

SFAT allows review for ex-Deutsche trader over trading of HSBC shares

21 May 2013

The Securities and Futures Appeals Tribunal (SFAT) allowed the application for review by Mr Christian Denk, a former trader of Deutsche Securities Asia Limited (DSAL), against the decision of the Securities and Futures Commission (SFC) to publicly reprimand him concerning the trading of HSBC Holdings plc (HSBC) shares during the Closing Auction Session (CAS) (Note 1).

The SFC's decision followed its investigation into the trading of HSBC shares in the last seconds of the CAS on 9 March 2009. During the CAS that day, the indicative equilibrium price (IEP) of HSBC shares fell 10.8% from around \$37 to \$33 (Notes 2 & 3).

The SFC's investigation stemmed from suspicions that the sudden fall in the share price of HSBC was the result of manipulation.

The investigation did not find any manipulation. However, the SFC considered the size of Denk's orders in the last seconds of the CAS on 9 March 2009 was likely to create undue volatility in the closing price of HSBC. The SFC believed Denk's conduct was in breach of his obligations under the Code of Conduct to act with due skill, care and diligence, in the best interests of market integrity (Note 4). The SFAT disagreed and delivered its reasons on 20 May 2013 (Note 5).

The SFC alleged that the fall in HSBC share price was the result of the interaction of a number of at-auction sell orders for a total of 5.4 million HSBC shares placed by Denk in the last seconds of the CAS and an at-auction limit sell order for 6,000 HSBC shares at \$33 placed earlier by a retail investor (Note 6). Under the CAS algorithm, \$33 became the closing price of HSBC shares on 9 March 2009.

Denk contended that he was trading on behalf of Deutsche Bank London and placed the at-auction sell orders for hedging purposes (Note 7). There was no connection between DSAL, including Denk, and the retail investor who placed the \$33 at-auction limit sell order to offset some of his earlier purchases (Note 8).

The SFC considered that Denk should have managed his hedging requirements well before the market close. As an experienced trader, Denk ought to have known that the size of his orders would likely move the share price in view of the market liquidity in the circumstances.

In its reasons, the SFAT commented on the inherent instability of the closing auction system which meant, amongst other things, that Denk was unable to view the order depth when placing his sell orders. The SFAT also commented on the relevant standard of proof in disciplinary cases.

End

Notes:

1. Denk was licensed under the Securities and Futures Ordinance to carry on business in Type 1 (dealing in securities) and Type 2 (dealing in futures) regulated activities and was accredited to DSAL from February 2007 to February 2010. He is currently not accredited to any licensed corporation.
2. Please see SFC press release dated [11 March 2009](#).
3. The CAS was an additional trading session of 10 minutes introduced by Hong Kong Exchanges and Clearing Limited (HKEx) on 26 May 2008 for facilitating trading at market close. The CAS was designed to provide an elaborate process to arrive at an IEP which would accommodate the matching of the largest number of shares at the relevant time based on the orders inputted. The CAS was later suspended by HKEx. From 23 March 2009, the securities market closes at 4:00 pm and HKEx uses its pre-CAS method for calculating closing prices for securities. Please see HKEx press release dated 20 March 2009.
4. Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission
5. The Reasons For Determination is available on the SFAT's website (www.sfat.gov.hk/english/determination/index.htm).
6. Two types of orders were allowed to be inputted during the CAS: at-auction orders and at-auction limit orders. An at-auction order did not carry an order price and were ranked by their order entry time. At-auction limit orders were first ranked in accordance with their limit price and then by the order entry time.

7. Denk placed his sell orders at 16:09:57, when the IEP was at \$37.0. At 16:09:58, Denk finished inputting his last order, when the IEP was driven down to \$33. According to Denk, his sell orders were for hedging the option book he managed for Deutsche Bank London. Out of the sell orders of 5.4 million HSBC shares, he could only execute 3,812,000 shares at \$33, because there was insufficient liquidity in the market to absorb all his orders. In order to fulfil his hedging requirements, he subsequently sold 1.902 million shares in the London market at \$35.39 and another 300,000 shares to another trading desk at Deutsche Bank off the exchange on 9 March 2009.
8. The retail investor placed an at-auction limit sell order for 6,000 HSBC shares at \$33 at 16:06:59. According to the retail investor, he bought HSBC shares in the morning trading session on 9 March 2009 with a view to increasing his holding in HSBC in order to take up additional shares in the HSBC 5 for 12 rights issue announced on 2 March 2009. During the day, he bought more HSBC shares to average down his cost for the purchases as the price of HSBC shares kept falling. However, he had insufficient funds to settle all his trades and began to sell his HSBC shares from 14:42 without success. He eventually reduced his selling price to \$33 because he needed funds to settle the shares he had bought earlier in the day.