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FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF MARKET REGULATION, Complainant, v. RESPONDENT, Respondent.	Disciplinary Proceeding No. 20080150419 Hearing Officer – LBB **EXTENDED HEARING PANEL DECISION** Dated: October 7, 2013

The Department of Market Regulation failed to prove that Respondent violated NASD Rule 2110 by disclosing confidential information and misrepresenting the source of information. The Complaint is dismissed.

Appearances

Shannon D. Rozner, Esq., Edwin T. Aradi, Esq., and James J. Nixon, Esq., for the Department of Market Regulation.

Dana S. Gloor, Esq., and David S. Richan, Esq., for Respondent.

DECISION

I. Introduction

Respondent was a resident of Hong Kong, where she was employed as a salesperson by China International Capital Corporation (Hong Kong) Limited ("CICC HK"), a Hong Kong securities broker that was not a FINRA member firm. [Respondent] worked in the CICC HK Sales & Trading Department. One function of salespeople in the Sales & Trading Department was to provide information to customers on the securities offered by CICC HK, including IPOs. For IPOs underwritten by the firm, the Sales & Trading Department was an important source of information for the firm and the issuers of the IPOs, providing feedback from potential investors about such matters as the proposed price range for the offering.

While employed by CICC HK and working in Hong Kong, [Respondent] registered with FINRA as a general securities representative through CICC US Securities, Inc. ("CICC US"), which CICC HK had formed to conduct a securities business in the United States. Although she was registered through CICC US for a portion of the period relevant to this proceeding, she never worked for CICC US, and CICC US did not conduct any securities business until after the events at issue in this proceeding.

In September 2008, FINRA received an anonymous tip, alleging that [Respondent] had sent e-mails to potential investors that contained nonpublic information about two IPOs that CICC HK had underwritten. Upon receipt of the tip, FINRA opened an investigation. Following the investigation, the Department of Market Regulation filed a one-cause complaint, charging [Respondent] with violating NASD Rule 2110,[1] which requires FINRA members to observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business.[2] The Complaint alleges that [Respondent] acted unethically by disclosing nonpublic information about Chinese IPOs, disclosing nonpublic information about Chinese companies to potential investors, and distributing a CICC HK IPO report during a blackout period to an unapproved person. In addition, the Complaint alleges that on one instance [Respondent] misrepresented the source of the information she provided to clients.

[1] NASD Rule 2110 stated that "[a] member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade." NASD Rule 2110 applies with equal force to FINRA members and their associated persons. *John Joseph Plunkett*, Exchange Act Rel. No. 69766, 2013 SEC LEXIS 1699, at *3 n.3 (June 14, 2013). The Rule was the predecessor of FINRA Rule 2010, which has the identical language.

[2] The FINRA Rules, which include NASD Procedural and Conduct Rules, are available at www.finra.org/Rules. Following the consolidation of NASD and the member regulation, enforcement, and arbitration functions of NYSE Regulation into FINRA, FINRA began developing a new "Consolidated Rulebook" of FINRA Rules. The first phase of the new consolidated rules became effective on December 15, 2008. *See* FINRA Regulatory Notice 08-57 (Oct. 2008). Because the Complaint in this case was filed after December 15, 2008, the FINRA procedural rules apply. The conduct rules that apply are those that existed at the time of the conduct at issue.

[Respondent] denies that she acted unethically. In general, she asserts that her conduct met applicable standards in Hong Kong, was undertaken in good faith and consistent with CICC HK's instructions, and that most of the information she disclosed did not constitute confidential, nonpublic information. [Respondent] also asserted that FINRA lacked jurisdiction to charge her with any alleged misconduct that occurred before she was registered with CICC US.

The Extended Hearing Panel conducted a hearing in New York from April 30, 2013, to May 7, 2013.[3] Based on the evidence, the Extended Hearing Panel dismisses the Complaint for three reasons.

First, the information that [Respondent] disclosed before she was registered with CICC US was neither confidential nor inaccurate. Much of the information she distributed had been provided to CICC HK's sales force to be disseminated to potential investors.

Second, NASD Rule 2110 does not govern her conduct before she registered with CICC US because she was not associated with CICC US at the time. [Respondent] was never employed by CICC US, and there is no evidence that she ever did any work on behalf of CICC US.

