

COMMISSION IMPLEMENTING DECISION (EU) 2017/2319**of 13 December 2017****on the equivalence of the legal and supervisory framework applicable to recognised exchange companies in Hong Kong Special Administrative Region in accordance with Directive 2014/65/EU of the European Parliament and of the Council****(Text with EEA relevance)**

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU ⁽¹⁾, and in particular Article 25(4)(a) thereof,

Whereas:

- (1) Article 23(1) of Regulation (EU) No 600/2014 of the European Parliament and of the Council ⁽²⁾ requires investment firms to ensure that the trades they undertake in shares admitted to trading on regulated markets, or traded on trading venues should take place on regulated markets, multilateral trading facilities (MTFs) or systematic internalisers, or third-country trading venues assessed by the Commission as equivalent in accordance with Article 25(4)(a) of Directive 2014/65/EU.
- (2) Article 23(1) of Regulation (EU) No 600/2014 only applies a trading obligation in respect of shares. The trading obligation does not comprise other equity instruments, such as depositary receipts, ETFs, certificates and other similar financial instruments.
- (3) The equivalence procedure for trading venues established in third countries set out in Article 25(4)(a) of Directive 2014/65/EU aims to allow investment firms to undertake trades in shares that are subject to the trading obligation in the Union, on third-country trading venues recognised as equivalent. The Commission should assess whether the legal and supervisory framework of a third country ensures that a trading venue authorised in that third country complies with legally binding requirements which are equivalent to the requirements resulting from Regulation (EU) No 596/2014 of the European Parliament and of the Council ⁽³⁾, from Title III of Directive 2014/65/EU, from Title II of Regulation (EU) No 600/2014 and from Directive 2004/109/EC of the European Parliament and of the Council ⁽⁴⁾, and which are subject to effective supervision and enforcement in that third country. This should be read in the light of the objectives pursued by that act, in particular its contribution to the establishment and functioning of the internal market, market integrity, investor protection and ultimately, but no less importantly, financial stability.
- (4) In accordance with the forth subparagraph Article 25(4)(a) of Directive 2014/65/EU, a third-country legal and supervisory framework may be considered equivalent where that framework fulfils at least the conditions that (a) the markets are subject to authorisation and to effective supervision and enforcement on an ongoing basis, (b) have clear and transparent rules regarding the admission of securities to trading so that such securities are capable of being traded in a fair, orderly and efficient manner, and are freely negotiable, (c) security issuers should be subject to periodic and ongoing information requirements ensuring a high level of investor protection, and (d) market transparency and integrity should be ensured by the prevention of market abuse in the form of insider dealing and market manipulation.

⁽¹⁾ OJ L 173, 12.6.2014, p. 349.

⁽²⁾ Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (OJ L 173, 12.6.2014, p. 84).

⁽³⁾ Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC (OJ L 173, 12.6.2014, p. 1).

⁽⁴⁾ Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (OJ L 390, 31.12.2004, p. 38).

