Speech by Ms Teresa Cheng, SC
Secretary for Justice
3rd IBA Asia-based International Financial Law Conference
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Ms Vivian Lam [Conference Chair], Mr Paul Christopher [Host Committee Chair], Distinguished Guests, Ladies and Gentlemen,

It is my great pleasure and honour to join you this morning at the 3rd IBA Asia-based International Financial Law Conference.

2. First of all, on behalf of the Government of the Hong Kong Special Administrative Region ('HKSAR'), I would like to extend our warmest welcome to all the participants of this Conference.

3. Hong Kong is acclaimed globally for our status as an international financial centre. Such reputation is attributed to our rule of law, friendly business environment, sound regulatory regime, and importantly our soft power, human talents that gravitate to Hong Kong. The Heritage Foundation's 2018 Index of Economic Freedom report[1] ranks Hong Kong as the world's freest economy for 24 consecutive years. The latest Global Financial Centres Index[2] ranks Hong Kong first in Asia and third globally, just behind London and New York.

4. The sound legal framework, rules and regulations have long been the cornerstone of the financial industry in Hong Kong. The legal infrastructure for the financial industry in Hong Kong is supported by two major pillars which are: firstly, the common law; and secondly, the statutory regulatory scheme.

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1 Press release for the Heritage Foundation's 2018 Index of Economic Freedom report, 2 February 2018 (https://www.heritage.org/press/2018-index-economic-freedom-global-economic-freedom-hit-all-time-high)

2 Page 4, the Global Financial Centres Index 22, September 2017 (http://www.longfinance.net/images/gfci/gfci_22.pdf)

5. I will speak briefly this morning on certain aspects of these two elements. I will start by outlining the crucial role of the common law in Hong Kong. I will then follow with a discussion of the role and recent initiatives of the Securities and Futures Commission ('SFC') and Hong Kong Monetary Authority ('HKMA') in promoting investor protection and corporate governance in Hong Kong. In my discussion, I will mention some examples of legal developments in Hong Kong and their relationship with SFC and HKMA in promoting Hong Kong as an international financial centre.

Common law in Hong Kong

6. The historical past of many places in Asia including Hong Kong has resulted in such jurisdictions inheriting a common law system. Despite a common legal ancestry, these common law jurisdictions have, for quite some time, been developing their own body of common law jurisprudence according to their respective economic, social and financial circumstances.

7. After China's resumption of the exercise of sovereignty over Hong Kong in 1997, the Basic Law of the HKSAR provides a guarantee for an independent judiciary (Articles 2, 19 and 85), an independent prosecutorial function of the Department of Justice (Article 63) and relevantly, the continuity of the common law system. Article 8 provides that '[t]he laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene [the Basic Law], and subject to any amendment by the legislature of the [HKSAR]'.

8. Under the Basic Law, the courts of the HKSAR, in adjudicating cases, may refer to precedents of other common law jurisdictions (Article 84). Moreover, the Basic Law (Article 92) specifically provides for judges to be chosen on the basis of their judicial and professional qualities, and may be recruited from other common law jurisdictions. Judges from other common law

jurisdictions may be invited to sit on the Court of Final Appeal ('CFA') (Article 82). As at February 2018, there are 12 Non-Permanent Judges from other common law jurisdictions sitting from time to time on the CFA. These judges are of the highest international standing, including leading retired or serving judges of the UK Supreme Court and the High Court of Australia. The overseas Non-Permanent Judges have written or contributed to, many of the CFA's leading judgments, and their judgments have also been cited in final appellate courts in other jurisdictions, constituting an important source in the common law jurisprudence.

9. The independence of the Judiciary in Hong Kong is well recognised internationally. In the Global Competitiveness Reports of the World Economic Forum, Hong Kong's judicial independence ranked first in Asia for the past three years.

10. Against this constitutional background, Hong Kong does not only maintain but also continues to develop its case law whilst upholding our rule of law. According to the Worldwide Governance Indicators Project of the World Bank, which provides trends over longer periods rather than year on year fluctuations only, Hong Kong's percentile ranking in rule of law has improved from 69.9% in 1996 to 93.3% in 2016[3] over 20 years, or a leap from a top 70 place to a top 15 place. These statistics suggest an upward trend of the rule of law in Hong Kong.

