

PART VI
CAPITAL REQUIREMENTS, CLIENT ASSETS,
RECORDS AND AUDIT RELATING
TO INTERMEDIARIES

Division 1 - Interpretation

140. Interpretation of Part VI

In this Part, unless the context otherwise requires -
"specified amount requirements" (指明數額規定) means the
requirements specified in the financial resources rules
pursuant to section 141(2)(a)(i).

Division 2 - Capital requirements

141. Financial resources of licensed corporations

(1) The Commission may, after consultation with the Financial
Secretary, make rules requiring licensed corporations to maintain
such financial resources as are specified in the rules.

(2) Without limiting the generality of subsection (1) and
without prejudice to section ~~384(9)~~384A(7) and ~~(108)~~^{*}, the
Commission may in the rules referred to in subsection (1) -

- (a) require licensed corporations to maintain
financial resources in accordance with -

* **The amendment is consequential to the relocation of provisions in Part XVI.**

- (i) specified requirements as to the amount in which they are to be maintained; and
 - (ii) any other specified requirements;
- (b) specify the assets, liabilities and other matters to be taken into account under the rules to determine the amount of the financial resources of licensed corporations for the purposes of the rules and the extent to which, and the manner in which, they are to be taken into account for that purpose;
- (c) provide for the different treatment of the assets, liabilities and other matters for the purposes of the rules according to whether or not they are approved by the Commission for that purpose;
- (d) provide that the rules, or any of the provisions of the rules, do not apply to licensed corporations which maintain financial resources, in Hong Kong or elsewhere, in accordance with an authorization of an authority, in Hong Kong or elsewhere, which in the opinion of the Commission performs a function which involves the imposition of requirements relating to financial resources of persons carrying on activities similar to any regulated activity for which a licensed person may be licensed, or apply to such licensed corporations with specified modifications or only in specified circumstances;

- (e) provide for the grant of approvals for specified purposes and for the amendment or revocation of such approvals, and for the publication of such approvals and of any amendment or revocation of such approvals in the specified manner;
- (f) require licensed corporations to submit to the Commission -
 - (i) at specified intervals, returns relating to their financial resources and trading activities; and
 - (ii) notice in writing of specified circumstances relating to their financial resources and trading activities;
- (g) require licensed corporations to submit returns to the Commission in response to a request by the Commission for information relating to their financial resources and trading activities;
- (h) provide for any other matter relating to financial resources of licensed corporations.

142. Failure to comply with financial resources rules

(1) If a licensed corporation becomes aware of its inability to maintain, or to ascertain whether it maintains, financial resources

in accordance with the specified amount requirements that apply to it, it shall ~~on the~~
~~day on which it becomes aware of such inability~~

- (a) as soon as reasonably practicable notify the Commission by notice in writing of that fact; and
- (b) subject to subsection (2), immediately cease carrying on any regulated activity for which it is licensed, otherwise than for the purpose of completing such transactions as the Commission may permit.

(2) Where the Commission considers appropriate, the Commission may permit a licensed corporation which gives notice to the Commission under subsection (1)(a) to carry on any regulated activity for which it is licensed, subject to such conditions as may be imposed by the Commission by notice given to it, whether orally or in writing.

(3) If a licensed corporation becomes aware of its inability to comply with, or to ascertain whether it complies with, all or any of the requirements of the financial resources rules that apply to it, other than the specified amount requirements, it shall within one business day thereafter notify the Commission by notice in

¹ Under section 65C of the Securities Ordinance, the requirement is to "forthwith" notify the SFC and cease trading. In our attempt to clarify the meaning of "forthwith", we have inadvertently relaxed the requirement. On reflection, given the significant implication of non-compliance with the financial resources rules in terms of investor protection, we propose the amendment to tighten the respective time limits such that the reporting to the SFC should be "as soon as reasonably practicable" and the cessation of the regulated activity should be "immediate". **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

writing of that fact.

(4) Without limiting the generality of the financial resources rules and the rules that may be made under section 147, a licensed corporation to which any of the requirements of the financial resources rules apply shall -

- (a) keep its records in sufficient detail to establish readily whether all of such requirements are being complied with; and
- (b) where the Commission by notice in writing served on it requires it to do so, make its records available to the Commission within 5 business days after the service of the notice.

(5) Without prejudice to sections 187 and 188, where the Commission reasonably believes that a licensed corporation is unable to maintain, or to ascertain whether it maintains, financial resources in accordance with the specified amount requirements that apply to it, the Commission may, whether or not notice has been given under subsection (1)(a) -

- (a) ²by notice in writing served on the licensed corporation suspend the licensed corporation's licence, whether in relation to all or any, or any part of all or any, of the regulated activities for which it is licensed for such period or until the

² Technical amendment to enable specification of the time a decision can take effect referred to in the newly introduced clause 142(7B). **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

occurrence of such event as the Commission may specify; or

- (b) permit the licensed corporation to carry on any regulated activity for which it is licensed, subject to such conditions as may be imposed by the Commission by notice given to it, whether orally or in writing.

(6) Where any conditions are imposed pursuant to subsection (2) or (5)(b) by notice given to a licensed corporation in writing, the Commission may amend any of the conditions in such manner as may be specified by the Commission, by notice given to the licensed corporation, whether orally or in writing, and where any of the conditions are so amended -

- (a) such conditions shall have effect subject to the amendment accordingly; and
- (b) where the conditions are amended by notice in writing, this subsection shall apply, with necessary modifications, to the conditions as so amended as if they had been imposed pursuant to subsection (2) or (5)(b) (as the case may be).

(7) Where any conditions are imposed pursuant to subsection (2) or (5)(b), or amended under subsection (6), by notice given to a licensed corporation otherwise than in writing, the Commission shall as soon as reasonably practicable give ~~to~~ the licensed corporation a further notice in writing to confirm the conditions imposed or the conditions as amended (as the case may be), subject

to such amendment (if any) in respect of the conditions as it may specify in the notice, and where any conditions are so confirmed subject to any amendment -

- (a) the conditions shall have effect subject to the amendment accordingly; and
- (b) subsection (6) shall apply, with necessary modifications, to the conditions as so amended as if they had been imposed pursuant to subsection (2) or (5)(b) (as the case may be).

³(7A) Notwithstanding anything in this section, the Commission shall not impose any conditions pursuant to subsection (2) or (5)(b), or amend any conditions under subsection (6), by notice given to a licensed corporation otherwise than in writing if the licensed corporation has on the occasion of being heard pursuant to subsection (9A) in respect of the imposition or amendment (as the case may be) made a request to the Commission that the conditions shall only be so imposed, or amended, by notice given to it in writing.

³ This is to address the concern of some Members and stockbrokers about possible disputes over conditions imposed orally. We believe that it would indeed be beneficial to the market that the SFC has the flexibility to impose conditions orally such that the relevant matter can be dealt with more speedily and the concerned licensed corporation can, for example, continue trading as soon as possible. This is shared by some brokers. However, in the light of the different views expressed, we propose the amendment to provide the concerned licensed corporation an option to request to have the imposition of in-writing conditions. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

⁴(7B) The suspension of a licence under subsection (5)(a) takes effect at the time when notice is served in respect of it pursuant to that subsection or at the time specified in the notice, whichever is the later.

(8) The imposition of any conditions pursuant to subsection (2) or (5)(b), or the amendment of any conditions under or pursuant to subsection (6) or (7), takes effect at the time when notice is given in respect of it pursuant to such subsection or at the time specified in the notice, whichever is the later.

(9) Where a licence of a licensed corporation is suspended under subsection (5)(a), sections 192(1), 193(2) and (5), 194 and 195 shall apply, with necessary modifications, in relation to the suspension as if it were a suspension under section 187 or 188.

⁴ We propose the amendment such that the SFC can order immediate suspension of the licence of a corporation which is in breach of the Financial Resources Rules without awaiting, for example, the determination of any relevant appeal. This is considered justified and necessary in the light of SFC's regulatory experience as failure to comply with the Financial Resources Rules by a licensed corporation is a very serious matter, and such that its ability to protect investors' would not be undermined. Such arrangement is also consistent with for example, clause 143(6) that concerns with the time the conditions imposed by the SFC (when a licensed corporation fails to comply with the Financial Resources Rules) can take effect. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

⁵(9A) Notwithstanding anything in this section, the Commission shall not exercise any power under subsection (1)(b), (2), (4)(b), (5), (6), (7), (7B) or (8) in respect of a licensed corporation unless the Commission has given the licensed corporation a reasonable opportunity of being heard.