- (5) The purpose of this equivalence assessment is to assess, inter alia, whether the legally binding requirements which are applicable in Hong Kong to recognised exchange companies established and authorised under the Hong Kong Securities and Futures Ordinance (SFO) ('recognised exchange companies') and supervised by the Securities and Futures Commission ('SFC') are equivalent to the requirements resulting from Regulation (EU) No 596/2014, from Title III of Directive 2014/65/EU, from Title II of Regulation (EU) No 600/2014 and from Directive 2004/109/EC, which are subject to effective supervision and enforcement in that third country.
- (6) As regards the conditions that the markets are subject to authorisation and to effective supervision and enforcement on an ongoing basis, under the SFO (Chapter 571 of the Laws of Hong Kong) the recognised exchange company must operate a multilateral system in accordance with non-discretionary rules. It does not enjoy discretion over how it executes trades and is not allowed to trade on its own account or engage into matched principal trading. Furthermore, a recognised exchange company must provide members with impartial access to its markets and services. The access criteria must be impartial, transparent, and applied in a non-discriminatory manner. To this effect, operating rules of a recognised exchange company must have reasonable and non-discriminatory standards for access and eligibility requirements. The Rules of the Exchange are reviewed and approved by the SFC. To access the trading system of a recognised exchange company, it is necessary to become an exchange participant of the recognised exchange company. Exchange participants must meet certain criteria. Among other things, they must be a company incorporated in HK, licensed under Section 116(1) of the SFO and hold a valid business registration certificate under the Business Registration Ordinance.
- (7) The four conditions set out in the fourth subparagraph of Article 25(4)(a) of Directive 2014/65/EU must be fulfilled in order to determine that the legal and supervisory arrangements of a third country regarding the trading venues authorised therein are equivalent to those laid down in Directive 2014/65/EU.
- (8) According to the first condition, third-country trading venues must be subject to authorisation and to effective supervision and enforcement on an ongoing basis.
- (9) Section 19(1)(a) of the SFO provides that no person shall operate a stock market unless the person is a recognised exchange company. The SFC may recognise a company as an exchange company if it is satisfied that doing so is in the interest of the investing public or in the public interest or for the proper regulation of the securities markets. The SFC may, after consultation with the public and then with the Financial Secretary of Hong Kong Special Administrative Region, grant recognition to a company as an exchange company. The SFC may also, with the consent of the Financial Secretary, grant recognition to an exchange controller. The recognition may be subject to conditions imposed by the SFC. Once recognised, a recognised exchange company which operates a stock market has the duty to ensure an orderly, informed and fair market in securities traded on its subsidiary exchanges. In accordance with Division 2 to 4 of Part III of the SFO, a recognised exchange company must ensure that risks associated with its business and operations are managed prudently. In discharging these duties, it has to act in the interest of the public, having particular regard to the interest of the investing public, and must ensure that the interest of the public prevails where it conflicts with the interest of the recognised exchange company or that of the recognised exchange controller. The recognised exchange company must comply with any lawful requirement placed on it under any enactment or rule of law and with any other legal requirement.
- (10) The SFC is the regulator of the securities markets in Hong Kong. Under Part III of the SFO, the SFC is responsible for supervising, monitoring and regulating activities carried out by recognised exchange companies and recognised exchange controllers. The SFC monitors a recognised exchange company to assess whether it complies with its statutory duties on an initial and ongoing basis. If the recognised exchange company fails to comply with such duties, the SFC has the power to take appropriate actions set out in Part III of the SFO. Sections 28 and 72 of the SFO provide that the SFC may withdraw the company's recognition as an exchange company. Under the SFO, the SFC has regulatory, administrative and investigative powers and may impose court orders by civil proceedings in accordance with Sections 213 and 214 of the SFO, administrative or criminal sanctions, as well as initiate or refer matters for criminal prosecution. Furthermore, pursuant to Section 399(1) of the SFO the SFC may publish codes and guidelines as it considers appropriate for providing guidance for the furtherance of any of its regulatory objectives, functions and the operation of any provision of the SFO. Recognised exchange companies are responsible for the establishment and enforcement of its own trading rules to ensure compliance

by their EPs. To ensure continuing compliance with the SFO requirements, the SFC may review and audit the operations of the recognised exchange companies and recognised exchange controllers, their electronic trading and clearing systems and risk management. Under Section 23 of the SFO, the SFC may direct a recognised exchange company to make or amend any rules which it is permitted to make under that provision. The SFC may require a recognised exchange company to provide books, records and other information of its business or in respect of any trading in securities. The SFC can also order a recognised exchange companies to take particular actions, including requiring a recognised exchange company to take such action relating to the management, conduct or operation of their business or prohibit them from actions relating to the management, conduct or operation of their business specified in the Restriction Notice as per Section 92(1) of the SFO. Further, under Section 29 of the SFO, the SFC has the power to suspend dealings in securities and close a recognised exchange company in case it is of the opinion that orderly trading on the stock market is threatened. The SFO empowers the SFC to impose disciplinary measures (Part IX of the SFO) and prosecute offenders for securities related misconduct (Section 388 of the SFO). The SFC's surveillance and disciplinary oversight extend beyond listed companies and licensees to market participants, including investors. The SFC has powers under the SFO to take disciplinary, civil and criminal actions for market misconduct. Under Part XIII of the SFO the SFC has recourse to the Market Misconduct Tribunal and, where appropriate, imposing civil sanctions. Respectively, under Part XIV of the SFO the SFC can refer a case to the criminal law courts. Where appropriate the SFC may also seek warrants to search premises in accordance with Section 191 of the SFO and cooperate with domestic and overseas regulatory bodies to conduct investigations pursuant to Section 186 of the SFO.