Third, with respect to [Respondent]'s conduct after she was registered with FINRA, the Extended Hearing Panel concluded that she made two inappropriate disclosures, but in doing so she did not violate Rule 2110. In the first instance, she disclosed information about sales by CICC HK's customers that she believed was public. In the second instance, she delivered a research report to a CICC HK client who had been inadvertently omitted from the firm's list of

[3] The Extended Hearing Panel is composed of a current member of the District 10 Committee, a former member of the District 8 Committee, and a Hearing Officer. At the hearing, Market Regulation presented testimony from a FINRA examiner, the current compliance officer from CICC US, and Respondent. Respondent testified on her own behalf, and presented witnesses from current and former CICC HK employees, including her supervisor, who was also president of CICC US; a CICC HK customer (who was also her husband); and Kristi Swartz, an expert witness on Hong Kong law and custom for securities brokers.

approved recipients. The Extended Hearing Panel concluded that [Respondent]'s inappropriate disclosures were not sufficiently related to the conduct of securities business in the United States to come within the ambit of Rule 2110. She made the disclosures solely in her capacity as an employee of CICC HK; she was not working for CICC US, and CICC US was not yet operating. Further, the nature of her conduct did rise to the level of an ethical violation. In the first instance she erred in concluding that the subject information was in the public domain, and in the second instance she delivered the research report to a firm that had been inadvertently left off the distribution list. All of the other information she disclosed after she registered with CICC US did not constitute confidential information under Hong Kong practice.

For the foregoing reasons, the Extended Hearing Panel dismisses the Complaint in its entirety.

II. Respondent's Employment in the Securities Industry and FINRA Registration

[Respondent] began her employment in the securities industry in the United States, but moved to Hong Kong to work for CICC HK in 2006. Although she became registered with FINRA through CICC US, she was never employed by the U.S. firm and performed no work for it.

A. Respondent Moves from United States Securities Firms to CICC HK in Hong Kong

Respondent was first employed in the securities industry in the United States in 1999, working at member firms in New York. She was registered with FINRA though U.S. member firms from 2000 through June 2006. She became employed by CICC HK in June 2006, when she signed an employment contract with the firm. CX-10, CX-61, CX-70. CICC HK is a Hong Kong securities broker that services large institutional clients from around the world. Tr. 1093,

1181. While Respondent was employed by the CICC HK, a large percentage of the firm's business was derived from underwriting IPOs for Chinese issuers. Tr. 899, 1122-1123.

[Respondent] continued her employment with CICC HK until June 2010, when she left to join the Hong Kong office of a Singaporean bank. She was a salesperson in the Hong Kong office of the Sales & Trading Department of CICC HK during her entire tenure with the firm. Tr. 103, 1009-1011, 900. The functions of the Sales & Trading Department of CCC HK were:

- Identifying institutions and corporations as potential clients;
- Offering market analysis and investment ideas to institutional and corporate clients;
- Conducting agency trading for institutional and corporate clients;
- Ensuring proper documentation and account details for client trading; and
- Distribution of company specific and industry specific research notes and reports to clients.

CX-4 at 4.

B. CICC US Becomes a FINRA Member Firm in August 2007

CICC US was formed 2005, primarily to market Chinese IPOs in the United States. Tr. 741, 1122-1123. CICC US applied for FINRA membership on January 30, 2007, when it filed a Form BD. The firm's membership application was approved on August 21, 2007. CX-62.

The firm was not engaged in the securities business before becoming a FINRA member firm in 2007, or in 2008, when alleged violations occurred while Respondent was registered. Tr. 696, 886, 1122-1123. It did not have any clients or conduct any securities transactions until November 2009. CX-56; Tr. 695, 731, 1122-1123. Prior to the approval of its FINRA membership, CICC US had only two employees, the firm's principals. Tr. 885-886, 888. The firm had no revenue other than bank interest in 2008. CX-72; Tr. 695, 732, 1122. Its only expenses were legal, professional, and incidental expenses. CX-72.

C. Respondent Registers with CICC US

Respondent became registered with FINRA, through CICC US, on August 30, 2007, when the firm filed a Form U4 on her behalf. CX-61, CX-70. Respondent was registered with CICC US from August 2007 until June 30, 2010, while employed in Hong Kong by CICC HK. She has not been registered with a FINRA member firm since June 30, 2010. CX-61; Tr. 86, 106, 1009-1011.[4]

The Forms U4 for CICC US were created by the CICC HK compliance department. Tr. 896, 931. Both Respondent and Dr. Wang, who was her supervisor at CICC HK and a co-president of CICC US, signed Respondent's Form U4. CX-70 at 13; Tr. 51, 885. The Form U4 filed for Respondent had glaring errors. Although Respondent had moved to Hong Kong when she started working for CICC HK in June 2006, her Form U4 listed her residential address as New York. The Form U4 also incorrectly identified her current employer as Cazenove, Inc., where she had worked before she became employed at CICC HK. Tr. 61-64; CX-61. Most importantly, the Form U4 incorrectly stated that Respondent had been an employee of CICC US since June 2006, the date on which she started working for CICC HK. CX-61. She was not employed by CICC US, and did not do anything on behalf of the firm, prior to her FINRA registration. Tr. 892-893, 926.