(10) A licensed corporation which contravenes subsection (1)(a) or (b) commits an offence and is liable -

(a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 2 years and, in the case of a continuing offence, to a further fine of \$100,000 for every day during which the offence continues; or

(b) on summary conviction to a fine at level 6 and to imprisonment for 6 months and, in the case of a continuing offence, to a further fine of \$10,000 for every day during which the offence continues.

(11) A licensed corporation which contravenes a condition imposed pursuant to subsection (2) or (5)(b), or as amended under or pursuant to subsection (6) or (7), commits an offence and is liable -

(a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 2 years and, in the case of a continuing offence, to a further fine of

⁵ Technical amendment to make it clear that an opportunity of being heard is being afforded. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

\$100,000 for every day during which the offence continues; or

- (b) on summary conviction to a fine at level 6 and to imprisonment for 6 months and, in the case of a continuing offence, to a further fine of \$10,000 for every day during which the offence continues.

(12) A licensed corporation which, without reasonable excuse, contravenes subsection (3) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$200,000 and to imprisonment for 1 year; or
- (b) on summary conviction to a fine at level 5 and to imprisonment for 6 months.

(13) A licensed corporation which contravenes subsection (4) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 2 years; or
- (b) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

(14) The financial resources rules may provide that a licensed corporation which, without reasonable excuse, contravenes any specified provision of the financial resources rules that applies to it, other than that imposing any of the specified amount requirements, commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$200,000 and a term of imprisonment of 1 year;

(b) on summary conviction a fine at level 5 and a term of imprisonment of 6 months.

⁶(15) A licensed corporation is not excused from complying with subsection (3) only on the ground that to do so might tend to incriminate it.

143. Monitoring compliance with financial resources rules

(1) The Commission may at any time, by notice in writing served on an executive officer of a licensed corporation, require the licensed corporation to satisfy the Commission that it complies with all of the requirements of the financial resources rules that apply to it.

⁶ At the Bills Committee meeting on 16 July 2001, we briefed Members on our policy intention: in order that timely remedial action can be taken which is essential for investor protection, an intermediary or an associated entity in breach of certain prescribed requirements imposed under the Financial Resources Rules and other rules made under this Part is required to report to the SFC the breach. As the information might incriminate the intermediary or associated entity, we propose to restrict the use of the information by introducing a use immunity provision to protect him. To reflect the policy intention, amendments are now introduced in clauses 142, 144, 145, 147, 148, and 161 to require notification of certain breaches to the SFC; and a new clause 161A is added to provide that such notification shall not be admissible in evidence against the intermediary or associated entity in criminal proceedings in a court of law except under limited circumstances (e.g. perjury) as permitted under human rights principles. The proposed amendments are modeled on clauses 172, 176 and 180 under Part VIII which have been scrutinized and agreed by Members at the meeting on 17 July 2001.

—(2) Without limiting the generality of subsection (1), the Commission and any person authorized by the Commission under subsection (9) may exercise any of the powers of an auditor referred to in section 158 for the purpose of ascertaining whether a licensed corporation complies with all of the requirements of the financial resources rules that apply to it.

(3) Without prejudice to sections 187 and 188, where a licensed corporation, upon being required to do so under subsection (1), fails to satisfy the Commission that it maintains financial resources in accordance with the specified amount requirements that apply to it, the Commission may -

- (a) by notice in writing served on the licensed corporation suspend the licensed corporation's licence, whether in relation to all or any, or any part of all or any, of the regulated activities for which it is licensed for such period or until the occurrence of such event as the Commission may specify; or
- (b) permit the licensed corporation to carry on any regulated activity for which it is licensed, subject to such conditions as may be imposed by the Commission by notice given to it, whether orally or in writing.

⁷ Technical amendment to enable specification of the time a decision can take effect referred to in the newly introduced clause 143(5B). **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

(4) Where any conditions are imposed pursuant to subsection (3)(b) by notice given to a licensed corporation in writing, the Commission may amend any of the conditions in such manner as may be specified by the Commission, by notice given to the licensed corporation, whether orally or in writing, and where any of the conditions are so amended -

- (a) such conditions shall have effect subject to the amendment accordingly; and
- (b) where the conditions are amended by notice in writing, this subsection shall apply, with necessary modifications, to the conditions as so amended as if they had been imposed pursuant to subsection (3)(b).

(5) Where any conditions are imposed pursuant to subsection (3)(b), or amended under subsection (4), by notice given to a licensed corporation otherwise than in writing, the Commission shall as soon as reasonably practicable give ~~to~~ the licensed corporation a further notice in writing to confirm the conditions imposed or the conditions as amended (as the case may be), subject to such amendment (if any) in respect of the conditions as it may specify in the notice, and where any conditions are so confirmed subject to any amendment -

- (a) the conditions shall have effect subject to the amendment accordingly; and
- (b) subsection (4) shall apply, with necessary modifications, to the conditions as so amended as

if they had been imposed pursuant to subsection (3)(b).

⁸(5A) Notwithstanding anything in this section, the Commission shall not impose any conditions pursuant to subsection (3)(b), or amend any conditions under subsection (4), by notice given to a licensed corporation otherwise than in writing if the licensed corporation has on the occasion of being heard pursuant to subsection (7A) in respect of the imposition or amendment (as the case may be) made a request to the Commission that the conditions shall only be so imposed, or amended, by notice given to it in writing.

⁸ This is to address the concern of some Members and brokers about possible disputes over conditions imposed orally. We believe that it would indeed be beneficial to the market that the SFC has the flexibility to impose conditions orally such that the relevant matter can be dealt with more speedily and the concerned licensed corporation can, for example, continue trading as soon as possible. This is shared by some brokers. However, in the light of the different views expressed, we propose the amendment to provide the concerned licensed corporation an option to request to have the imposition of in-writing conditions. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

⁹(5B) The suspension of a licence under subsection (3)(a) takes effect at the time when notice is served in respect of it pursuant to that subsection or at the time specified in the notice, whichever is the later.

(6) The imposition of any conditions pursuant to subsection (3)(b), or the amendment of any conditions under or pursuant to subsection (4) or (5), takes effect at the time when notice is given in respect of it pursuant to such subsection or at the time specified in the notice, whichever is the later.

(7) Where a licence of a licensed corporation is suspended under subsection (3)(a), sections 192(1), 193(2) and (5), 194 and 195 shall apply, with necessary modifications, in relation to the suspension as if it were a suspension under section 187 or 188.

(7A) Notwithstanding anything in this section -

(a) the Commission or any person authorized by the Commission under subsection (9) shall not exercise any power under subsection (2) in respect of a licensed corporation;

⁹ We propose the amendment such that the SFC can order immediate suspension of the licence of a corporation which is in breach of the Financial Resources Rules without awaiting, for example, the determination of any relevant appeal. This is considered justified and necessary in the light of SFC's regulatory experience as failure to comply with the Financial Resources Rules by a licensed corporation is a very serious matter, and such that its ability to protect investors' would not be undermined. Such arrangement is also consistent with for example, clause 143(6) concerning the time the conditions imposed by the SFC when a licensed corporation fails to comply with the Financial Resources Rules, can take effect. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

¹⁰(b) the Commission shall not exercise any power under subsection (3), (4), (5), (5B) or (6) in respect of a licensed corporation,

unless the Commission or the person (as the case may be) has given the licensed corporation a reasonable opportunity of being heard.

(8) A licensed corporation which contravenes a condition imposed pursuant to subsection (3)(b), or as amended under or pursuant to subsection (4) or (5), commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 2 years and, in the case of a continuing offence, to a further fine of \$100,000 for every day during which the offence continues; or
- (b) on summary conviction to a fine at level 6 and to imprisonment for 6 months and, in the case of a continuing offence, to a further fine of \$10,000 for every day during which the offence continues.

(9) For the purposes of subsection (2), the Commission may authorize any person in writing to exercise any of the powers referred to in that subsection.

Division 3 - Client assets

¹⁰ Technical amendment to make it clear that there is an opportunity of being heard before the SFC or the person authorized by the SFC (as the case may be) exercises the power under clause 143(2), (3), (4), (5), (5B) or (6).

**144. Client securities and collateral held by
intermediaries and their associated
entities**

(1) The Commission may make rules requiring intermediaries and their associated entities to treat and deal with client securities and collateral of the intermediaries, and to ensure that client securities and collateral of the intermediaries that are received or held by any other person ~~on their behalf~~ of the intermediaries or the associated entities (as the case may be)¹¹ are treated and dealt with, in such manner as is specified in the rules.

