

SFC reprimands and fines Huatai Financial Holdings (Hong Kong) Limited \$800,000 over naked short selling

17 Sep 2018

The Securities and Futures Commission (SFC) has reprimanded and fined Huatai Financial Holdings (Hong Kong) Limited (Huatai Financial) \$800,000 for failures relating to the short selling of Great Wall Motor Company Limited (Great Wall) shares in 2015 (Note 1).

On 28 August 2015, Great Wall announced its proposed bonus issue of shares, which was equivalent to 200 per cent of its existing issued shares and was subject to the fulfilment of certain conditions. The settlement date of the bonus shares was expected to be on 13 October 2015.

The SFC investigation found that:

- On 30 September 2015, **when the bonus shares started trading on an ex-rights basis**, Huatai Financial's proprietary desk manually booked an entry in its trading system to reflect Huatai Financial's entitlement to 360,000 bonus shares as a result of its pre-existing holding of 180,000 Great Wall shares. The entry caused Huatai Financial's trading system to show a total of 540,000 Great Wall shares as a single position without differentiating between its pre-existing holding of 180,000 shares and the 360,000 bonus shares which had not yet been settled.
- On 6 October 2015, without performing any checks or verifications, a proprietary trader of Huatai Financial assumed that the bonus shares had become unconditional and placed an order to sell 500,000 shares of Great Wall, causing Huatai Financial to become short by 320,000 shares in Great Wall (Notes 2 & 3).

The SFC considers that Huatai Financial failed to act with due skill, care and diligence in dealing in the bonus shares and to diligently supervise its staff members and implement adequate and effective systems and controls to ensure compliance with the short selling requirements.

In deciding the sanctions against Huatai Financial, the SFC took into account that:

- the dealing in the bonus shares involved a single, unintentional short sale;
- Huatai Financial self-reported the regulatory breach to the SFC;
- there is no evidence to suggest that Huatai Financial had acted in bad faith in short selling the bonus shares;
- Huatai Financial has taken remedial measures to strengthen its internal controls and systems;
- Huatai Financial has cooperated with the SFC in resolving the SFC's concerns; and
- Huatai Financial has an otherwise clean disciplinary record.

End

Notes:

1. Huatai Financial is licensed under the Securities and Futures Ordinance (SFO) to carry on Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities.
2. Section 170(1) of the SFO prohibits "naked" or "uncovered" short selling. It is a criminal offence for a person to sell securities at or through a recognised stock market unless at the time of the sale, he has a presently exercisable and unconditional right to vest the securities in the purchaser of them, or believes and has reasonable grounds to believe that he has such a right.
3. Prior to the settlement date, Great Wall did not make any public announcement regarding the fulfilment of the conditions. The public did not have reasonable grounds to believe that they had presently exercisable and unconditional rights to vest the bonus shares in the purchaser of them before the settlement date.

[A copy of the Statement of Disciplinary Action is available on the SFC website](#)

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STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded Huatai Financial Holdings (Hong Kong) Limited (**Huatai Financial**)¹ and fined it \$800,000 pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. The disciplinary action is taken in respect of a short selling incident in relation to the shares of Great Wall Motor Company Limited (stock code: 2333) (**Great Wall**).

Summary of facts

Background

3. On 28 August 2015, Great Wall issued an announcement (**Announcement**) regarding its proposed bonus issue of shares (**Bonus Shares**) of 200% of its existing issued shares (**Bonus Issue**). The Bonus Issue was subject to the fulfilment of certain conditions (**Conditions**). According to the timetable set out in the Announcement, the Bonus Shares were expected to be despatched on 13 October 2015 (**Settlement Date**).
4. Prior to the Settlement Date, Great Wall did not make any public announcement regarding the fulfilment of the Conditions. The public did not have reasonable grounds to believe that they had presently exercisable and unconditional rights to vest the Bonus Shares in the purchaser of them before the Settlement Date².

Disposal of the Bonus Shares before the Settlement Date

5. As at 30 September 2015, i.e. the ex-entitlement date of the Bonus Issue (**Ex-Date**), Huatai Financial owned 180,000 shares of Great Wall. Pursuant to the Bonus Issue, it was entitled to an additional 360,000 Bonus Shares of Great Wall.
6. On 30 September 2015, Huatai Financial's proprietary desk manually booked an entry in Huatai Financial's Asset and Investment Management System (**AIMS System**) to reflect Huatai Financial's entitlement to the 360,000 Bonus Shares.
7. After the entry, the AIMS System showed a total of 540,000 Great Wall shares as one position without differentiating between the initial 180,000 shares and the 360,000 Bonus Shares which had not yet been settled.

¹ Huatai Financial is licensed to carry on business in in Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities under the SFO.

² Section 170(1) of the SFO prohibits "naked" or "uncovered" short selling. It is a criminal offence for a person to sell securities at or through a recognized stock market unless at the time of the sale, he has a presently exercisable and unconditional right to vest the securities in the purchaser of them, or believes and has reasonable grounds to believe that he has such a right.

8. On 6 October 2015, a proprietary trader of Huatai Financial placed an order to sell 500,000 Great Wall shares (**Disposal**). The Disposal caused Huatai Financial to become short by 320,000 shares in Great Wall (**Net Short Position**).

The SFC's findings

9. The SFC found that:
 - (a) The proprietary trader responsible for handling the Disposal knew that the Bonus Issue was subject to the fulfillment of the Conditions. However, without performing any checks or verifications, he assumed that the Conditions had been fulfilled after the Ex-Date.
 - (b) Although the Settlement Date was stated in the Announcement as well as in the email sent from his colleague to him on 30 September 2015, the proprietary trader did not pay attention to such information.
 - (c) In the mistaken belief that Huatai Financial had presently exercisable and unconditional rights to sell the Great Wall shares reflected in the AIMS System, including the Bonus Shares, he placed the Disposal order on 6 October 2015.
10. The SFC also found that at the time when the Disposal was executed, Huatai Financial did not have formal policy in place governing the booking of bonus shares. There was also no control in place to alert the proprietary trader to the fact that the Bonus Shares had not yet been settled and were not available for trading.

The SFC's concerns

11. The SFC considers that Huatai Financial had:
 - (a) failed to act with due skill, care and diligence in handling and dealing in the Bonus Shares; and
 - (b) failed to diligently supervise its staff members and implement adequate and effective systems and controls to ensure compliance with the short selling requirements.

Conclusion

12. In deciding the disciplinary sanctions set out at paragraph 1, the SFC has taken into account that:
 - (a) the dealing in the Bonus Shares involved a single, unintentional short sale;
 - (b) Huatai Financial self-reported the regulatory breach to the SFC;
 - (c) there is no evidence to suggest that Huatai Financial had acted in bad faith in short selling the Bonus Shares;
 - (d) Huatai Financial has taken remedial measures to strengthen its internal controls and systems;

- (e) Huatai Financial has cooperated with the SFC in resolving the SFC's concerns; and
- (f) Huatai Financial has an otherwise clean disciplinary record.