Respondent did not become an employee of CICC US even after she registered with the firm. Tr. 888, 1126.[5] She never did anything for the benefit of, or on behalf of, CICC US. She did not sign an employment agreement with CICC US. Tr. 97-98, 729, 895-896. Her job

[4] FINRA has jurisdiction to initiate this proceeding pursuant to FINRA By-Laws, Article V, Sec. 4. Market Regulation filed the Complaint on June 22, 2012, within two years after the termination of Respondent's registration with CICC US, a FINRA member firm, and the Complaint charges her with violations in 2008, when she was registered with CICC US.

[5] The president of CICC US testified that she had never been an employee at the time he left the firm in April 2008. Tr. 888. CICC US's first functioning compliance officer testified that, as of the time he left the firm in December 2008, she had never been an employee of CICC US. Tr. 1126.

responsibilities at CICC HK did not change when she was registered with CICC US. Tr. 85. Furthermore, as noted above, the firm did not begin operations until November 2009, after the occurrence of the events that are the subject of the Complaint.

III. Securities Sales and Information Practices in Hong Kong and at CICC HK

One function of the Sales & Trading Department's sales force was to provide information to customers on the securities offered by CICC HK, including IPOs. Most of the information the sales force provided to customers came from CICC HK. For IPOs underwritten by the firm, the sales force was also an important source of information for the firm and issuers, providing feedback from potential investors about such matters as the proposed price range for the offering.

CICC HK's management and the firm's analysts provided information to the sales force in meetings each morning. The morning meetings at CICC HK included briefings on news, expected earnings of issuers, CICC HK's published research, and feedback on previously-published research. Tr. 89, 165-167. The morning meetings regularly included presentations by research analysts. Tr. 155. The morning meetings were a forum for an exchange of ideas among the participants. Tr. 155, 156, 283, 903, 1232. The compliance department, the head of research, or the head of Sales & Trading reviewed and approved the dissemination of all information to the Sales & Trading Department. Tr. 153-154, 161. The information discussed in morning meetings was intended to be transmitted to potential customers unless there was a specific direction from CICC HK management to keep the information confidential. In Hong Kong, salespeople regularly communicate information from analysts and management to potential investors, including information that has not been published. Tr. 91, 163, 251, 282, 837, 985, 1136, 1184.

In Hong Kong, issuers provide more information to the public and brokers about corporate developments, including sales and earnings, than provided by firms in the United

States. Tr. 828-830. Brokerage firms' analysts meet with issuers and get information, or hints, about corporate matters, including the issuers' anticipated earnings. Tr. 845, 972-974. However, issuers are prohibited from disclosing information for a period before the issuance of annual or quarterly reports. These blackout periods apply only to issuers, and do not apply to brokers. Tr. 1255-1256.[6]

The IPO process in Hong Kong is much more open than in the United States. During the entire IPO process, there is much more information available, and more communication among investment bankers, salespeople, analysts, and with clients. Tr. 829, 846, 858, 907. At CICC HK, information about an upcoming IPO was often provided to the sales force in a meeting specifically about the IPO. Tr. 903. Information about an IPO would be provided to the sales force by research reports, prospectuses, red herrings, research analysts, and the firm's Equity Capital Markets department. Tr. 901-902. In addition, for each IPO, the sales force at CICC HK received a selling memorandum from the firm that provided information that was supposed to be shared with potential investors. The selling memorandum would explain why the proposed IPO was a good investment, and would include the preliminary price range. Tr. 250-251, 1238.

The firm's discussions of the IPO with the sales force would include the merits of the offering, the timetable, and the price range. Tr. 904, 1235. The sales force was supposed to communicate the information discussed in the meeting to institutional investors. Tr. 899, 904-905, 954-957, 1191-1192. It is a common practice in Hong Kong for the underwriter's sales force to provide preliminary pricing information to potential investors. Tr. 835. In fact, one role

[6] Respondent's expert, Kristi Swartz, has been in practice in Hong Kong as a solicitor since 2000. She is currently managing partner of the Hong Kong office of Blank Rome Solicitors. Her legal practice focuses on securities law, licensing, and regulatory compliance. Tr. 1246-1249; RX-1. The Extended Hearing Panel found her testimony and expert report credible and persuasive.

of the underwriter's sales force in the IPO process in Hong Kong is to provide such information as the preliminary price range to potential investors, and to provide feedback to the firm and the issuer on the potential investors' reaction to the proposed price range. Tr. 832-836, 1273-1274.