11. A paper written by two academia in the United States concerning a comparative study of Asian common law systems published in the Asian Journal of Comparative Law[4] in December 2017 refers to Hong Kong, Malaysia and Singapore, which, in the authors' views, are three of the most active and vibrant common

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[3] See website of the Worldwide Governance Indicators (http://info.worldbank.org/governance/wgi/#doc).

[4] Kwai Hang NG and Brynna JACOBSON of the University of California, San Diego, 'How Global is the Common Law? A Comparative Study of Asian Common Law Systems – Hong Kong, Malaysia, and Singapore', Asian Journal of Comparative Law, 12 (2017), pp. 209–232, published online on 30 August 2017, copyright owned by the National University of Singapore, 2017

law systems in Asia. These legal systems, the authors opined, are more global and transnational than perhaps the common law practised elsewhere. The authors have drawn, amongst others, the following conclusions empirically and I would like to share some of their observations:

(a) *"……the common law in Asia is not positioned as a set of local laws rooted in common customs or practices, but as a globalized system of law that operates as a well-tested set of legal know-hows……foreign cases are prominently used in the three jurisdictions."*; and

(b) *"Today, English court decisions remain the biggest category of foreign citations. However, even putting aside the English cases, there remains a substantial level of foreign cases from other established common law countries, including Australia, Canada, New Zealand, India, and the United States that cannot be overlooked. There are also cross-citations among the three jurisdictions, albeit unevenly distributed."*

12. This comparative study of the Asian common law systems further notes that:

> *"Compared to Singapore and Malaysia, English decisions play an even stronger role in the foreign judgments cited [in Hong Kong]. Among Hong Kong cases that cite to foreign decisions, 66 per cent of them directly cited to English cases exclusively with no other foreign citations. By comparison, the figures are 40 per cent for Malaysia and 34 per cent for Singapore. Citation to English law is a powerful way to signal the continuity of its English common law heritage. Hong Kong remains the jurisdiction that stays closest to the decisions of English courts."*

Developments in case law in financial sector

13. Turning to financial law, although much of the legal infrastructure and regulatory regime in Hong Kong is constituted by statutory-based regulation, case law continues to have a pivotal role.

14. The global financial crisis of 2008 gave rise to litigation in various jurisdictions as investors sought remedies for damages suffered as a result of mis-selling of financial products[5][6].

15. The common allegations made by plaintiffs in these cases were that they were unsophisticated investors and relied on the financial institutions for advice in making investments, while the financial institutions breached their various duties by misrepresenting the nature or risk-level of the investments or by failing to adequately advise the investors of the risks of the complex financial instruments that were promoted to them.

16. The plaintiffs in the earlier decisions in Hong Kong were generally unsuccessful in their claims[7]. The basis of the decisions tend to be the 'non-advisory' and 'non-reliance' clauses in the client agreements and standard terms of business.

17. In the recent Court of Appeal decision in *Chang Pui Yin v Bank of Singapore Ltd*[8], the court held that the

[5] In Hong Kong, for example, cases include Kwok Wai Hing Selina v HSBC Private bank (Suisse) SA [2012] 4 HKC 260; DBS Bank (Hong Kong) Ltd v San-Hot HK Industrial Co Ltd [2013] 4 HKC 1; Shum Kin Yee v DBS Bank Hong Kong Ltd (unreported, DCCJ 1726/2011, 31 July 2013); DBS Bank (Hong Kong) Ltd v Sit Pan Jit (unreported, CACV 91/2015, 10 June 2016) (leave to appeal refused by the CFA: FAMV 45/2016, 17 February 2017); Zhang Hong Li v DBS Bank (Hong Kong) Ltd (unreported, HCCL 2/2011, 13 April 2017); Chang Pui Yin v Bank of Singapore Ltd [2017] 4 HKLRD 458; Li Kwok Heem John v Standard Chartered International (USA) Ltd [2016] 1 HKC 535, etc.

[6] In Singapore, for instance, cases include ALS Memasa v UBS AG [2012] SGCA 43; Deutsche Bank AG v Chang Tse Wen [2013] SGCA 49; Tradewaves Ltd v Standard Chartered Bank [2017] SGHC 93], etc.

[7] *Kwok Wai Hing Selina v HSBC Private bank (Suisse) SA* [2012] 4 HKC 260; *DBS Bank (Hong Kong) Ltd v San-Hot HK Industrial Co Ltd* [2013] 4 HKC 1; *DBS Bank (Hong Kong) Ltd v Sit Pan Jit* (unreported, CACV 91/2015, 10 June 2016).