- (11) The 2001 Memorandum of Understanding (MOU) entered into between the exchange controller and the SFC on Matters relating to SFC Oversight, Supervision of Exchange Participants and Market Surveillance requires recognised stock exchanges to provide data and information to the SFC on a regular or ad hoc basis. For monitoring purposes the SFC has access to orders and transaction information on a real-time basis. Under Item 16 of appendix II of the MOU, recognised exchange companies are required to, as soon as practicable, notify the SFC of matters designated as serious, and share information with the SFC within prescribed time periods as agreed between both parties. Under Section 27 of the SFO, the SFC may require a recognised exchange company to provide books and records kept in connection with or for the purposes of its business or in respect of any financial instruments traded; and such other information relating to its business or any trading in securities, futures contracts or OTC derivative products. Recognised exchange companies are required to keep records of all orders and transactions relating to any financial instruments which the SFC may reasonably require for the performance of its functions. They are required to keep those records for a period of not less than seven years.
- (12) It can therefore be concluded that recognised exchange companies in Hong Kong are subject to authorisation and to effective supervision and enforcement on an ongoing basis.
- (13) According to the second condition, third-country trading venues must have clear and transparent rules regarding admission of securities to trading so that such securities are capable of being traded in a fair, orderly and efficient manner, and are freely negotiable.
- (14) A recognised exchange company's statutory duty under the section 21 of the SFO is to ensure an orderly, informed and fair market. Listing rules are requirements set out in the exchange rulebook in compliance with the SFO where the market operator establishes its internal rules to ensure the provision of a fair, orderly and efficient market for the trading of securities and require that the issue of securities is conducted in a fair and orderly manner, and that all holders of issued securities are treated fairly and equally. The listing rules contain the basic qualification requirements for listing of securities. These rules also comprise requirements which have to be met before securities may be listed and also continuing obligations with which an issuer must comply once listing has been approved. According to Section 24 of the SFO, the SFC must approve those listing rules. An applicant for listing must be duly incorporated, must satisfy certain capital requirements, disclosure requirements and have sufficient management presence in Hong Kong. Both the applicant and its business must, in the opinion of the market operator, be suitable for listing. A recognised exchange company retains an absolute discretion to accept or reject applications for listing. Any waiver from the listing rules can only be granted on a case-by-case basis having regard to the circumstances of a particular case. Where such waiver is intended to have a general effect, it may only be granted with the prior consent of the SFC. A recognised exchange company must certify to the SFC that the security has been approved for listing and quotation. The securities must be freely transferable and meet

certain criteria regarding the distribution of securities to the public. Finally, to secure orderly trading of securities, the SFC can suspend trading in a financial product or class of financial products traded on a recognised exchange company.

- (15) As part of its duty to ensure an orderly, informed and fair trading, a recognised exchange company must ensure an appropriate level of trade transparency on a timely and equitable basis. The pre-trade information includes best bid and ask quotations, price and order depth. The full order book, including current bid and offer prices and depth of trading interest at those prices, is made public on a continuous and real-time basis during the continuous trading session. Market participants can access the pre-trade information directly via the market data systems of exchanges or indirectly through information vendors. There are no exemptions from pre-trade transparency. Transactions carried out on a recognised exchange are subject to post-trade disclosure of information. Transaction details with regards to on-exchange transactions are disseminated on a real time basis and include, inter alia, prices, closing prices, and market turnover information. Market participants can access the post-trade information directly via the market data systems of exchanges or indirectly through information vendors.
- (16) It can therefore be concluded that recognised exchange companies in Hong Kong have clear and transparent rules regarding the admission of securities to trading so that such securities are capable of being traded in a fair, orderly and efficient manner and are freely negotiable.
- (17) According to the third condition, security issuers must be subject to periodic and ongoing information requirements ensuring a high level of investor protection.
- (18) The listing rules of a recognised exchange company are required to have clear, comprehensive and specific disclosure requirements applying to annual and interim reports. Issuers whose securities are admitted to trading are required to publish annual financial statements and half-yearly financial reports as set out in the rulebook of the exchange. The reports must be audited and comply with generally accepted accounting standards. A recognised exchange company must monitor issuers' ongoing compliance with the disclosure obligations under the Listing Rules. In addition, a recognised exchange company also reviews issuers' annual reports with a focus on issuers' listing rules compliance and their disclosure of material events and developments as part of its ongoing monitoring and compliance activities. The SFC carries out active surveillance of company activities and in-depth reviews of selected listed companies with a view to identifying any corporate non-compliance or misbehaviour. The disclosure of comprehensive and timely information about security issuers allows investors to assess the business performance of issuers and ensures appropriate transparency for investors through a regular flow of information.
- (19) It can therefore be concluded that issuers of securities admitted on recognised exchange companies in Hong Kong are subject to periodic and ongoing information requirements ensuring a high level of investor protection.
- (20) According to the fourth condition, the third-country legal and supervisory framework must ensure market transparency and integrity by preventing market abuse in the form of insider dealing and market manipulation.
- (21) The securities laws of Hong Kong establish, as further set out below, a comprehensive regulatory and supervisory framework to ensure market integrity, prohibit fraudulent or deceptive conduct on recognised exchange companies and dissemination of false or misleading information regarding securities or issuers, as well as to prevent insider trading and market manipulation. The SFO regulates market abuse and establishes civil and criminal regimes in respect of market misconduct. Market misconduct, as defined by the SFO, encompasses six offences, i.e. insider dealing under Sections 270 and 291 of the SFO, false trading under Sections 274 and 295 of the SFO, price rigging under Sections 275 and 296 of the SFO, disclosure of information about prohibited transactions under Sections 276 and 297 of the SFO, disclosure of false and misleading information inducing transactions under Sections 277 and 298 of the SFO and market manipulation under Sections 278 and 299 of the SFO. Offences under the civil regime are heard by the Market Misconduct Tribunal before which the SFC may institute proceedings. For offences under the criminal regime the SFC has power to conduct summary prosecutions in the Magistrate Courts. According to Section 107 of the SFO, the SFC may seek criminal sanctions against persons who induce another to buy or sell securities by fraudulent or reckless misrepresentation or, under Section 298 of the SFO, against persons who disclose false or misleading information likely to induce another to buy securities. Under Section 277 of the SFO, the latter behaviour is also considered misconduct under the civil market misconduct regime. Furthermore, Section 300 of the SFO sets out criminal liabilities for persons who use in a securities transaction deceptive or fraudulent conduct, device or scheme with intention to defraud or deceive.

