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# SFC reprimands and fines Credit Suisse (Hong Kong) Limited and Credit Suisse AG \$2.8 million for regulatory breaches

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The Securities and Futures Commission (SFC) has reprimanded and fined Credit Suisse (Hong Kong) Limited (CSHK) and Credit Suisse AG (CSAG) (collectively, Credit Suisse) \$2.8 million over their failures to comply with the disclosure requirements when they published certain research reports on Hong Kong-listed securities (Notes 1 to 4).

The SFC found that CSHK and CSAG failed to disclose their investment banking relationships with subject companies in certain research reports on Hong Kong-listed securities published between 2006 and 11 August 2016. This was caused by an information technology (IT) logic issue in one of Credit Suisse's IT system feeds and it was rectified on 11 August 2016.

In addition, an update by Credit Suisse in August 2016 to revise the market maker disclosure in its research reports led to an inadvertent exclusion of that disclosure from a disclosure template for its research reports. As a result, certain research reports on Hong Kong-listed securities distributed by CSHK or CSAG between August 2016 and 31 May 2017 did not disclose that CSHK was a market maker. This issue was fully rectified on 31 May 2017.

The SFC takes the view that CSHK and CSAG have failed to put in place effective systems and controls to ensure compliance with the disclosure requirements and timely detection of the disclosure failures.

In deciding the penalty, the SFC took into account that:

- CSHK self-reported the two incidents to the SFC;
- CSHK and CSAG have cooperated with the SFC in resolving the SFC's concerns; and
- Credit Suisse has taken remedial measures to rectify the failures and strengthen its internal controls and systems.

End

Notes:

1. CSHK is licensed under the SFO to carry on business in Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 5 (advising on futures contracts), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities.
2. CSAG is registered to carry on business in Type 1 (dealing in securities), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities.
3. In respect of CSAG, the failures in question concerned the business activities of the Hong Kong branch of CSAG.
4. Paragraph 16.5(b) of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of Conduct) requires that a firm that makes, or will make, a market in the securities in respect of the issuer or the new listing applicant should disclose that fact in the research report. Paragraph 16.5(d) of the Code of Conduct provides that a firm that has an investment banking relationship with the issuer or the new listing applicant should disclose that fact in the research report.

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

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## STATEMENT OF DISCIPLINARY ACTION

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### The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded Credit Suisse (Hong Kong) Limited (**CSHK**)<sup>1</sup> and Credit Suisse AG (**CSAG**)<sup>2</sup>, and fined them a total of \$2.8 million pursuant to sections 194 and 196 of the Securities and Futures Ordinance (**SFO**).
2. The disciplinary action is taken in relation to two incidents of failures by CSHK and CSAG (together, **Credit Suisse**) to comply with the disclosure requirements under paragraph 16.5 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (**Code of Conduct**) in respect of certain research reports issued by them.

### Summary of facts

#### *Incident 1*

3. On 6 October 2016, CSHK self-reported to the SFC that, due to an information technology logic issue, the conflict of interest disclosures were omitted in certain research reports covering Hong Kong-listed securities published by it. CSAG, which has published research reports prepared by CSHK for its Private Banking clients, was also affected by the incident.
4. According to CSHK:
  - (a) the incident was caused by an information technology (**IT**) logic issue in one of Credit Suisse's IT system feeds (**IT Logic Issue**), which affected the inclusion of conflict of interest disclosures (**Conflict Disclosures**) in certain research reports on "dual-covered companies", i.e. companies with multiple products or securities covered by Credit Suisse's research department.
  - (b) Conflict Disclosures were included in research reports to indicate whether: (i) the subject of the report is a Credit Suisse client; (ii) Credit Suisse has received investment banking revenue from the subject company in the last 12 months; and (iii) Credit Suisse expects to receive or intends to seek compensation for investment banking services from the subject company in the next 3 months.
  - (c) **The omission of Conflict Disclosures in certain research reports on dual-covered companies had occurred since 2006, when the relevant IT system was implemented. The IT Logic Issue was rectified on 11 August 2016.**

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<sup>1</sup> CSHK is licensed under the SFO to carry on business in Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 5 (advising on futures contracts), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities.