[8] [2017] 4 HKLRD 458.

‘non-reliance’ and ‘non-advisory’ clauses were unconscionable under the Unconscionable Contracts Ordinance and that they were exemption clauses which did not satisfy the test of reasonableness under the Control of Exemption Clauses Ordinance. Accordingly, the bank was unable to rely on them.

18. The plaintiffs were an elderly couple, Mr and Mrs Chang, and a company solely owned by Mrs Chang for her investments. The judge found that the Changs had limited investment knowledge and their investment objective had always been to preserve their capital and achieve a return slightly better than bank deposits. The Changs’ relationship manager at the bank, however, recommended high risk products to them. By August 2008, substantial losses were incurred in the Changs’ investment accounts.

19. The central issue before the Court of Appeal was whether the bank owed any and if so what duties to the plaintiffs in light of the ‘non-reliance’ and ‘non-advisory’ clauses.

20. Referring to a number of UK decisions, the court accepted that even a salesperson can owe a low level duty of care not to make any negligent misstatements and to use reasonable care not to recommend a highly risky investment without pointing out that it was such. The court relied on the House of Lords decision in *Customs and Excise Commissioners v Barclays Bank plc*[9].

21. Lord Hoffmann held that whether a defendant has assumed responsibility does not depend on what the defendant subjectively intended, but is a legal inference to be drawn from the defendant’s conduct against the background of all the circumstances of the case. In this context, the construction of the ‘non-reliance’ and ‘non-advisory’ clauses became relevant and an important background to the findings in that case.

[9] [2007] 1 AC 181.

22. Cases[10] such as *Chang Pui Yin* illustrate the continuing importance of the common law, as supplemented by various consumer or investor protection legislation, in structuring the relationships between parties in the financial services industry in Hong Kong.

23. While Hong Kong courts have dealt with a number of cases arising from the 2008 financial crisis, many more cases have been resolved by mediation. In October 2008, the HKMA engaged the Hong Kong International Arbitration Centre to draw up a Lehman Brothers-Related Investment Products Dispute Mediation and Arbitration Scheme. The Scheme was launched in November 2008; and as at the end of 2012, a total of 143 mediations had taken place with a settlement rate of 89%.

24. Following the success of that Scheme, the Government set up a Financial Dispute Resolution Centre ('FDRC') in June 2012 to assist financial institutions and their clients to resolve monetary disputes through mediation or arbitration.

25. Currently, subject to the parties' consent, the FDRC may also handle cases with a claim outside its Terms of Reference, i.e. $1,000,000 or beyond the 24 months limitation period under the scheme. The success rate in mediation cases handled by the FDRC has generally been about 80%. The FDRC has been important for claimants who do not have the resources to go to court and has contributed to supporting Hong Kong's status as an international financial centre.

Initiatives to enhance regulatory regime

26. This brings me now to say a few words on the important role of the regulators in Hong Kong in the areas of investor protection and corporate governance in the financial sector.

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[10] *Li Kwok Heem John v Standard Chartered International (USA) Ltd* [2016] 1 HKC 535; *Zhang Hong Li v DBS Bank (Hong Kong) Ltd* (unreported, HCCL 2/2011, 13 April 2017).

27. In the aftermath of the Lehman Brothers collapse and the financial crisis, both the SFC and HKMA have strengthened their regulation of intermediaries in their sale of financial products.

28. For example, the SFC Handbook for Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Product was issued in 2010 (with revised editions in 2013 and 2015) to enhance product disclosure and to increase transparency with respect to public offers of investment products. The Code of Conduct for Persons Licensed by or Registered with the SFC was also amended to enhance intermediary conduct and selling practices. For structured products, the HKMA has recently published a circular setting out the enhanced disclosure requirements and reminded all banks to follow similar standards as those applicable to investment products regulated by the Securities and Futures Ordinance ('SFO').

29. Legislative amendments have also been implemented to improve the regulatory scheme to deal with issues which came to light during the financial crisis. These include amendments to provide for uniform regulation of public offerings of structured products under the SFO[11]; introduction of a new regime in the SFO for regulating the over-the-counter derivative market[12]; and introduction of a new cross-sector resolution regime for 'within scope financial institutions' in Hong Kong to mitigate the risks which a failing financial institution may pose to the stability and effective working of the Hong Kong financial system[13].