Section 384 of the SFO establishes a criminal liability for persons knowingly or recklessly giving false or misleading information to the SFC or the recognised exchange controller. Where a corporation is found guilty of an offence, Section 390 of the SFO extends criminal liability to any officer of the corporation who consented, connived or was reckless to the commission of the offence.

- (22) It can therefore be concluded that the legal and supervisory framework in Hong Kong ensures market transparency and integrity by preventing market abuse in the form of insider dealing and market manipulation.
- (23) It can therefore further be concluded that the legal and supervisory framework governing recognised exchange companies operated in Hong Kong under the supervision of the SFC comply with the four conditions for legal and supervisory arrangements and hence should be considered to provide for an equivalent system to the requirements for trading venues laid down in Directive 2014/65/EU, Regulations (EU) No 600/2014 and (EU) No 596/2014 and Directive 2004/109/EC.
- (24) Given that a significant number of EU issued shares admitted to trading and traded on EU trading venues are also traded on trading venues in Hong Kong, Hong Kong trading venues often act as additional centres of liquidity for those EU issued shares. This feature allows EU investment firms to trade in EU issued shares admitted to trading and traded on EU venues outside business hours of the EU trading venues. The recognition of the legal and supervisory framework of Hong Kong would preserve the ability of EU investment firms to continue trading in EU issued shares outside business hours of EU trading venues
- (25) This decision is based on data that demonstrates that overall EU trading in a number of shares admitted on exchanges in Hong Kong is of such frequency that MiFID firms could not avail themselves of the exception set out in Article 23(1)(a) of Regulation (EU) No 600/2014. This implies that the trading obligation set out in Article 23(1) of Regulation (EU) No 600/2014 would apply to a significant number of shares admitted to trading in Hong Kong.
- (26) The decision will be complemented by cooperation arrangements to ensure the effective exchange of information and coordination of supervisory activities between the national competent authorities and the SFC.
- (27) This Decision is based on the legally binding requirements relating to recognised exchange companies applicable in Hong Kong at the time of the adoption of this Decision. The Commission should continue monitoring on a regular basis the evolution of the legal and supervisory arrangements for these trading venues, market developments, the effectiveness of supervisory cooperation in relation to monitoring and enforcement and the fulfilment of the conditions on the basis of which this Decision has been taken.
- (28) The Commission should conduct the regular review of the legal and supervisory arrangements applicable to recognised exchange companies in Hong Kong. This is without prejudice to the possibility of the Commission to undertake a specific review at any time, where relevant developments make it necessary for the Commission to reassess the equivalence granted by this Decision. Any reassessment could lead to the repeal of this Decision.
- (29) Considering that Regulation (EU) No 600/2014 and Directive 2014/65/EU apply from 3 January 2018, it is necessary that this decision enters into force on the day following the day of publication in the *Official Journal of the European Union*.
- (30) The measures provided for in this Decision are in accordance with the opinion of the European Securities Committee,

HAS ADOPTED THIS DECISION:

Article 1

For the purposes of Article 23(1) of Regulation (EU) No 600/2014 the legal and supervisory framework in Hong Kong Special Administrative Region applicable to recognised exchange companies authorised therein and as set out in the Annex to this Decision shall be considered to be equivalent to the requirements resulting from Directive 2014/65/EU, Regulations (EU) No 600/2014 and (EU) No 596/2014 and Directive 2004/109/EC and to be subject to effective supervision and enforcement.

Article 2

This Decision shall enter into force on the day following that of its publication in the *Official Journal of the European Union*.

Done at Brussels, 13 December 2017.

For the Commission
The President
Jean-Claude JUNCKER

ANNEX

Recognised exchange companies:

The Stock Exchange of Hong Kong Limited (SEHK)