(2) Without limiting the generality of subsection (1) and without prejudice to section ~~384(9)~~384A(7) and ~~(108)~~^{*}, the Commission may in the rules referred to in subsection (1) -

- (a) require client securities and collateral of intermediaries to be held, and accounted for, in the specified manner;
- (b) provide that the client securities and collateral shall not be deposited, transferred, lent, pledged, repledged or otherwise dealt with except in the specified manner;
- (c) specify the circumstances in which the client securities and collateral may, notwithstanding that they are subject to a lawful claim or lien,

¹¹ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

be dealt with by intermediaries or their associated entities;

- (d) provide for the approval, subject to such conditions as the Commission considers appropriate, of companies or overseas companies as being suitable for the safe custody of the client securities and collateral;
- (e) require intermediaries and their associated entities to ensure, or to take reasonable steps to ensure, that persons who receive or hold the client securities and collateral on their behalf of the intermediaries or the associated entities (as the case may be)¹² comply with specified requirements;
- (f) require the maintenance of records in relation to the client securities and collateral (including records of performance of reconciliations in respect of movements of the client securities and collateral into and out of accounts of intermediaries or their associated entities) in the specified manner;
- (g) require the submission to the Commission, upon request or at specified intervals, of specified information, records and documents for the purpose

¹² Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

of enabling the Commission to ascertain readily whether the rules are being complied with;

- (h) require specified matters, and the circumstances relevant thereto, to be notified to the clients of intermediaries or the Commission, or both;
- (i) require a person who becomes aware that he does not comply with any specified provision of the rules that applies to him to notify the Commission of that fact and of any further specified information, within the specified time;
- (j) provide for any other matter relating to the client securities and collateral.

(3) Except as provided in the rules made under this section, client securities and collateral of an intermediary are not liable to be taken in execution against the intermediary or an associated entity of the intermediary under the order or process of a court.

(4) Rules made under this section may provide that an intermediary, or an associated entity of an intermediary, which, without reasonable excuse, contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$200,000 and a term of imprisonment of 2 years;
- (b) on summary conviction a fine at level 6 and a term of imprisonment of 6 months.

(5) Rules made under this section may provide that an

intermediary, or an associated entity of an intermediary, which, with intent to defraud, contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$1,000,000 and a term of imprisonment of 7 years;
- (b) on summary conviction a fine of \$500,000 and a term of imprisonment of 1 year.

⁶(5A) A person is not excused from complying with a requirement in any rules made pursuant to subsection (2)(i) to give notification to the Commission only on the ground that to do so might tend to incriminate the person.

(6) Notwithstanding anything in this section -

- (a) the power of the Commission to make rules under this section in respect of intermediaries shall, where the intermediaries are ~~exempt persons~~ registered institutions¹³, be regarded as the power to make rules in respect of the intermediaries only in relation to client securities and collateral received or held by them in the course of the businesses which constitute ~~the~~ any¹⁴ regulated

¹³ **We accept the comment of some Members that the term “exempt person” is a misnomer and does not reflect the proposed regulatory framework whereby authorized institutions engaging in regulated activities are subject to a whole range of regulatory requirements and disciplinary sanctions. We informed Members at the meeting on 14 September 2001 that we would replace “exempt person” with “registered institution” and “exempt” with “registered” throughout the Bill to duly reflect our policy intention.**

¹⁴ **Technical amendment for consistency. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

activities for which they are ~~exempt as exempt~~
~~persons~~registered¹³;

- (b) the power of the Commission to make rules under this section in respect of associated entities shall, where the associated entities are authorized financial institutions, be regarded as the power to make rules in respect of the associated entities only in relation to client securities and collateral received or held by them in the course of their businesses of receiving or holding client securities and collateral of intermediaries of which they are associated entities.

(7) Notwithstanding anything in subsection (3), that subsection -

- (a) ¹³applies to client securities and collateral received or held by an ~~exempt person~~registered institution only if the client securities and collateral were received or held by the ~~exempt person~~registered institution in the course of the business which constitutes any regulated activity for which the ~~exempt person is exempt~~registered institution is registered;
- (b) applies to client securities and collateral received or held by an associated entity that is an authorized financial institution only if the client securities and collateral were received or

held by the associated entity in the course of its business of receiving or holding client securities and collateral of the intermediary of which the associated entity is an associated entity.

**145. Client money held by licensed corporations
and their associated entities**

(1) The Commission may make rules requiring licensed corporations and their associated entities to treat and deal with client money of the licensed corporations in such manner as is specified in the rules.

(2) Without limiting the generality of subsection (1) and without prejudice to section ~~384(9)~~384A(7) and ~~(108)~~^{*}, the Commission may in the rules referred to in subsection (1) -

- (a) require client money of licensed corporations or any part thereof to be paid into segregated accounts established for client money and designated as trust accounts or client accounts;
- (b) specify when and how the client money or any part thereof is to be paid into such accounts and require it to be dealt with, and accounted for, in the specified manner;
- (c) specify the amount or proportion of the client money that is not to be paid into such accounts, and the

deductions that may be made before the client money is paid into such accounts;

- (d) specify the circumstances in which the client money may be paid out of such accounts, including the circumstances in which the client money that is the subject of a lawful claim or lien may be paid out of such accounts;
- (e) require interest accruing from the holding of the client money in such accounts to be dealt with and paid in the specified manner;
- (f) specify the persons in Hong Kong with whom such accounts are to be established and maintained;
- (g) provide for authorization by the Commission as a condition for payment out of such accounts in specified circumstances;
- (h) require the maintenance of records in relation to such accounts (including records of performance of reconciliations of payments of the client money into and out of such accounts) in the specified manner;
- (i) require the submission to the Commission, upon request or at specified intervals, of specified information, records and documents for the purpose of enabling the Commission to ascertain readily whether the rules are being complied with;

- (j) require specified matters, and the circumstances relevant thereto, to be notified to the clients of licensed corporations or the Commission, or both;
- (k) require a person who becomes aware that he does not comply with any specified provision of the rules that applies to him to notify the Commission of that fact and of any further specified information, within the specified time;
- (l) provide for any other matter relating to the client money.

(3) Except as provided in the rules made under this section, client money of a licensed corporation is not liable to be taken in execution against the licensed corporation or an associated entity of the licensed corporation under the order or process of a court.

(4) Rules made under this section may provide that a licensed corporation, or an associated entity of a licensed corporation, which, without reasonable excuse,¹⁵ contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$200,000 and a term of imprisonment of 2 years;

¹⁵ As we have undertaken at the Bills Committee meeting on 2 March 2001, we propose the amendment such that non-compliance with specified requirements of the Client Money Rules would not be a strict liability offence. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

(b) on summary conviction a fine at level 6 and a term of imprisonment of 6 months.

(5) Rules made under this section may provide that a licensed corporation, or an associated entity of a licensed corporation, which, with intent to defraud, contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

(a) on conviction on indictment a fine of \$1,000,000 and a term of imprisonment of 7 years;

(b) on summary conviction a fine of \$500,000 and a term of imprisonment of 1 year.

⁶(5A) A person is not excused from complying with a requirement in any rules made pursuant to subsection (2)(k) to give notification to the Commission only on the ground that to do so might tend to incriminate the person.

(6) Notwithstanding anything in this section, no rules made under this section shall apply to associated entities that are authorized financial institutions.

(7) Notwithstanding anything in subsection (3), that subsection does not ~~apply to prevent~~ client money of a licensed corporation that is received or held by an associated entity that is an

authorized financial institution- from being taken in execution against the associated entity.¹⁶

146. Claims and liens not affected

Nothing in sections 144 and 145 and any rules made under any of those sections shall be construed as taking away or affecting a lawful claim or lien which any person has in respect of client assets of an intermediary (whether received or held by the intermediary or an associated entity of the intermediary), but the existence of any such claim or lien does not relieve the intermediary or an associated entity of the intermediary of the duty to comply with the requirements of those rules that apply to the intermediary or the associated entity (as the case may be).

Division 4 - Records

147 Keeping of accounts and records by intermediaries and their associated entities

(1) The Commission may make rules to provide for -

¹⁶ Client money placed with an authorized financial institution is fungible and indeed becomes the assets of the institution, which itself is subject to the prudential supervision by the HKMA under the Banking Ordinance. For this reason, client money held by the institution as an associated entity of a licensed corporation is to be liable to be taken against the institution. The original intention of clause 145(7) is to reflect this. However, as pointed out by the Legal Service Division of the Legislative Council, clause 145(7) as drafted in the Blue Bill has the effect of having the client money held by the institution as an associated entity of a licensed corporation being liable to be taken in execution not only against the institution, but also the licensed corporation. We propose the amendment to accordingly refine the scope. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

- (a) the keeping by intermediaries of such accounts and records as are specified in the rules;
- (b) the keeping by associated entities of intermediaries of such accounts and records in respect of client assets of the intermediaries that they receive or hold as are specified in the rules.