30. In relation to corporate governance of intermediaries, the SFC last year introduced a new Manager-in-Charge of Core Functions regime for licensed corporations to foster a stronger sense of senior management responsibility and drive proper

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[11] Securities and Futures and Companies Legislation (Structured Products Amendment) Ordinance 2011.

[12] Securities and Futures (Amendment) Ordinance 2014.

[13] Financial Institutions (Resolution) Ordinance.

conduct and behaviour. Under the regime, each licensed corporation must appoint at least one individual to be a Manager-in-Charge for each of 8 designated core functions[14].

31. The SFC has also continued to be active in its enforcement role through the courts and the Market Misconduct Tribunal ('MMT'), including proceedings to seek court orders to disqualify directors and MMT proceedings on failures to disclose inside information, and insider dealing and other market misconduct.

32. The SFC also has power to apply to the court to wind up a listed company in the interest of the investing public (section 212 of the SFO). This power was successfully relied upon in 2015 to wind up a listed company[15] in circumstances where there had been fraud on a massive scale.

33. Furthermore, in a recent case involving another listed company, the SFC obtained orders for compensation for investors under section 213 of the SFO in respect of their losses resulting from false and misleading statements made in the company's financial results[16].

34. The HKMA has also been active in promoting good corporate governance in banks. For example, the HKMA finalised in October 2017 the revision of a Supervisory Policy Manual modules related to corporate governance, namely on

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[14] The 8 core functions are as follows (http://www.sfc.hk/edistributionWeb/gateway/EN/circular/intermediaries/licensing/doc?refNo=16EC68)
- (i) Overall Management Oversight;
- (ii) Key Business Line;
- (iii) Operational Control and Review;
- (iv) Risk Management;
- (v) Finance and Accounting;
- (vi) Information Technology;
- (vii) Compliance; and
- (viii) Anti-Money Laundering and Counter-Terrorist Financing

[15] *Re China Metal Recycling (Holdings) Ltd (No. 3)* [2015] 2 HKLRD 415.

[16] *Securities and Futures Commission v Qunxing Paper Holdings Co Ltd* [2018] HKCFI 271.

"Corporate Governance of Locally Incorporated Authorized Institutions".

35. The Manual is to be read in conjunction with a guidance issued by the HKMA in December 2016 on empowerment of independent non-executive directors ('INEDs') in the banking industry. The guidance proposes measures to be taken by banks to ensure that there are sufficient suitably qualified people who are able to understand the risks that their institutions were exposed to willing to serve as INEDs.

36. In view of the increasing emphasis on investor protection, the SFC has taken initiatives to enhance relevant regulatory regime, and introduced a reform to the Professional Investor Regime in March 2016 to ensure that specified categories of professional investors would also be covered by important Code protections[17]. A key objective is to extend these protections to all individual clients of intermediaries.

37. The SFC also amended the Code of Conduct for Persons Licensed by or Registered with the SFC, with effect from 9 June 2017, to require licensed or registered intermediaries to include a term in their client agreements that any financial product recommended by them to the client must be 'reasonably suitable' for the client, having regard to the client's financial situation, investment experience and investment objectives. This mandatory suitability clause must also state that no other provision of the client agreement may derogate from that clause. This new requirement is intended to avoid the type of situation that arose in the *Chang Pui Yin* case by contractually binding the intermediary to complying with the suitability requirement and by limiting the ability of intermediaries from avoiding liabilities to investors on the basis of non-reliance or non-advisory clauses. While the Court of Appeal decision in Chang Pui Yin will remain important for protection of investors in cases arising before

[17] Circular to Licensed Corporations and Registered Institutions - Timetable for implementation of the new Professional Investor Regime, 21March 2016 (http://www.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=16EC15)

9 June 2017, the new requirement in the Code of Conduct should further alleviate the problems of mis-selling of financial products, thereby enhancing consumer and investor protection.

38. I hope, this morning, I have briefly highlighted both the robustness of the common law in Hong Kong in the context of the financial services industry and the important roles of the Hong Kong regulators in investor protection and corporate governance. The insights to be gained in the various sessions of this Conference over the next two days would no doubt provide much food for thought for Hong Kong financial industry as well as regulators.

39. Last but not the least, may I wish the Conference every success, and for those coming from overseas, an enjoyable stay in Hong Kong.

Thank you.