

AND THEY SHOOT HORSES, TOO

They shoot insider traders in the People's Republic of China (PRC) as well as lame horses.

Some PRC officials see no difference between the two.

Corruption at high levels is, also, a shooting offence in the PRC.

Some PRC officials see no difference between lame horses, that need to be shot, and corrupt PRC Government officials.

English Common Law does not hold with such draconian sentencing of white-collar criminals, unlike the (emerging) Criminal Code of the PRC's Judicial Branch of Government where jurisprudential determinations lean toward deterrent forms of sentencing rather than redressing the balance: Considerations of restoring moral rightness.

Often, in the PRC, deterring certain crimes means forcibly implanting a bullet in the suspected felon's brain: Shoot first; consider reprieve, later.

Effective April 2001, insider trading will become a criminal offence in the Hongkong Special Administrative Region (HKSAR) of the PRC.

This will usher in a new era, opening the door more than a little ajar for other offences to be considered contrary to sections of the Criminal Code of the HKSAR: Chapter 200, The Crimes Ordinance, inter alii.

This is according to The Securities and Futures Bill, which was introduced on April 2, 2000, when the HKSAR Government launched, what it called, '*a three-month consultation exercise*.'

Mr Rafael Hui, Secretary for Financial Services, said, on introducing the wide-sweeping Securities and Futures Bill: '*Hong Kong needs a modern regulatory framework for the securities and futures market to enhance our competitiveness as an international financial centre, and the prime capital formation centre for the Mainland of China ....*

*' ... The Bill, which seeks to meet the 21<sup>st</sup> Century requirements of our market and its users, is now ready for the public comment ...'.*

Under the Bill, criminal sanctions may be imposed on an individual, with the maximum penalty for a person, convicted of market misconduct activities, being raised to 10 years in prison and a fine of \$HK10 million.

This would be an alternative to civil proceedings, instituted by the Market Misconduct Tribunal.

The Bill, also, contains provisions, providing auditors of publicly listed companies to make secret reports to The Securities and Futures Commission (SFC), on a purely voluntary basis, of any suspected fraud or misconduct in the management of publicly listed companies, with the auditors, being afforded immunity from prosecution under Common Law.

There are other, wide-sweeping amendments to existing HKSAR legislation since this new Bill consolidates 10 existing Ordinances.

One new ruling will give the SFC the right to access to the working papers of an auditor of a publicly listed company in a preliminary enquiry into alleged misconduct of the company.

The reason that, under the last British Administration of Hongkong, as the territory used to be called, criminal sanctions, which may have called for the death penalty in the PRC, were never considered to be placed on the statute books, and that included insider trading and corruption offences, was due to the wide divergence of opinion between the thinking of the PRC's Judicial Branch of Government; and, the way in which that Government metered out its kind of punishment to felons and petty criminals, and that which the British considered the appropriate punishment to fit the crime.

Public censure was as far as the last British Governmental Administration of Hongkong decided that it wanted to go: It decided that it did not want to open death's door, even a crack.

With the passing into law in the HKSAR of the new legislation, making it a criminal offence to be caught, indulging in insider trading, it must make some people feel very uncomfortable to learn that, just a few miles north, there is a execution squad, ready, willing and able to put an end to the lives of all those who try, via immoral methods, to increase the size of their bank accounts via insider trading.

The measure of justice is an old, old chestnut in the Western World, roasted to death over open pit fires, but, in today's world, it is not considered appropriate that a man be shot to death for stealing a horse -- or be shot to death for dealing on the inside in a stock play, too.

The definition as to who is to be considered an insider is going to be a tricky one, to be sure, because the determinant factor(s) as to who is, and who is not, an insider should be based on an objective test, not a subjective determination.

At least, that is how the West views its standards of proof.

Will one man in the HKSAR decide who is an insider trader?

Or will there be a panel to consider the matter?

To have one good and true HKSAR Government employee sit in judgment over an alleged insider trader would make such trials go very smoothly, to be sure.

Even if a panel is empowered to make decisions of this nature, will the panel have the courage of its convictions when faced with a powerful mogul, sitting before it, a mogul with considerable political clout ... as well as financial clout?