(2) Without limiting the generality of subsection (1) and without prejudice to section ~~384(9)~~384A(7) and ~~(108)~~^{*}, the Commission may in the rules referred to in subsection (1) -

- (a) require intermediaries and their associated entities to keep the specified accounts and records for specified purposes;
- (b) provide for the manner in which the accounts and records are to be kept;
- (c) provide for the period for which, and the location at which, the accounts and records are to be kept before they may be destroyed;
- (d) require a person who becomes aware that he does not comply with any specified provision of the rules that applies to him to notify the Commission of that fact and of any further specified information, within the specified time;

- (e) provide for any other matter relating to accounts and records to be kept, whether by intermediaries ~~and/or~~¹⁷ their associated entities.

(3) An entry in the accounts or records of an intermediary or an associated entity of an intermediary shall, ~~unless there is in the absence of~~ evidence to the contrary, be deemed to have been made by ~~it or with its authority.~~
or with the authority of the intermediary or the associated entity (as the case may be)¹⁸.

(4) A person who, with intent to defraud -

- (a) enters, records or stores, or causes to be entered, recorded or stored, in any accounts or records kept in compliance with, or in purported compliance with, rules made under this section, any matter which he knows to be false or misleading in a material particular;
- (b) deletes, destroys, removes or falsifies, or causes to be deleted, destroyed, removed or falsified, any matter that has been entered, recorded or stored in any accounts or records kept in compliance with, or in purported compliance with, rules made under this section; or

¹⁷ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

¹⁸ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

- (c) fails to enter, record or store in any accounts or records kept in compliance with, or in purported compliance with, rules made under this section, as soon as reasonably practicable, any matter that should be so entered, recorded or stored,

commits an offence and is liable -

- (i) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 7 years; or
- (ii) on summary conviction to a fine of 500,000 and to imprisonment for 1 year.

(5) Rules made under this section may provide that an intermediary, or an associated entity of an intermediary, which, without reasonable excuse, contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$200,000 and a term of imprisonment of 2 years;
- (b) on summary conviction a fine at level 6 and a term of imprisonment of 6 months.

(6) Rules made under this section may provide that an intermediary, or an associated entity of an intermediary, which, with intent to defraud, contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$1,000,000 and a term of imprisonment of 7 years;

(b) on summary conviction a fine of \$500,000 and a term of imprisonment of 1 year.

⁶(6A) A person is not excused from complying with a requirement in any rules made pursuant to subsection (2)(d) to give notification to the Commission only on the ground that to do so might tend to incriminate the person.

_____(7) Notwithstanding anything in this section, the power of the Commission to make rules under this section in respect of intermediaries shall, where the intermediaries are ~~exempt person registered institutions~~¹³, be regarded as the power to make rules in respect of the intermediaries only in relation to accounts and records relating to the businesses which constitute ~~the any~~¹⁹ regulated activities for which they are ~~exempt as exempt persons~~¹³ registered¹³.

148 Provision of contract notes, receipts, statements of account and notifications by intermediaries and their associated entities

(1) The Commission may make rules to provide for -

(a) the preparation by intermediaries of such contract notes, receipts, statements of account and notifications as are specified in the rules, and the provision thereof to clients of the intermediaries;

¹⁹ Technical amendment for consistency. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

- (b) the preparation by associated entities of intermediaries, in respect of client assets of the intermediaries that they receive or hold, of such receipts, statements of account and notifications as are specified in the rules, and the provision thereof to clients of the intermediaries.

(2) Without limiting the generality of subsection (1) and without prejudice to section ~~384(9)~~384A(7) and ~~(108)~~^{*}, the Commission may in the rules referred to in subsection (1) -

- (a) require intermediaries, in relation to all transactions they enter into, over any specified period of time, with or on behalf of a client of the intermediaries in the conduct of any of the businesses which constitute ~~the~~any²⁰ regulated activities for which they are licensed or ~~exempt~~registered¹³, to prepare and provide to the client a contract note and, where applicable, a statement of account in the specified manner and circumstances;
- (b) require intermediaries and their associated entities, in relation to every client of the intermediaries to whom they intermediaries²¹ have

²⁰ Technical amendment for consistency. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

²¹ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

provided financial accommodation, to prepare and provide to the client a statement of account in the specified manner and circumstances;

- (c) require intermediaries and their associated entities, in relation to every receipt of client assets from or for the account of a client of the intermediaries, to prepare and provide to the client a receipt in the specified manner and circumstances;
- (d) require intermediaries and their associated entities, in relation to every notification which relates to client assets received or held by them intermediaries or the associated entities (as the case may be)²² on behalf of a client of the intermediaries, and which is received from any person other than the client (including any notification concerning any entitlement relating to client assets), to prepare and provide to the client a notification in the specified manner and circumstances;
- (e) provide for the time when contract notes, receipts, statements of account and notifications are to be provided and the period for which, and the location

²² Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

at which, copies thereof are to be kept before they may be destroyed;

- (f) require a person who becomes aware that he does not comply with any specified provision of the rules that applies to him to notify the Commission of that fact and of any further specified information, within the specified time;
- (g) provide for any other matter relating to contract notes, receipts, statements of account and notifications to be prepared and provided to clients of intermediaries, whether by the intermediaries ~~and~~²³ their associated entities.

(3) Rules made under this section may provide that an intermediary, or an associated entity of an intermediary, which, without reasonable excuse, contravenes any specified provision of the rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$200,000 and a term of imprisonment of 2 years;
- (b) on summary conviction a fine at level 6 and a term of imprisonment of 6 months.

(4) Rules made under this section may provide that an intermediary, or an associated entity of an intermediary, which, with intent to defraud, contravenes any specified provision of the

²³ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

rules that applies to it commits an offence and is liable to a specified penalty not exceeding -

- (a) on conviction on indictment a fine of \$1,000,000 and a term of imprisonment of 7 years;
- (b) on summary conviction a fine of \$500,000 and a term of imprisonment of 1 year.

⁶(4A) A person is not excused from complying with a requirement in any rules made pursuant to subsection (2)(f) to give notification to the Commission only on the ground that to do so might tend to incriminate the person.

—(5) Notwithstanding anything in this section, the power of the Commission to make rules under this section in respect of intermediaries shall, where the intermediaries are ~~exempt persons registered institutions~~¹³, be regarded as the power to make rules in respect of the intermediaries only in relation to contract notes, receipts, statements of account and notifications relating to the businesses which constitute ~~the~~any²⁴ regulated activities for which they are ~~exempt as exempt persons registered~~¹³.

Division 5 - Audit²⁵

²⁴ Technical amendment for consistency. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

²⁵ We note a gap in the Blue Bill whereby an associated entity of a registered institution (formerly “exempt person”), which is not itself an authorized financial institution, is not required to comply with any audit related requirement under either the SF Bill or the Banking Ordinance. The amendments to replace “a licensed corporation” with “an intermediary” in various provisions under Division 5 seek to close such a gap.

**149 Auditor to be appointed by licensed corporations
and ~~their~~ associated entities of intermediaries**

(1) A licensed corporation shall appoint an auditor to perform the functions required of an auditor of the corporation under or pursuant to the provisions of this or any other Ordinance.

(2) An associated entity of a ~~licensed corporation~~ an intermediary shall appoint an auditor to perform the functions required of an auditor of the associated entity under or pursuant to the provisions of this or any other Ordinance.

(3) A licensed corporation, and an associated entity of a ~~licensed corporation~~ an intermediary, shall, within 7 business days after its appointment of an auditor under subsection (1) or (2) (as the case may be), notify the Commission by notice in writing of the name and address of the auditor.

(4) A person -

(a) is not eligible for appointment as an auditor under subsection (1) or (2) -

(i) if he is an officer or employee of the licensed corporation or the associated entity the accounts of which are to be audited, or is in the employment of such an officer or employee; or

(ii) if he ~~does not belong~~belongs²⁶ to a class of persons prescribed by rules made under section 384 for the purposes of this subsection;

(b) is, subject to paragraph (a), eligible for appointment as an auditor under subsection (1) or (2), notwithstanding that he is, apart from that appointment, already an auditor appointed by the licensed corporation or the associated entity the accounts of which are to be audited, whether for the purposes of the Companies Ordinance (Cap. 32) or otherwise.