<sup>2</sup> CSAG is registered to carry on business in Type 1 (dealing in securities), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities.

- (d) Between 2006 and 11 August 2016, a total of 3,607 research reports related to Hong Kong-listed securities issued by CSHK or CSAG were potentially impacted by the IT Logic Issue.

#### *Incident 2*

5. In or around April 2017, CSHK self-reported to the SFC that certain research reports published by it might not have contained the market maker disclosure in accordance with paragraph 16.5(b) of the Code of Conduct.
6. An internal review conducted by CSHK in or around March 2017 revealed that since 4 August 2016, the market maker disclosure<sup>3</sup> was absent from research reports that were published on Hong Kong-listed companies for which CSHK made a market for the options on the relevant stocks.
7. The failure appeared to be the result of an attempt made by Credit Suisse to revise the market maker disclosure for Credit Suisse research reports. On 4 August 2016, the system associated with Credit Suisse research report disclosures was updated. The update inadvertently excluded the market maker disclosure from a template of disclosures in Credit Suisse research reports that were published on securities (including Hong Kong-listed securities) where Credit Suisse made a market in the security or a related derivative.
8. On 10 April 2017, CSHK implemented a tactical fix (**Fix**) to rectify the issue in respect of Hong Kong-listed companies for which CSHK made a market for the related options. On 31 May 2017, CSHK expanded the Fix to include Hong Kong-listed companies for which CSHK made a market for the warrants and/or callable bull/bear contracts on the underlying securities.
9. CSHK identified that a total of 913 research reports issued by CSHK or CSAG between 4 August 2016 and 31 May 2017 were impacted by the incident.

#### *SFC's findings*

10. Based on the information set out above, the SFC found that CSHK and CSAG failed to:
  - (a) disclose the firms' market making activities and/or investment banking relationship with the issuer in certain research reports issued by them; and
  - (b) put in place effective systems and controls to ensure compliance with the disclosure requirements under paragraph 16.5 of the Code of Conduct and timely detection of the disclosure failures.
11. CSHK's and CSAG's failures constitute a breach of:
  - (a) General Principle 3 (capabilities) and paragraph 4.3 (internal control, financial and operational resources) of the Code of Conduct, which require a licensed or registered person to employ effectively the resources and procedures which are needed for the proper

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<sup>3</sup> The market making disclosure would be in the form similar to "As of the date of this report, Credit Suisse makes a market in the following subject companies ([stock codes])."

performance of its business activities and have internal control procedures which can be reasonably expected to protect its operations and its clients from financial loss arising from professional misconduct or omissions;

- (b) paragraph 16.5(b) (firm financial interests and business relationships) of the Code of Conduct, which provides that a firm<sup>4</sup> that makes, or will make, a market in the securities<sup>5</sup> in respect of the issuer or the new listing applicant should disclose that fact in the research report;
- (c) paragraph 16.5(d) (firm financial interests and business relationships) of the Code of Conduct, which provides that a firm that has an investment banking relationship<sup>6</sup> with the issuer or the new listing applicant should disclose that fact in the research report; and
- (d) General Principle 7 (compliance) and paragraph 12.1 (compliance: in general) of the Code of Conduct, which require a licensed or registered person to comply with, and implement and maintain measures appropriate to ensure compliance with, relevant regulatory requirements.

## **Conclusion**

- 12. In deciding the disciplinary sanctions set out at paragraph 1, the SFC has taken into account:
  - (a) CSHK self-reported the two incidents to the SFC;
  - (b) CSHK and CSAG have cooperated with the SFC in resolving the SFC's concerns; and
  - (c) Credit Suisse has taken remedial measures to rectify the failures and strengthen its internal controls and systems.

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<sup>4</sup> "Firm" for the purposes of paragraph 16 of the Code of Conduct means any intermediary and its group of companies that carry on a business in Hong Kong in investment banking, proprietary trading or market making, or agency broking in relation to securities.

<sup>5</sup> "Securities" refers to, among other things, shares issued by an issuer and any warrants or options on these shares which are listed or traded on The Stock Exchange of Hong Kong Limited.

<sup>6</sup> Any compensation or mandate for investment banking services received within the preceding 12 months would constitute an investment banking relationship.