An insider is, normally, defined as one who has knowledge of facts about a corporation not available to the general public -- officers, directors, key employees, relatives of the above-mentioned, of a corporation, etc.

The (US) Securities Exchange Act of 1934 makes a distinction between a person, being in possession of insider information, and persons, who trade in listed securities, making a secret profit due to his/her privileged position only where he fails to disclose material of a non-public nature.

In determining whether or not a person, not a director or officer of a corporation, is a corporate '*insider*' who, as a purchaser or seller of shares, has a duty to disclose material facts unknown to sellers/buyers, the test is whether or not he or she had such a relationship to the corporation that he or she had access to information which should be used only for corporate purposes and not for personal benefit of anyone.

The present position in regard to insider dealings is that there are 2 exclusive sets of provisions:

- a. Provisions, relating to directors, designed to prevent dealings by them, using undisclosed corporate information; and,
- b. Provisions, relating to shareholders whose primary intention is not that of earning a secret profit, but to build up a substantial stake in a corporation, unbeknown to the controllers of the corporation -- takeovers or having control a substantial block of shares of the corporation.

Insiders, however, need not be officers, senior management or directors of a corporation, since if one takes advantage of a situation whereby he or she has been put in possession of insider information by an insider, then such an individual may be deemed, himself or herself, to be an insider by virtue of the position that he/she holds by accident or design.

A question, which may, soon, be a sticking point, is whether or not a person, coming into contact with insider information, has a duty to disclose that information to The (HKSAR) Securities and Futures Commission if that is to be the Governmental body that will be enforcing the new legislation.

That an officer, making secret use of insider information of a corporate nature, due to his privileged position within a corporation, breaches his duty of fidelity, leaving himself open to a civil action by the company, is unquestionable, but whether or not he or she should be shot for being greedy is something else, again.

The HKSAR is, today, stating that criminal sanctions should be instituted for such acts, leading to 10 years in jail and/or a \$HK10-million fine.

The PRC Government has, already, determined the death sentence is the correct and proper punishment for insider trading activities where an officer of a corporation makes a secret profit, making use of information, known to officers of the corporation, only.

With the HKSAR-PRC border, being a stone's throw away from downtown Hongkong, if a known insider travels to Guangdong, he takes the chance of being shot to death if the PRC Authorities catch him and convict him of insider trading.

It may behoove the Hongkong Police Force not to pursue a suspect, who flees to the PRC, but instead inform their counterparts in the PRC, who can then take the appropriate action as they see fit, making the life of HKSAR policemen much simpler.

(In fact, such cooperative acts have been known to take place in the past)

As for the matter of accountants, making secret reports to the SFC about suspected misconduct/fraud on the part of the management of the company(ies) that they are commissioned to audit, this would appear to be inadvisable since, if an employee of an accounting firm, who determines that he does not like the management of the company that he is auditing on behalf of the shareholders of the company, he can just make an iniquitous report, which, on the surface, may appear to be reasonable.

Years down the line and tens of thousands of dollars later, the corporation, or any and all of its officers, may be exonerated of any wrongdoing, but by then, the damage would have been done.

And the accountant, who made the '*mistaken*' report to the SFC, would still be sticking the knife into those senior management that he did not like, for one reason or another.

Shades of Nazi Germany, one might be tempted to state.

The history of considering what sanctions should be imposed on insiders and insider dealings goes back more than 60 years in the West, dating back to the Cohen Committee, which was first established as a review of British Company Law, prior to the outbreak of World War II, and resulted in the promulgation of the 1948 Act.

As late as 1979, Professor L.C.B. Gower, internationally recognised as an expert on modern company law, made the claim: *'It is a subject which has been under sporadic discussion for over 40 years and under constant debate for the past ten (that was up to 1979), but upon which there has, as yet, been no very effective action in this country (England). It is generally accepted that to make use of inside information is deplorable, but that this nevertheless occurs, though how frequently is uncertain. There is, however, less unanimity on the best way of attempt to prevent it.'*

The PRC Government has a very effective method of dealing with the conundrum: Shoot offenders.

The fear: Will the HKSAR Government, eventually, follow suit; and, is the criminalisation of insider trading phase one in the preparation of accepting the PRC Criminal Code?

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