(5) A licensed corporation, or an associated entity of a ~~licensed corporation~~an intermediary, which fails to appoint an auditor in accordance with subsection (1) or (2) within one month after -

- (a) it becomes licensed or becomes such an associated entity (as the case may be); or
- (b) the auditor first appointed under subsection (1) or (2) after it becomes licensed or becomes such an associated entity, or any auditor further appointed under subsection (1) or (2), ceases to

²⁶ We propose the amendment to reflect the policy intention that the SFC may make rules to prescribe a person as **not** being eligible for appointment as an auditor under this clause. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

be an auditor of the licensed corporation or of the associated entity (as the case may be),
commits an offence and is liable -

- (i) on conviction on indictment to a fine of \$200,000 and to imprisonment for 1 year; or
- (ii) on summary conviction to a fine at level 5 and to imprisonment for 6 months.

(6) A licensed corporation, or an associated entity of a ~~licensed corporation~~ an intermediary, which contravenes subsection (3) commits an offence and is liable on conviction to a fine at level 5.

(7) Nothing in this section prejudices the operation of any other requirements relating to the appointment of an auditor, whether under the Companies Ordinance (Cap. 32) or otherwise.

(8) In this section, a reference to an associated entity of a ~~licensed corporation~~ an intermediary shall be construed as a reference to such associated entity other than one that is an authorized financial institution.

**150 Notification of proposed change of
auditors by licensed corporations
and ~~their~~ associated entities of intermediaries**

(1) A licensed corporation, and an associated entity of a ~~licensed corporation~~ an intermediary, shall within one business day after -

- (a) it gives notice to its members of a motion, to be moved at its general meeting -
 - (i) to remove an auditor appointed by it under section 149 before the expiration of his term of office; or
 - (ii) to replace with another auditor, or not to reappoint, an auditor appointed by it under section 149 at the expiration of his term of office; or
- (b) an auditor appointed by it under section 149 ceases to be its auditor before the expiration of his term of office, otherwise than in consequence of a motion referred to in paragraph (a),

notify the Commission by notice in writing of that fact.

(2) A licensed corporation, or an associated entity of ~~a licensed corporation~~ an intermediary, which contravenes subsection (1) commits an offence and is liable on conviction to a fine at level 5.

(3) In this section, a reference to an associated entity of a ~~licensed corporation~~ an intermediary shall be construed as a reference to such associated entity other than one that is an authorized financial institution.

**151 Notification of end of financial year by
licensed corporations and ~~their~~
associated entities of intermediaries, etc**

(1) A licensed corporation, and an associated entity of a ~~licensed corporation an intermediary~~, shall -

- (a) in the case of the licensed corporation, within one month after it becomes licensed; or
- (b) in the case of the associated entity, within one month after it becomes such an associated entity,

notify the Commission by notice in writing of the date on which its financial year ends.

(2) A licensed corporation, and an associated entity of a ~~licensed corporation an intermediary~~, shall not -

- (a) except with the approval in writing of the Commission under subsection (3)(a), alter the date notified to the Commission under subsection (1) as the date on which its financial year ends;
- (b) except with the approval in writing of the Commission under subsection (3)(b), adopt any period which exceeds 12 months as its financial year.

(3) On an application in writing by a licensed corporation or an associated entity of a ~~licensed corporation an intermediary~~, the Commission may, subject to such conditions as it considers appropriate, grant approval in writing in respect of -

- (a) an alteration of the date notified to the Commission under subsection (1) as the date on which its financial year ends;

(b) the adoption of any period which exceeds 12 months as its financial year.

(4) A licensed corporation, or an associated entity of a ~~licensed corporation~~ an intermediary, which contravenes subsection (1) or (2), or a condition imposed pursuant to subsection (3), commits an offence and is liable on conviction to a fine at level 5.

(5) Nothing in this section prejudices the operation of section 122 of the Companies Ordinance (Cap. 32).

(6) In this section, a reference to an associated entity of a ~~licensed corporation~~ an intermediary shall be construed as a reference to such associated entity other than one that is an authorized financial institution.

152 Audited accounts, etc. to be submitted by licensed corporations and ~~their associated entities~~ of intermediaries

(1) Subject to subsections (3) and (4), a licensed corporation, and an associated entity of a ~~licensed corporation,~~ an intermediary, shall -

(a) prepare such financial statements and other documents, for such periods, as are prescribed by rules made under section 384 for the purposes of this section; and

(b) submit the financial statements and other documents, together with an auditor's report, to the Commission not later than 4 months after the end of the financial year to which they relate.

(2) Subject to subsections (3) and (4), a licensed corporation that ceases, in such circumstances as are prescribed by rules made under section 384 for the purposes of this section, carrying on ~~any~~ all²⁷ of the regulated activities for which it is licensed, and an associated entity of ~~a licensed corporation~~ an intermediary that ceases to be such an associated entity, shall -

- (a) prepare such financial statements and other documents, which shall be made up to (and including) the date of the cessation, as are prescribed by the rules; and
- (b) submit the financial statements and other documents, together with an auditor's report, to the Commission not later than 4 months after the date of the cessation.

(3) Without limiting the generality of subsection (1) or (2), the requirements under such subsection relating to the financial statements and other documents, and the auditor's report, referred to in such subsection include the requirements that -

- (a) the financial statements and other documents are to relate to such matters and contain such particulars as are prescribed by rules made under section 384 for the purposes of this section;

²⁷ **Technical amendment to make clear that the requirement is applicable only when the licensed corporation ceases the conduct of all the regulated activities it has been licensed for.**

- (b) the auditor's report is to contain such particulars, including such statement of opinion, as are prescribed by the rules;
- (c) the financial statements and other documents, and the auditor's report, are to be prepared in accordance with such principles or bases as are prescribed by the rules; and
- (d) without limiting the generality of section 129B of the Companies Ordinance (Cap. 32), the financial statements and other documents are to be signed by such person as is prescribed by the rules.

(4) On an application in writing by the licensed corporation or the associated entity by which any financial statements and other documents, and any auditor's report, are required under subsection (1) or (2) to be submitted, the Commission may, where it is satisfied that there are special reasons for so doing, extend the period within which the financial statements and other documents, and the auditor's report, are required to be submitted, for such period and subject to such conditions as the Commission considers appropriate, and upon the Commission granting the extension, subsection (1) or (2) (as the case may be) shall apply subject to the extension accordingly.

(5) A licensed corporation, or an associated entity of ~~a licensed corporation~~ an intermediary, which, without reasonable excuse, contravenes subsection (1) or (2), or a condition imposed pursuant to subsection (4), commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$200,000 and to imprisonment for 1 year; or
- (b) on summary conviction to a fine at level 5 and to imprisonment for 6 months.

(6) A licensed corporation, or an associated entity of a ~~licensed corporation~~ an intermediary, which, with intent to defraud, contravenes subsection (1) or (2), or a condition imposed pursuant to subsection (4), commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 7 years; or
- (b) on summary conviction to a fine of \$500,000 and to imprisonment for 1 year.

(7) In this section, a reference to an associated entity of a ~~licensed corporation~~ an intermediary shall be construed as a reference to such associated entity other than one that is an authorized financial institution.

153 Auditors of licensed corporations or ~~their~~ associated entities of intermediaries to lodge report with Commission, etc. in certain cases

- (1) If a person -
 - (a) in the course of performing his functions as an auditor appointed under section 149 by a licensed corporation or an associated entity of a ~~licensed corporation~~ an intermediary or, where an associated entity of a ~~licensed corporation~~ an intermediary

is an authorized financial institution, as an auditor appointed for the purposes of the Banking Ordinance (Cap. 155) by the associated entity, becomes aware of a reportable matter; or

- (b) in the course of performing his functions as an auditor appointed under section 149 by a licensed corporation or an associated entity of ~~a licensed corporation~~ an intermediary, proposes to include any qualification or adverse statement in any report prepared by him on the financial statements or other documents of the licensed corporation or the associated entity (as the case may be) which are required to be submitted to the Commission under section 152,

he shall -

- (i) in the case of paragraph (a), as soon as reasonably practicable after he becomes aware of the reportable matter, lodge with -
 - (A) in the case of an auditor appointed under section 149 by a licensed corporation or an associated entity of ~~a licensed corporation~~ an intermediary, the Commission; or
 - (B) in the case of an auditor appointed for the purposes of the Banking Ordinance (Cap. 155) by an associated entity of ~~a licensed~~

~~corporation an intermediary~~, the Commission
and the Monetary Authority,

a written report on the reportable matter;

- (ii) in the case of paragraph (b), as soon as reasonably practicable after he first proposes the inclusion of the qualification or adverse statement, lodge with the Commission a written report on the qualification or adverse statement.