IV. The Complaint Is Dismissed with Respect to Respondent's Conduct Prior to Her FINRA Registration

The complaint charges Respondent with improperly disclosing confidential information concerning Citic Bank Co., China Merchants Bank, and Genesis Energy Holdings, Ltd., and misrepresenting the source of information concerning Genesis, before Respondent was registered with FINRA, and before CICC US was a FINRA member firm. The Extended Hearing Panel dismisses the charges in the Complaint relating to communications prior to Respondent's FINRA registration for two reasons. First, Market Regulation did not establish that Respondent engaged in any improper conduct during this period. The information she disclosed was not confidential, and much of it was provided to the sales force by CICC HK for the purpose of dissemination to potential investors. The Extended Hearing Panel also dismisses the allegation that Respondent misrepresented the source of her information about Genesis because she did not misrepresent the source. Second, the Extended Hearing Panel dismisses the Complaint with respect to the alleged violations that occurred before Respondent was registered with CICC US because Respondent was not associated with CICC US, or any member firm, when she made the allegedly improper communications, and therefore could not have violated NASD Rule 2110.

A. The Complaint Is Dismissed with Respect to Respondent's Communications about the Citic Bank IPO Because Respondent Did Not Disclose Confidential Information

In 2007, CICC HK was an underwriter for an IPO for Citic Bank Co., a large Chinese Bank. Tr. 208-209. On April 8, 2007, Respondent sent an e-mail to CICC HK clients and contacts, disclosing the anticipated share price range and timing of the IPO. CX-15. On

April 12, Respondent sent a second e-mail to clients and contacts, informing them that the anticipated price range had been lowered, and that she (or CICC HK) expected more demand for the offering, and predicting that it would be oversubscribed.[7] She also expressed her personal opinion of the reason for the reduction in the anticipated price of the offering. CX-16; RX-12. The Complaint charges that both of these e-mails improperly disclosed confidential information.

Respondent did not improperly disclose the information in the e-mails. When she sent her e-mails, the initial and revised pricing information, and the information about the timing of the IPO, was already public, and had been provided to the CICC HK sales force for the purpose of providing the information to investors. CX-14; RX-10, RX-12, RX-14, RX-59 – 61, RX-79; Tr. 224-227, 984, 1191.[8]

The Extended Hearing Panel finds that Respondent did not disclose confidential information about the Citic Bank IPO. She was expected to provide information on IPO pricing and timing to potential investors, and to provide feedback to her firm on the investors' reaction to the information. In addition, the information was available to the public when she sent her e-mails to potential investors. The Extended Hearing Panel dismisses the Complaint with respect to the Citic Bank disclosures.

[7] The Complaint refers to an April 11 e-mail. Although the date on the copy of the e-mail in the record is April 11, the actual date was April 12, Hong Kong time. At the hearing, it was established that the time printed on some of the e-mails that are in evidence was New York time, rather than Hong Kong time, because they were printed in connection with FINRA's investigation or the litigation. Hong Kong time is 12 hours ahead of New York time. In addition, the time on one article in the record reflected Greenwich Mean Time, not Hong Kong time. The times and dates used in this decision will be Hong Kong time, because in several instances the precise times are important to understand whether Respondent was authorized by her firm to disclose information, or whether information was already in the public domain.

[8] On May 9, 2007, Respondent was reprimanded by her firm for sending the second e-mail. The text of the reprimand referred both to the revised price range and the expression of her views about the reason for the change in the price range, but did not specifically say what was improper in Respondent's e-mail. CX-20. The evidence showed that the firm's concern was that the opinion she had expressed about the reason for the price change was inappropriate in Chinese culture. The firm was not concerned about the disclosure of the price range for the IPO. Tr. 241, 245-246, 268-269, 908-909.

B. The Complaint Is Dismissed with Respect to Respondent's Communications about China Merchants Bank Because She Did Not Disclose Confidential Information

China Merchants Bank is a large Chinese bank. Tr. 270. In April 2007, CICC HK was providing analyst coverage of the bank's stock. Tr. 270-272. On April 10, 2007, Respondent sent e-mails to potential investors, predicting that China Merchants Bank's 2006 earnings, which had not yet been reported, would be about 10% higher than CICC HK's previous expectations. She also predicted that earnings for the first quarter of 2007 would be up 70% due to a widening net interest margin and fee income. In one, she stated that management had told CICC HK their actual numbers. CX-22 – CX-25. The Complaint charges that Respondent disclosed confidential information about China Merchants Bank's earnings in the e-mails she sent on April 10, 2007.

Respondent had received the information she disclosed from CICC HK's research department in a morning meeting and in a research report. The information was based on a China Merchants Bank announcement on August 10 concerning the approval of a large tax deduction by the Chinese government. RX-19, RX-63, RX-64, RX-65, RX-80; Tr. 292, 294, 275, 280, 285, 1010, 1019, 1021-1023, 768-773.

The Extended Hearing Panel finds that Respondent did not disclose confidential information about China Merchants Bank's anticipated earnings. The information was not confidential, and as a CICC HK salesperson, Respondent was authorized and expected to disclose the information. In addition, the projections were derived from public information, and investors and analysts could use the same information to make earnings predictions. The Extended Hearing Panel dismisses the Complaint with respect to the China Merchants Bank disclosures.

