

To Catch a Tiger: Cross Border Regulation At Its Best

by Niall Coburn

The case of Tiger Asia Management LLC (Tiger Asia) shows that the Securities & Futures Commission of Hong Kong (HK SFC) has thrown down the gauntlet to foreign participants operating outside their jurisdiction, but who violate securities laws on their turf. Recently, the HK SFC was given the all clear by *The Hong Kong Court of Final Appeal* to proceed with its civil action for damages against Tiger Asia and its management for insider dealing on the Hong Kong Stock Exchange, even though the hedge fund is neither regulated, nor has any presence in the region.

Recent HK SFC action against Tiger Asia illustrates, that it not only acts as an enforcer, but is prepared to be a civil protector of collective interests for persons dealing on Hong Kong securities' markets, who have been injured by regulatory misconduct by firms operating outside their jurisdiction. The message from the HK SFC is clear: if you violate our laws we will not hesitate to take civil action even if we don't regulate you! This matter is interesting because both the US SEC and the HK SFC have taken parallel enforcement action on both sides of the Pacific against Tiger Asia, with different, but successful outcomes. As a result, foreign corporations operating outside the jurisdiction and not registered in Hong Kong cannot ignore the SFC regulatory action or the recent decision of the Hong Kong Court of Final Appeal. This is because of the multi - million damages and penalty awards that may-be made against foreign firms in any regulatory action.

Tiger Asia

Tiger Asia was founded in 2001 and is based in New York - an asset management company that specialised in equity investments in China, Japan and Korea. All of its employees are located in New York. Tiger Asia has no physical presence in Hong Kong.¹

The case turned on the interpretation of the rarely used Section 213 of the *Securities and Futures Ordinance Act* (s213) that allows the regulator to act in the public interest. This civil provision will provide a useful weapon in the SFC's regulatory armoury in the future and, in doing so, will provide a basis where they can take action against cross-border transactions that violate laws and affect the investing public in Hong Kong. It also raises the bar for risk management and compliance officers working in the investment industry space.

United States Action

On 12 December, 2012, the US Securities and Exchange Commission (SEC) and the US Attorney's Office for the District of New Jersey, commenced criminal and civil proceedings against Tiger Asia. The proceedings alleged that during 2008 and 2009 Mr Hwang, the owner of the fund and Mr Park, committed insider trading by short-selling in relation to dealing in

¹ Hong Kong SFC Media release, 15 July 2013

securities of the Bank of China (BOC) and the China Construction Bank Corporation (CCB) in confidential information received in private placement offerings. The charges also allege that they separately attempted to manipulate the prices of the publically traded Chinese banks' shares, in which Tiger Asia had substantial short positions and placed losing trades in an attempt to lower the price of the shares and increase the value of their short positions. This enabled Mr Hwang and Mr Park to illicitly pocket higher management fees of \$496,000 and make an overall profit for the hedge fund of \$16.2 million.² The circumstances were such that even Gordon Gecko, the fictitious banker in the film "Wall Street" would have flinched twice before embarking on the deals.

Tiger Asia, Hwang and Park have paid a high price for their collective contraventions agreeing to settle and pay a total of \$44 million to criminal and civil authorities in America that includes disgorgement penalties and prejudgement interest.³ The SFC, as a result of the Court of Final Appeal's recent decision, is pursuing them on this side of the Pacific.

Hong Kong SFC Action

In 2009 the SFC commenced proceedings under Section 213 of the *Securities and Futures Ordinance Act* (S213) that allows the regulator to act in the public interest. The SFC sought remedial orders, damages and injunctions in relation to the securities violations concerning insider dealing and market manipulation. Interestingly enough, the SFC took proceedings, irrespective of the United States enforcement action and despite Tiger Asia not having staff or any presence in the Hong Kong jurisdiction.

In the Court of First Instance, Tiger Asia and its officers successfully argued that the SFC had no jurisdiction under s213 to bring the action under that provision, since there had been no pre-existing criminal conviction or determination by the Market Misconduct Tribunal (MMT). The Court of First Instance ruled in favour of Tiger Asia and stopped the SFC from proceeding with the action against them.

The SFC persisted and successfully won in the Court of Final Appeal, which recent decision vindicated the position of the SFC actions and importantly clarified the law and the use of s213 in regulatory action.⁴

In overturning the Court of First Instance's decision, the Court of Final Appeal confirmed that s213 was a free-standing remedy available to the SFC and was not dependent on any criminal conviction or determination by the MMT. The Court found that the SFC was able to

² U.S. Securities and Exchange Commission, Litigation Release No 22569 / December 13, 2002. Securities and Exchange Commission v Tiger Asia Management, LLC, et al, Civil Action No 12-cv-7601 (DMC).

³ U.S. Securities and Exchange Commission, Litigation Release No 22569 / December 13, 2002. Securities and Exchange Commission v Tiger Asia Management, LLC, et al, Civil Action No 12-cv-7601 (DMC).

⁴ Securities and Futures Commission v Tiger Asia Management LLC and Others - Court of Final Appeal No 178 of 2011 Judgment 10 May 2013.

proceed against Tiger Asia under that provision and commented that s213 “*provides a valuable tool to the Commission to protect the investing public which is an important objective of the SFO ... and ... much needed ammunition to the Commission to protect investors.*”⁵ In essence, the Court of Final Appeal concluded that the SFC could use s213 against Tiger Asia as it is a free-standing remedy and not dependent upon any previous finding or determination by a tribunal or court.