(2) If a person appointed as an auditor under section 149 by a licensed corporation or an associated entity of ~~a licensed corporation an intermediary~~ -

- (a) resigns as an auditor of the licensed corporation or the associated entity (as the case may be) before the expiration of his term of office as such auditor;
- (b) does not seek reappointment as an auditor of the licensed corporation or the associated entity (as the case may be) at the expiration of his term of office as such auditor; or
- (c) otherwise ceases to be an auditor of the licensed corporation or the associated entity (as the case may be),

he shall within one business day thereafter notify the Commission by notice in writing of that fact, and in the notice state the reasons therefor, and give particulars of any connected circumstances which he considers should be brought to the attention of the Commission

or, where no such circumstances exist, make a statement to that effect.

(3) In this section -

"prescribed requirement" (訂明規定) means-

~~(a) any of the requirements under section 144(3) or 145(3);²⁸~~

~~(b) such of the requirements under any of the rules made under section 144, 145, 147 or 148 as are prescribed by rules made under section 384 for the purposes of this definition;~~

"reportable matter" (須報告事項), in relation to a person acting as an auditor within the meaning of subsection (1)(a), means a matter that, in the opinion of the person -

(a) in the case of a licensed corporation -

(i) constitutes on the part of the licensed corporation or any of its associated entities a failure to comply with any prescribed requirement;

(ii) adversely affects to a material extent the financial position of the licensed corporation or any of its associated entities; or

²⁸ We propose the amendment as clauses 144(3) and 145(3) are not relevant for the purpose of reporting by an auditor of a licensed corporation or its associated entity - they are not requirements imposed on a licensed corporation or its associated entity in the first place. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

- (iii) constitutes on the part of the licensed corporation a failure to comply with section 142 or with all or any of the requirements of the financial resources rules that apply to it; or
- (b) in the case of an associated entity of ~~a licensed corporation~~ an intermediary -
 - (i) constitutes on the part of the associated entity a failure to comply with any prescribed requirement; or
 - (ii) where the associated entity is not an authorized financial institution, adversely affects to a material extent the financial position of the associated entity.

154 Immunity in respect of communication with Commission, etc. by auditors of licensed corporations or ~~their associated entities of intermediaries~~

(1) Without prejudice to sections 368 and 369, no duty which a person may be subject to as an auditor appointed under section 149 by a licensed corporation or an associated entity of ~~a licensed corporation~~ an intermediary or, where an associated entity of a ~~licensed corporation~~ an intermediary is an authorized financial

institution, as an auditor appointed for the purposes of the Banking Ordinance (Cap. 155) by the associated entity shall be regarded as contravened by reason of his communicating in good faith to the Commission or the Monetary Authority, whether or not in response to a request made by the Commission or the Monetary Authority (as the case may be), any information or opinion on a matter which -

- (a) he becomes aware of in his capacity as such auditor (whether or not in the course of performing his functions as such auditor); and
- (b) is relevant to any function of the Commission or the Monetary Authority (as the case may be).

(2) In addition to applying to a person who is an auditor appointed under section 149 by a licensed corporation or an associated entity of ~~a licensed corporation~~ an intermediary, or appointed for the purposes of the Banking Ordinance (Cap. 155) by an associated entity of ~~a licensed corporation~~ an intermediary, subsection (1) also applies to -

- (a) a person whose appointment as an auditor appointed under section 149 by a licensed corporation or an associated entity of ~~a licensed corporation~~ an intermediary, or appointed for the purposes of the Banking Ordinance (Cap. 155) by an associated entity of ~~a licensed corporation~~ an intermediary, has ceased, in which case a reference to a matter in that subsection shall be construed on the basis that ~~it refers to any matter~~ paragraph (a) of that

subsection requires the matter to be one²⁹ which he becomes aware of in his capacity as such auditor (whether or not in the course of performing his functions as such auditor) before the appointment has ceased;~~and~~

(b) an auditor appointed, whether or not under section 149 or for the purposes of the Banking Ordinance (Cap. 155), by a former licensed corporation or by a former associated entity of ~~a licensed corporation~~ an intermediary, in which case a reference to a matter in that subsection shall be construed on the basis that ~~it refers to any matter~~ paragraph (a) of that subsection requires the matter to be one³⁰ which he becomes aware of in his capacity as such auditor (whether or not in the course of performing his functions as such auditor); ~~and~~

(c) ³¹a person whose appointment as an auditor, whether or not under section 149 or for the purposes of the Banking Ordinance (Cap. 155), by a former licensed

²⁹ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

³⁰ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

³¹ We propose the amendment to cover the scenario whereby a person whose appointment as an auditor of a former licensed corporation or a former associated entity of a licensed corporation has ceased. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

corporation or by a former associated entity of an intermediary, has ceased, in which case a reference to a matter in that subsection shall be construed on the basis that paragraph (a) of that subsection requires the matter to be one which he becomes aware of in his capacity as such auditor (whether or not in the course of performing his functions as such auditor) before the appointment has ceased.

(3) In this section -

"former associated entity of a ~~licensed corporation~~" (持牌法團的 ~~an intermediary~~) (前有聯繫實體) means a corporation which was formerly an associated entity of a ~~licensed corporation an intermediary~~;

"former licensed corporation" (前持牌法團) means a corporation which was formerly a licensed corporation.

155 Power of Commission to appoint auditors for licensed corporations and their associated entities

(1) Subject to subsection (3), where -

(a) a licensed corporation has failed to satisfy the Commission in accordance with section 143 that it complies with all of the requirements of the financial resources rules that apply to it;

- (b) the Commission has reasonable cause to believe that a licensed corporation or any of its associated entities has failed to comply with any prescribed requirement;
- (c) the Commission has reasonable cause to believe that a licensed corporation or any of its associated entities has failed to submit any financial statements or other documents in accordance with section 152; or
- (d) the Commission has received a written report lodged by a person under section 153 in relation to a licensed corporation or any of its associated entities,

the Commission may appoint an auditor to examine and audit, either generally or in respect of any particular matter, the accounts and records of the licensed corporation and any of its associated entities (including records of transactions entered into by the licensed corporation with any other person and of client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be)), and, without prejudice to section 157, to report to the Commission on such matters as the Commission may direct.

(2) Where an auditor is appointed under subsection (1) to examine and audit the accounts and records of a licensed corporation and any of its associated entities, the auditor may, for the purpose of carrying out the examination and audit, examine any client assets

of the licensed corporation³² received or held by the licensed corporation or the associated entity (as the case may be).

(3) The Commission shall not appoint an auditor under subsection (1) to examine and audit the accounts and records of an associated entity that is an authorized financial institution unless the Commission has first consulted the Monetary Authority in respect of the appointment and of the scope of the examination and audit to be carried out by the auditor.

(4) ~~Subject to subsection (4A)~~³³, where an auditor appointed under subsection (1) has examined and audited the accounts and records of a licensed corporation or an associated entity of a licensed corporation, the Commission may, where it is of the opinion that it is appropriate to do so having regard to the conduct (whether before or after the appointment) of the licensed corporation or the associated entity (as the case may be), by notice in writing direct the licensed corporation or the associated entity (as the case may be) to pay a specified amount, being the whole or a part of the costs and expenses of the examination and audit, within the specified time and in the specified manner.

³³(4A) The Commission shall not give a direction under subsection (4) unless it has given the licensed corporation or the associated entity to which the direction is to be given a reasonable

³² Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

³³ We propose the amendment to include a procedural safeguard that requires the SFC to give the concerned licensed corporation or associated entity a reasonable opportunity of being heard before it can order the corporation to bear any audit cost incurred under this clause.

opportunity of being heard.

(5) Where a licensed corporation or an associated entity of a licensed corporation fails to comply with a direction of the Commission under subsection (4), the Commission may recover the specified amount referred to in the direction as a civil debt due to it.

(6) In this section, "prescribed requirement" (訂明規定) means—

~~(a) any of the requirements under section 144(3) or 145(3);³⁴~~

~~(b)~~—such of the requirements under any of the rules made under section 144, 145, 147 or 148 as are prescribed by rules made under section 384 for the purposes of this definition.

156 Power of Commission to appoint auditors for licensed corporations and their associated entities on application

³⁵(1) Subject to subsections (3) to (6), on an application in writing by a person who alleges that a licensed corporation or any of its associated entities —

(a) has failed to account to the person as a client of the licensed corporation for any client assets held

³⁴ We propose the amendment as clauses 144(3) and 145(3) are not relevant for the purpose of reporting by an auditor of a licensed corporation or its associated entity - they are not requirements imposed on a licensed corporation or its associated entity in the first place. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

³⁵ Technical amendment for greater clarity. **Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.**

on behalf of the person by the licensed corporation or the associated entity (as the case may be); or
(b) has failed to act in accordance with instructions given by the person as a client of the licensed corporation to the licensed corporation or the associated entity (as the case may be), and has failed -

(i) to account to the person for any profit that may have been secured or increased by the person had the instructions been followed; or

(ii) to compensate the person for any loss that may have been avoided or reduced by the person had the instructions been followed,

the Commission may appoint an auditor to examine and audit, either generally or in respect of any particular matter, the accounts and records of the licensed corporation and any of its associated entities (including records of transactions entered into by the licensed corporation with any other person and of client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be)), and, without prejudice to section 157, to report to the Commission on such matters as the Commission may direct.