C. The Complaint Is Dismissed with Respect to Respondent's Communications about Genesis Energy Holdings Because She Did Not Disclose Confidential Information or Misrepresent the Source of Her Information

Genesis Energy Holdings, Ltd. is an oil and gas services company based in Hong Kong. Tr. 325. On March 30, 2007, Genesis announced it had signed a nonbinding letter of intent with Liberia for possible investment in oil and gas projects in Liberia. CX-28. Respondent sent e-mails concerning Genesis on April 13, 2007, to a fellow trader at CICC HK and three clients. The e-mail to the CICC HK trader suggested that he buy Genesis for his personal account because there was a big oil deal coming the following week, and reported that top management of a Chinese oil company was buying Genesis stock. CX-30. The e-mail to the clients said Genesis management told Respondent about an oil deal that would be announced the following week. CX-31. The Complaint alleges that the e-mails disclosed information that was not known to the general public, and misrepresented to the three clients that the source of her information was Genesis management.

On April 13, 2007, before she sent the e-mails, [Respondent] had lunch with the vice president for investor relations of Genesis and his assistant investor relations manager. She had been invited to the lunch by a friend who was salesperson at another brokerage firm, who also attended the lunch. The information in her e-mails was derived from the information disclosed by Genesis personnel at the lunch. Tr. 330-332, 336, 337, 344, 1024-1025. Much of the information she disclosed was already known to the public. RX-24.[9]

Respondent's e-mails did not inappropriately disclose any information about Genesis. The disclosure of information by a vice president for investor relations and his assistant to

[9] Market Regulation cites a release by Genesis the following week, announcing the appointment of a technical advisory board, as the allegedly confidential information that Genesis made public after Respondent's e-mails. CX-33; Complaint ¶ 26. The release does not mention a Liberian oil deal. CX-33. The appointment of a technical advisory board was not mentioned at the lunch. Tr. 352, 1076. The relationship to the information about an impending oil deal in Respondent's e-mails is indirect, at best.

salespeople from two brokerage firms strongly suggests that Genesis did not regard the information as confidential. *See* Tr. 1252-1253. In addition, the information was known to the public or derivable from public sources. The Extended Hearing Panel dismisses the Complaint with respect to the Genesis disclosures.

Market Regulation also did not show that Respondent's attribution of information to Genesis management was a misrepresentation. Her information came from a member of Genesis management, and therefore her e-mail was accurate. Furthermore, the attribution of information to "management," rather than the vice president for investor relations and an assistant, was not material. Potential investors would expect a vice president for investor relations to be knowledgeable about developments at a company like Genesis, and to speak on behalf of management. The Extended Hearing Panel dismisses the Complaint with respect to the alleged misrepresentation about the source of Respondent's information about Genesis because the information was accurate.

D. The Complaint Is also Dismissed with Respect to Respondent's Conduct Prior to Her FINRA Registration Because She Was Not Associated with a Member Firm

Market Regulation argues that Respondent was associated with CICC US before the firm became a FINRA member because she was allegedly an employee while its FINRA application was pending. The evidence clearly establishes that Respondent was not employed by CICC US before the firm became a FINRA member, and was not associated with the firm under FINRA's By-Laws. Thus, Respondent's communications with respect to Citic Bank, China Merchants Bank, and Genesis Energy Holdings did not violate NASD Rule 2110.

At the time of the first three alleged violations, Article I, Sec. (rr) of NASD By-Laws defined "person associated with a member," in relevant part, as:

> a sole proprietor, partner, officer, director, or branch manager of a member, or other natural person occupying a similar status or performing similar functions, or a natural person engaged in the investment banking or securities business who is directly or indirectly controlling or controlled by a member, whether or not any such person is registered or exempt from registration with the NASD under these By-Laws or the Rules of the Association . . . .

In response to a motion in limine, Market Regulation argued that Respondent was an associated person under FINRA's By-Laws because she was "a natural person engaged in securities business who [was] directly or indirectly controlled by member, whether or not any such person is registered or exempt from registration."[10] Respondent was not engaged in the securities business for CICC US, which had no securities business. Furthermore, there is no evidence that she was ever controlled by CICC US.[11]

The only evidence Market Regulation offered to establish that [Respondent] was employed by CICC US before she registered with FINRA is her Form U4. But the document is unreliable, with obvious errors indicating that the CICC HK compliance department prepared the document carelessly, and that Respondent did not review it for accuracy.[12] Furthermore, there is persuasive evidence that Respondent was not employed by CICC US during the pre-registration period. The president of CICC US, its first functioning chief compliance officer, and Respondent all testified that she was never employed by the firm. The firm's financial

[10] Market Regulation's Omnibus Response to Respondent's Motions *In Limine* and Objections to Witnesses and Exhibits, April 4, 2013.

