have proper systems in place to ensure that share buy-back transactions were conducted in accordance with the Code on Share Buy-backs, nor were there any established policies or procedures regarding the conduct of share buy-back transactions or pre-arranged trades in the nature of the February and May Trades. There was no specific requirement for compliance approval to be obtained on a share buy-back transaction.
22. Mr Walters and Mr Wilson were senior members of CLSA involved in the February and May Trades, and Mr Eddy Lau, Mr KY Lau and Ms Li were senior members or responsible officers of CSB involved in the February and May Trades. While the Individuals from CLSA in particular followed existing internal procedures and obtained advice internally, including from a senior execution banker, on the method of execution of the February Trade, the advice received was flawed. Due to CLSA's and CSB's lack of proper systems or established policies and procedures, no CLSA or CSB employees obtained advice from their respective compliance or legal departments prior to conducting the February and May Trades.
23. The conduct of CLSA, CSB and their licensed persons in this case fell short of the standards expected of them under the Codes.
24. The Parties accept that they failed to comply with the Code on Share Buy-backs and consent to the disciplinary action taken against them.
25. The SFC reminds practitioners and parties who wish to take advantage of the securities markets in Hong Kong that they should conduct themselves in matters relating to takeovers, mergers and share buy-backs in accordance with the

Codes. As per section 1.7 of the Codes, advisers are expected to be conversant with the Codes as it is part of their responsibility to ensure their clients understand and abide by the requirements of the Codes. If there is any doubt about the application of the Codes, the Executive should be consulted at the earliest opportunity.

30 December 2019