In doing so, the Court found that s213 is a public interest provision available to the SFC in circumstances where a person has contravened a provision of the SFO. As a result, the SFC can bring proceedings against a foreign corporation operating within the region and obtain civil remedies to restore any party within the jurisdiction to the position they were prior to the contravention.

By using this civil provision, the SFC has succeeded in achieving a major regulatory victory and has widened its regulatory net. The regulator is now proceeding against Tiger Asia and its management for damages and other relief. Because of the circumstances, it was doubtful the SFC could have ever proceed criminally against Tiger Asia or its officers, given the significant risk that criminal charges in Hong Kong would be barred on the grounds of double jeopardy. This is because as mentioned, the United States authorities had already proceeded criminally against the parties within their own jurisdiction.

Analysis

Although cross-border regulations are complex, the Tiger Asia case is an example of securities regulators in the United States and Hong Kong running parallel actions to protect their markets. These regulators have shown they are not shy or easily dissuaded from side-stepping a legal fight that may protect market participants’ interests. In particular, the Tiger Asia case shows that the SFC displayed appropriate judgment in pursuing the hedge fund and its officers under s213, rather than hanging their hat on other cumbersome provisions which may not have had the same swift result for investors or pecuniary benefits. It appears, the SFC preferred not to be caught up in a criminal prosecution that was unpredictable, given the officers of Tiger Asia were not physically operating within the jurisdiction at the time of the offences.

By using the s213 route, the SFC also ruled out any double jeopardy defence by Tiger Asia, as the provision is a stand-alone civil remedy available for use in the public interest and not dependent on any criminal determination. It also means that a foreign company not licensed or regulated in Hong Kong, can be caught within the s213 net, if it violates securities laws and irrespective of the company not being registered or located outside the jurisdiction. The case illustrates that perceived regulatory enforcement gaps have been reduced.

⁵ Ibid, see pages 15 to 16 of the decision which is available on the Judiciary’s web site (www.judiciary.gov.hk)

In many respects, the enforcement strategy of the SFC in this case has been a “feather in their cap,” as their action was vindicated by The Court of Final Appeal. Certainly, this does not happen every day in the regulatory world! Going forward, this win will provide the SFC with more confidence and, of course, the regulatory armoury of s213 to take action in similar circumstances. It is clear that the SFC now has a greater reach in the region and, arguably, may adapt its regulatory stance to different cross-border transactions. Compliance officers and risk managers may wish to take heed of this judicial outcome. The Court of Final Appeal, in clarifying the use of s213 has made it clear that the provision can be used in the public interest to provide remedies for parties involved in impugned transactions. The consequence and interesting development is that this will allow regulators to take future parallel action on both sides of the Pacific.

From a practical enforcement perspective, The Court of Final Appeal also commented that, in using this provision, the SFC is subject to no review and can use evidence obtained from defendants under statutory compulsion. Additionally, the SFC does not have to satisfy the standards of criminal proof in presenting evidence. More importantly, the use of s213 by the SFC does not exclude the possibility of a criminal prosecution against any defendants further down the line.⁶

Warning shots - conclusions for foreign participants in Hong Kong

The clarification of the provision is of particular importance to the SFC in the context of combatting market misconduct perpetrated by foreign funds or other companies outside their jurisdiction who may breach regulations on their exchange. Section 213 allows for a faster outcome where foreign participants are involved and avoids painstaking criminal proceedings or cumbersome civil procedures.

The actions of the Hong Kong SFC raise a new bar for officers of foreign international companies who seek to undertake cross-border jurisdictional transactions in Hong Kong. Any perceived regulatory enforcement weakness has now been reduced as a result of the swift actions of the SFC and the clarification by the superior court.

The SFC, by proceeding against Tiger Asia, illustrates that it is prepared to regulate its own turf amidst the complexity and legal mine fields of cross-border transactions on their home exchange. As a result, compliance and risk management teams in financial institutions will have to take care and ensure that corporate governance standards are sufficient to deal with these cross border transactions.

The stakes for foreign firms located outside the jurisdiction who operate in the region are too high to ignore, simply because the penalties and civil damages may run into many millions of dollars for anyone involved in contraventions. More importantly, the SFC’s Executive

⁶ Securities and Futures Commission v Tiger Asia Management LLC and Others - Court of Final Appeal No 178 of 2011 Judgment 10 May 2013 p 6

Director of Enforcement, Mr Mark Steward, has recently announced that going forward the SFC intends to prosecute these types of cases “fairly and vigorously.”⁷ Tiger Asia clearly shows that the reach of the SFC is no longer restricted to one side of the Pacific.⁸

⁷ SFC Media Announcement, 23 February 2012.

⁸ Other sources considered: Financial Times Asia, “HK Opens civil case against Tiger Asia,” by Paul J Davis, 15 July, 2013; Dorsey & Whitney LLP (HK), “How to trap a tiger-regulators’ nets tighten around Tiger Asia on both sides of the Pacific.” 21 August, 2013; Bloomberg, “Tiger Asia Accused of Insider Trading in Hong Kong Case,” Eleni Himaras, 11 July, 2013; The Hong Kong Court of Final Appeal, press summary to judgment dated 10 May, 2013.