[11] Market Regulation also cites to NASD Rule 1011 in its pre-hearing brief, arguing that FINRA's Rules apply to "an employee of the Applicant, except any person whose functions are solely clerical or ministerial…." Pre-Hearing brief at 8. NASD Rule 1011 relates to registration, not jurisdiction. *Dep't of Enforcement v. Reichman*, No. 200801201960, 2011 FINRA Discip. LEXIS 18, at *25-27 (N.A.C. July 21, 2011).

[12] Respondent has not been charged with filing an inaccurate Form U4, and the Extended Hearing Panel expresses no opinion on whether her lack of care in signing her Form U4 despite the obvious errors constitutes a violation of NASD Rule 2110.

documents show that it paid no salaries or commissions to anyone before the firm's FINRA membership was approved. The firm had no operations, clients, or revenue during this period.

Even if Respondent had been an employee of CICC US, she was not an "associated person of a member firm" prior to her FINRA registration. Market Regulation argues that her actions prior to the firm's FINRA membership could violate FINRA's Rules, citing two cases in which persons associated with member firms prior to the firms' FINRA membership were found to have violated FINRA's Rules by their pre-registration conduct.[13] The facts of both of those cases are very different from the facts of the case against Respondent. Both involved senior members of their respective firms who were actively involved in the firm's business. The respondent in *Hatzis* was the founder and president of the applicant, and signed many of the documents submitted to FINRA by the firm. His alleged misconduct related specifically to the firm's membership application. He had submitted a Form U4 for himself with the firm's application for membership.[14] In *First Capital*, the individual respondent was the firm's senior vice president and compliance officer. At the time of the alleged violation, while the firm's membership application was pending, he had submitted a Form U4 for himself to FINRA.[15] Thus, the National Business Conduct Committee noted, at the time of the alleged violation, the individual respondent had already consented to be subject to FINRA's jurisdiction and rules. Neither case is comparable to the case against [Respondent]. Even if she had technically been a CICC US employee, there is no evidence that she had any role, let alone a senior role, in the

[13] *See* Dep't of Member Regulation's Pre-Hearing Brief at 8, citing *Dist. Bus. Con. Comm. v. First Capital Funding, Inc.*, 1990 NASD Discip. LEXIS 119, at *13-14 (N.B.C.C. Aug. 16, 1990), *aff'd*, 50 S.E.C. 1026 (1992), and *Dep't of Enforcement v. Hatzis*, 2010 FINRA Discip. LEXIS 14, at *4 (O.H.O. Mar. 22, 2010).

[14] *Hatzis*, 2010 FINRA Discip. LEXIS 14, at *33; *see*, NASD By-Laws, Article 1, Sec. (rr): "'person associated with a member' or 'associated person of a member' means: (1) a natural person who is registered or has applied for registration under the Rules of the Corporation…."

[15] *First Capital*, 1990 NASD Discip. LEXIS 119, at *3.

firm's operations before it became a FINRA member, and she did not submit a Form U4 until after the firm became a FINRA member.

The allegations concerning Citic Bank, China Merchants Bank, and Genesis Energy Holdings, are dismissed because Respondent was not associated with a member firm when the alleged disclosures occurred.

V. The Complaint Is Dismissed with Respect to the Alleged Disclosures of Confidential Information While Respondent Was Registered with FINRA

The Complaint charges that Respondent made three disclosures of confidential information while she was registered with CICC US, in violation of NASD Rule 2110. The Extended Hearing Panel finds that much of the information she disclosed was not confidential. Respondent admits that she made two inappropriate disclosures. At the time she made these disclosures, she was working solely for CICC HK. She had never worked for CICC US, and CICC US was not yet conducting any business. One disclosure was based on a mistaken belief that the information was public, and the other was done to correct the omission of a client's name from a list of those who should have received a research report. Under these unusual circumstances, the Extended Hearing Panel finds that these disclosures did not violate NASD Rule 2110.

A. The Charge Relating to Communications about China Mobile Hong Kong Ltd. Is Dismissed

China Mobile Hong Kong Ltd. is a mobile communications operator in Hong Kong. CICC HK provided analyst coverage of China Mobile. Tr. 358-359. Between July 28 and July 31, 2008, Respondent sent e-mails to clients reporting that she had heard from her analyst that China Mobile would miss its earnings forecast for the first half of 2008 by two points. She said the information was not known to "most of the street," and that a CICC HK client, a major mutual fund, was making substantial sales of the stock. She advised one client to go short on the

stock. CX-35, CX-37; Tr. 363. She was more explicit in the final e-mail, advising clients that CICC HK's analysts believed China Mobile's earnings would miss the forecasts, and said they should call her to chat because "we are in blackout period." CX-39. She told one client that China Mobile's "largest [shareholder], staff" were selling shares. China Mobile's staff were CICC HK clients. CX-38; Tr. 374.