(2) Where an auditor is appointed under subsection (1) to examine and audit the accounts and records of a licensed corporation and

any of its associated entities, the auditor may, for the purpose of carrying out the examination and audit, examine any client assets of the licensed corporation³⁶ received or held by the licensed corporation or the associated entity (as the case may be).

(3) A person making an application pursuant to subsection (1) shall state in the application -

(a) the particulars of the circumstances in which any licensed corporation or any associated entity of a licensed corporation is alleged to have failed to account for any client assets, or to act in accordance with instructions given to the licensed corporation or the associated entity and to account for any profit or compensate for any loss (as the case may be);

(b) the particulars of any client assets concerned;

(c) the particulars of the transactions in respect of which the alleged failure has occurred; and

(d) any other particulars the Commission may require, and shall verify all statements in the application by statutory declaration, which may be taken by any person authorized by the Commission in that behalf.

(4) The Commission shall not appoint an auditor under subsection (1) unless it is satisfied that -

³⁶ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 16 July 2001.

- (a) the person making the application pursuant to that subsection has a good reason for making the application; and
- (b) it is in the interest of -
 - (i) the licensed corporation and the associated entity the accounts and records of which are to be examined and audited by the auditor;
 - (ii) the person making the application; or
 - (iii) the investing public or the public,that the auditor be appointed.

(5) The Commission shall not appoint an auditor under subsection (1) to examine and audit the accounts and records of an associated entity that is an authorized financial institution unless the Commission has first consulted the Monetary Authority in respect of the appointment and of the scope of the examination and audit to be carried out by the auditor.

(6) The Commission shall not appoint an auditor under subsection (1) to examine and audit the accounts and records of a licensed corporation or an associated entity of a licensed corporation unless the Commission has given the licensed corporation or the associated entity (as the case may be) a reasonable opportunity of being heard.

(7) For the purposes of the law of defamation, every statement in an application made pursuant to subsection (1) shall, if made in good faith and without malice, be privileged.

(8) ~~W~~Subject to subsection (8A)³⁷, where an auditor appointed under subsection (1) has examined and audited the accounts and records of a licensed corporation or an associated entity of a licensed corporation, the Commission may, where it is of the opinion that it is appropriate to do so having regard to the conduct (whether before or after the appointment) of the licensed corporation or the associated entity (as the case may be) and of the person making the application pursuant to that subsection in respect of the appointment, by notice in writing direct the licensed corporation or the associated entity (as the case may be) or the person making the application to pay a specified amount, being =

³⁸(a) in the case of the licensed corporation or the associated entity (as the case may be), the whole or a part of the costs and expenses of the examination and audit, or

³⁸(b) in the case of the person making the application, the whole or a part of the costs and expenses of the examination and audit to the extent that they have been reasonably incurred for the purpose of ascertaining matters to which the application relates,

³⁷ See Footnote 39.

³⁸ **At the Bills Committee meeting on 16 July 2001, some Members expressed concern that a client making an application for an audit of a licensed corporation out of his perceived misconduct of the latter in its dealings with him, may be required to pay an overly large amount of audit cost incurred for a wider purpose (such as whether the corporation has put in place a proper operating system). We accept the comment and propose an amendment to limit the audit costs payable by the client to those incurred in relation to his application.**

within the specified time and in the specified manner.

³⁹(8A) The Commission shall not give a direction under subsection (8) unless it has given the licensed corporation, the associated entity or the person to which or to whom the direction is to be given a reasonable opportunity of being heard.

(9) Where a licensed corporation, an associated entity of a licensed corporation or a person making an application pursuant to subsection (1) fails to comply with a direction of the Commission under subsection (8), the Commission may recover the specified amount referred to in the direction as a civil debt due to it.

157 ⁴⁰Auditors appointed under section 155

or 156 to report to Commission

(1) An auditor appointed under section 155 or 156 shall make such interim reports to the Commission as it may require and shall, on the conclusion of the examination and audit which he is appointed to carry out, make a final report to the Commission.

(2) A report referred to in subsection (1) shall be made within such time and in such manner as the Commission may direct.

(3) The Commission may, if it considers appropriate, forward a copy of any report made to it under subsection (1) to the licensed

³⁹ We propose the amendment to include a procedural safeguard that requires the SFC to give the concerned licensed corporation or associated entity or client an opportunity of being heard before it can order the corporation to bear any audit cost incurred under this provision.

⁴⁰ We propose the amendments primarily to ensure that the SFC has the vires to pass the auditors' report to the concerned licensed corporation or associated entity, as the case may be. **Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.**

corporation or the associated entity the accounts and records of which are the subject of the examination and audit referred to in the report.

158 Powers of auditors appointed under section 155 or 156

(1) An auditor appointed under section 155 or 156 to examine and audit the accounts and records of any licensed corporation and any of its associated entities, for the purpose of carrying out the examination and audit, may, in addition to any other action that the auditor may reasonably take for the purpose -

- (a) examine on oath, ~~affirmation~~⁴¹ or otherwise -
 - (i) any officer, employee and agent of the licensed corporation or the associated entity (as the case may be); and
 - (ii) any auditor appointed by the licensed corporation or the associated entity (as the case may be) under section 149 or, where the associated entity is an authorized financial institution, for the purposes of the Banking Ordinance (Cap. 155),

⁴¹ "Oath" is already defined in section 3 of the Interpretation and General Clauses Ordinance (Cap.1) to cover "affirmation". **Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.**

in respect of any matter relating to the business of the licensed corporation or the associated entity (as the case may be) or to the client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be) and, for that purpose, administer oaths~~and affirmations~~ accordingly;

(b) require any officer, employee and agent of the licensed corporation or the associated entity (as the case may be) to -

(i) produce any accounts and records concerning any matter relating to the business of the licensed corporation or the associated entity (as the case may be) or to the client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be); and

(ii) explain the contents of the accounts and records so produced;

(c) require any auditor appointed by the licensed corporation or the associated entity (as the case may be) under section 149 or, where the associated entity is an authorized financial institution, for

the purposes of the Banking Ordinance (Cap. 155)
to -

- (i) produce any accounts and records held by him concerning any matter relating to the business of the licensed corporation or the associated entity (as the case may be) or to the client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be);
and
 - (ii) explain the contents of the accounts and records so produced;
- (d) require a recognized exchange company or recognized clearing house to -
- (i) produce any accounts and records kept by it, or information in its possession, concerning any matter relating to the business of the licensed corporation or the associated entity (as the case may be) or to the client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be);
and

- (ii) explain the contents of the accounts and records, and the information, so produced;
- (e) require any person receiving or holding client assets of the licensed corporation⁴² on behalf of the licensed corporation or the associated entity (as the case may be) to -
 - (i) produce any accounts and records kept by the person, or information in his possession, concerning any matter relating to the client assets; and
 - (ii) explain the contents of the accounts and records, and the information, so produced;
- (f) employ any person he considers necessary to assist him in carrying out the examination and audit which he is appointed to carry out; and
- (g) for the purpose of the examination and audit which he is appointed to carry out, authorize in writing any person employed by him to do any act or thing referred to in this subsection ~~(other than the examination of~~ (except to examine a person on oath

⁴² Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.

~~affirmation under paragraph (a) or to exercise any power conferred by this paragraph~~⁴³.

(2) If an auditor appointed under section 155 or 156, or a person authorized under subsection (1)(g), reasonably considers it necessary for the purpose of carrying out the examination and audit of the accounts and records of a licensed corporation and any of its associated entities which the auditor is appointed to carry out, the powers referred to in subsection (1) -

(a) are exercisable in relation to any other business carried on by the licensed corporation in conjunction with any regulated activity for which it is licensed,~~and~~ and to⁴⁴ any business of any of its associated entities, in which case any reference to "any matter relating to the business of the licensed corporation or the associated entity (as the case may be)"⁴⁵ in subsection (1)(a) to (g) shall be construed on the basis that it refers to any matter relating to such other business carried on by the licensed corporation,~~and~~ or to⁴⁶

⁴³ We propose the amendment such that a person employed by an auditor for the purpose would not have the power to further delegate the works to other persons. Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.