Respondent had received the information about the anticipated earnings shortfall from a CICC HK analyst in a morning meeting. The analyst said he had learned from a Chinese-language website that China Mobile would miss the earnings forecasts due to extra capital expenditures. Because he was a native Chinese speaker, he was able to get the information earlier than most of the street. Tr. 366, 369-371, 1028-1032; RX-1 at Ex. 4.3.

In Hong Kong, it is quite common to publish opinions on whether an issuer might miss earnings, a subject that is considered "ordinary teatime chat." Tr. 1257-1258. Respondent's reference in her e-mail to the blackout period referred to the issuer, because issuers are not permitted to talk to investors 30 days before an earnings announcement. Tr. 379.[16] The blackout did not apply to CICC HK. Tr. 379; see also general discussion of Hong Kong securities practices above.

Respondent also did not breach any confidentiality obligations by disclosing that a major mutual fund was selling China Mobile stock. In Hong Kong, it is a common practice to discuss trading flows as long as the salesperson does not disclose the client's name. Tr. 363, 1034-1035, 847-848, 852, 1260-1262, 1290, 1300-1301.

The Extended Hearing Panel finds that Respondent did not inappropriately disclose information China Mobile's projected earnings because the information was not confidential, and

[16] Respondent testified that her purpose in mentioning the blackout was to advise recipients not to call China Mobile management. Tr. 381.

as a salesperson, she was expected to provide such information to clients. Her disclosure about sales by a major mutual fund was not inappropriate because the information is not considered confidential in Hong Kong. The Extended Hearing Panel dismisses the Complaint with respect to the China Mobile earnings disclosures, including the disclosures about sales by a major mutual fund.

It was not permissible or accepted practice in Hong Kong to disclose orders by specific customers. China Mobile's staff was the company's largest private shareholder. Tr. 374-375. Respondent admits that she erred by disclosing sales of China Mobile stock by China Mobile's staff. Tr. 384, 1033. Respondent thought the information about staff sales was public information, because any shareholder who owns more than 5% of a public company must report all trades to the Hong Kong Stock Exchange within three days. Company directors must also disclose all trades within three days. Respondent believed the sales she disclosed were subject to these disclosures. Tr. 384-388, 1035-1037, 1059-1060, 1262-1263. She admitted that she made a mistake by not verifying that the sales had been disclosed on the Hong Kong Exchange website. In fact, the sales by the staff were not public information. Tr. 388-389.

As Respondent has acknowledged, her disclosure about sales by China Mobile staff was inappropriate. However, the Extended Hearing Panel finds that the disclosure did not violate NASD Rule 2110. The disclosure was careless, not intentional, and done in the good-faith belief that the information was not confidential. At the time of the disclosure, Respondent was employed by CICC HK, and acting on behalf of that firm. Although she was registered with CICC US, she was never employed by the firm or did any work on behalf of the firm, and the firm had not yet begun operations at the time of her disclosure. Under these circumstances, the

Extended Hearing Panel finds that her disclosures did not violate NASD Rule 2110, and dismisses the Complaint with respect to this charge.

B. The Charge Relating to Communications about China Southern Locomotive & Rolling Stock Corp. IPO Is Dismissed

Southern Locomotive is one of two train manufacturers in China. Tr. 404. In the summer of 2008, Southern Locomotive was planning an IPO, for which CICC HK would serve as an underwriter. Tr. 404. On Friday, July 11, 2008, Respondent sent e-mails to clients requesting meetings concerning an upcoming IPO. She said she could not name the issuer, but that it was "the largest locomotive maker in China." CX-44. Less than an hour later, she sent another e-mail, this time identifying the issuer as "southern locomotive" and disclosing that CICC HK would be the lead underwriter. CX-45.

Southern Locomotive's intention to apply for permission to issue an IPO, and CICC HK's role as an underwriter, were widely known. RX-1. There had been articles in the financial press about Southern Locomotive's proposed IPO application as early as June 26, 2008. RX-34 (Dow Jones), RX-35 (Reuters), RX-36 (Bloomberg), RX-38 (Xinhua Finance).

In Hong Kong, an IPO issuer must apply to the Hong Kong Stock Exchange to be listed. Hearings on IPO applications take place on Thursdays, and the results are known by the CICC HK sales staff on Friday mornings. Tr. 408, 1269-1270. Before Respondent sent her first e-mail, Respondent's manager had told her not to mention the name of the issuer to clients in case the IPO did not pass the hearing for listing on the Hong Kong Exchange, which would result in postponement of the IPO for a week. It is a common practice in Hong Kong for issuers not to mention the filing of the application, to save face in the event the application is rejected. It is also common to use a different name for the issuer. Tr. 406-408, 1270-1272. In the hour between the sending of the first and second e-mails, on a Friday morning, Respondent learned

that Southern Locomotive's IPO had passed the hearing, so it was permissible and appropriate for her to identify the company by name. Tr. 407, 412-13, 1268, 1273.

The Extended Hearing Panel finds that Respondent's disclosure of information about Southern Locomotive's IPO was not inappropriate. The IPO application was known to the public, and it was consistent with Hong Kong practice to use a slightly different name to identify the issuer before the application was approved. When the IPO was approved, it was proper to use the issuer's name in her communications. The Extended Hearing Panel dismisses the Complaint with respect to Southern Locomotive disclosures.

C. The Charge Relating to the Delivery of the Southern Locomotive Pre-IPO Research Report Is Dismissed

The Complaint charges Respondent with delivering a copy of a CICC HK research report on Southern Locomotive to an investor that was not on the list of those who were permitted to receive the report, during a period when distribution of research reports was prohibited. Respondent admitted that she delivered the research report to the client during a restricted period, but explained that the client was inadvertently left off the distribution list and should have received the report when it was distributed to authorized recipients.

Hong Kong has no law on when IPO research can be distributed. The timing of distribution is controlled by agreement of members of the syndicate. Typically, the syndicate agrees that research may be distributed only for a short period after the Hong Kong Stock Exchange approves the IPO. Tr. 415, 1275. The syndicate also controls who gets research reports. Tr. 424.

D.E. Shaw, a large hedge fund, should have been on the distribution list for the Southern Locomotive research report, but was inadvertently omitted. On July 11, before the issuance of the IPO research report, the head of the Sales & Trading Department in Hong had instructed

Sales & Trading to invite the hedge fund to the road show for the IPO. The hedge fund was invited to the road show, and attended. CX-57, CX-69; RX-46, RX-74, RX-77; Tr. 1042-1045. D.E. Shaw was one of CICC HK's biggest clients, and CICC HK expected the hedge fund to be an anchor investor in the Southern Locomotive IPO. Its omission from the list of those authorized to receive the report was the result of an administrative error, probably by Respondent or another member of her team. Tr. 428-430, 1044, 1047.[17]

On July 16, 2008, when Respondent learned that D.E. Shaw had not received a copy of the Southern Locomotive research report, she sent an e-mail to KP, the head trader at D.E. Shaw, noting that "no one has a copy of our precious south locomotive ipo report…" and said she would drop the research report off the next day. CX-53; Tr. 416. Soon after she sent the e-mail to KP, Respondent sent an e-mail to KP's assistant, saying she could not send the report by e-mail "since we are already in black out … but will drop [KP] a copy so you will have one." CX-54. She could not send the report by e-mail because research reports are always in hard copy, not electronic. Tr. 423. Although she said "we are already in black out," there was not a legal blackout. However, they were in the restricted period, when research cannot be distributed, by agreement of the syndicate. Tr. 172-173, 414, 418-419. Respondent personally delivered a copy of the Southern Locomotive IPO report to KP in Hong Kong next day. Tr. 415, 419, 1053.

Respondent admits that she deliberately broke the rule on delivery of IPO research reports by delivering the report to the hedge fund, and that she should have gotten approval from CICC HK to distribute the research report to the hedge fund. Tr. 440, 1059. Respondent should not have delivered the IPO research report to a firm that was not on the list of approved recipients, at a time when delivery was not permitted, without approval by her firm. However,

[17] D.E. Shaw ultimately made a large investment in the China Southern IPO. RX-75; Tr. 430, 1056, 1060.

the Extended Hearing Panel finds that her delivery of the report did not violate NASD Rule 2110, and dismisses the Complaint with respect to this charge. She delivered the report to someone who should have received it previously, to correct an error by her group. The report was not intended to be confidential with respect to D.E. Shaw, who would have learned the information in the research report soon, since D.E. Shaw was invited to the IPO road show. The delivery benefited both the issuer and D.E. Shaw, because D.E. Shaw made a substantial investment in the Southern Locomotive IPO. In addition, as with her disclosure of purchases by China Mobile staff, her disclosure was made in her capacity as a broker at CICC HK, while she was not working for CICC US, which had not yet started to do business.

VI. Conclusion

The Department of Market Regulation has failed to prove that Respondent violated NASD Rule 2110 by disclosing confidential information or misrepresenting the source of information. The Complaint is dismissed.

EXTENDED HEARING PANEL.

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Lawrence B. Bernard
Hearing Officer

Copies to: Respondent (*via first-class mail*)
Dana S. Gloor, Esq. (*via electronic and first-class mail*)
David S. Richan, Esq. (*via electronic mail*)
Shannon D. Rozner, Esq. (*via electronic and first-class mail*)
Edwin T. Aradi, Esq. (*via electronic mail*)
James J. Nixon, Esq. (*via electronic mail*)