⁴⁴ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.

⁴⁵ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.

⁴⁶ Technical amendment for greater clarity. Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.

such business of any of its associated entities;
and

(b) ⁴⁷are exercisable in relation to a related corporation of the licensed corporation or any of its associated entities, in which case -

(i) any reference to "any officer, employee and agent of the any officer, employee and agent of the licensed corporation or the associated entity (as the case may be)" in subsection (1)(a) to (g) shall be construed on the basis that it refers to ~~that of the related corporation or any of its associated entities;~~ to any officer, employee and agent of the related corporation;

(ii) any reference to "any auditor appointed by the licensed corporation or the associated entity (as the case may be) under section 149 or, where the associated entity is an authorized financial institution, for the purposes of the Banking Ordinance (Cap. 155)" in subsection (1)(a) to (g) shall be

⁴⁷ Mainly technical amendments for greater clarity and also to remove the inadvertent coverage of an associated entity of a related corporation of a licensed corporation, as pointed out by the Legal Service Division of the Legislative Council. **Members considered this amendment and did not propose further**

construed on the basis that it refers to any auditor appointed by the related corporation ~~or any of its associated entities~~, whether under this Ordinance or otherwise;

- (iii) any reference to "any matter relating to the business of the licensed corporation or the associated entity (as the case may be) or to the client assets of the licensed corporation received or held by the licensed corporation or the associated entity (as the case may be)" in subsection (1)(a) to (g) shall be construed on the basis that it refers, apart from the matter originally referred to, refers also to any matter relating to the business of the ~~related corporation or any of its associated entities~~ or to the ~~client assets of the related corporation received or held by the related corporation or any of its associated entities~~ corporation; and

(iv) any reference to "any person receiving or holding client assets of the licensed corporation on behalf of the licensed corporation or the associated entity (as the case may be)" in subsection (1)(a) to (g) shall be construed on the basis that it refers to any person receiving or holding client assets of the licensed corporation on behalf of the related corporation or any of its associated entities.

(3) A person who, without reasonable excuse, fails to comply with any requirement imposed on him (including the requirement to answer any question put to him) under this section (whether by an auditor appointed under section 155 or 156 or a person authorized under subsection (1)(g)) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$200,000 and to imprisonment for 1 year; or
- (b) on summary conviction to a fine at level 5 and to imprisonment for 6 months.

(4) A person who -

- (a) in purported compliance with a requirement imposed on him (including the requirement to answer any question put to him) under this section (whether by an auditor appointed under section 155 or 156 or a person authorized under subsection (1)(g)),

produces any accounts or records or gives an answer which is false or misleading in a material particular; and

- (b) knows that, or is reckless as to whether, the accounts or records or the answer is false or misleading in a material particular,

commits an offence and is liable -

- (i) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 2 years; or
- (ii) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

(5) A person who, with intent to defraud -

- (a) fails to comply with any requirement imposed on him (including the requirement to answer any question put to him) under this section (whether by an auditor appointed under section 155 or 156 or a person authorized under subsection (1)(g)); or
- (b) in purported compliance with a requirement imposed on him (including the requirement to answer any question put to him) under this section (whether by an auditor appointed under section 155 or 156 or a person authorized under subsection (1)(g)), produces any accounts or records or gives an answer which is false or misleading in a material particular,

commits an offence and is liable -

- (i) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 7 years; or
- (ii) on summary conviction to a fine of \$500,000 and to imprisonment for 1 year.

159 Offence to destroy, conceal, or alter accounts, records or documents, etc.

⁴⁸(1) A person commits an offence if he, with intent to prevent, delay or obstruct the carrying out of any examination and audit which an auditor appointed under this Part is required to carry out -

- (a) deletes, destroys, mutilates, falsifies, conceals, alters or otherwise makes unavailable any accounts, records or documents ~~concerning any matter relating to the business of a licensed corporation or any of its associated entities or to the client assets of a licensed corporation~~ related to such examination and audit, or aids or abets or conspires with another person to do so;
- (b) disposes or procures the disposal, in any manner and by any means, of any property ~~belonging to or in the possession of a licensed corporation or any of its associated entities~~ related to such

⁴⁸ To define the scope of the provision in terms of the scope of the relevant "examination and audit". **Members considered this amendment and did not propose further changes at the meeting on 17 July 2001.**

examination and audit, or aids or abets or conspires with another person to do so; or

(c) leaves, or attempts to leave, Hong Kong.

(2) A person who commits an offence under subsection (1) is liable -

(a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 7 years; or

(b) on summary conviction to a fine of \$500,000 and to imprisonment for 1 year.

(3) ⁴⁸If, in proceedings for an offence under subsection (1), it is proved that the accused person deleted, destroyed, mutilated, falsified, concealed or altered any accounts, records or documents ~~concerning any matter relating to the business of a licensed corporation or any of its associated entities or to the client assets of a licensed corporation~~ related to any examination and audit which an auditor appointed under this Part is required to carry out, or aided or abetted or conspired with another person to do so, he shall, in the absence of evidence to the contrary, be presumed to have done so with intent to prevent, delay or obstruct the carrying out of ~~any examination and audit which an auditor appointed under this Part is required to carry out~~ such examination and audit.

Division 6 - Miscellaneous

**160 Restriction on receiving or holding of
client assets**

(1) No person shall receive or hold in Hong Kong client assets of an intermediary unless the person is -

- (a) the intermediary;
- (b) an associated entity of the intermediary; or
- (c) an excluded person.

(2) A person who, without reasonable excuse, contravenes subsection (1) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$200,000 and to imprisonment for 2 years; or
- (b) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

(3) In this section, "excluded person" (豁除人士) means -

- (a) any authorized financial institution;
- (b) in the case of client collateral of any intermediary, any other intermediary or person with which or whom it is deposited, or to which or whom it is provided, in the circumstances referred to in paragraph (a)(A) or (B) or (b)(A) or (B) (as the case may be) of the definition of "securities collateral" or "other collateral" (as the case may be) in section 1 of Part 1 of Schedule 1;
- (c) any company or overseas company that is approved under rules made pursuant to section 144(2)(d) as being suitable for the safe custody of client securities and collateral of intermediaries; or

- (d) any person in Hong Kong that is specified under rules made pursuant to section 145(2)(f) as that with whom segregated accounts established for client money of licensed corporations and designated as trust accounts or client accounts are to be established and maintained.

161 Associated entities

(1) An associated entity of an intermediary shall within 7 business days after -

- (a) it becomes such an associated entity; or
- (b) it ceases to be such an associated entity,

notify the Commission by notice in writing of that fact and such other particulars as are prescribed by rules made under section 384 for the purposes of this section.

(2) Where there is any change in the particulars required to be provided by an associated entity of an intermediary under subsection (1), the associated entity shall within 7 business days thereafter notify the Commission by notice in writing of that fact and provide in the notice particulars of the change.

(3) Where an associated entity of an intermediary, other than an authorized financial institution, receives or holds client assets of the intermediary, the associated entity shall not, unless authorized in writing by the Commission, conduct any business other than that of receiving or holding client assets, whether on behalf of the intermediary or otherwise.

(4) An associated entity of an intermediary which, without reasonable excuse, contravenes subsection (1), (2) or (3) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$200,000 and to imprisonment for 2 years; or
- (b) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

(5) An associated entity of an intermediary which, with intent to defraud, contravenes subsection (1), (2) or (3) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$1,000,000 and to imprisonment for 7 years; or
- (b) on summary conviction to a fine of \$500,000 and to imprisonment for 1 year.

(6) An associated entity of an intermediary which becomes aware that it does not comply with subsection (1), (2) or (3) shall within one business day thereafter notify the Commission by notice in writing of that fact and of the surrounding circumstances.

(7) An associated entity of an intermediary which contravenes subsection (6) commits an offence and is liable -

- (a) on conviction on indictment to a fine of \$200,000 and to imprisonment for 2 years; or
- (b) on summary conviction to a fine at level 6 and to imprisonment for 6 months.

⁶(7A) An associated entity of an intermediary is not excused from complying with subsection (6) only on the ground that to do

so might tend to incriminate it.

(8) Notwithstanding anything in this section, the power of the Commission to make rules for the purposes of this section in respect of associated entities shall, where the associated entities are authorized financial institutions, be regarded as the power to make rules in respect of the associated entities only in relation to particulars relating to their businesses of receiving or holding client assets of intermediaries of which they are associated entities.

161A. Use of incriminating evidence in proceedings⁶

Notwithstanding any other provisions of this Ordinance, where a person -

- (a) is required under section 142(3) to notify the Commission of any matter;
- (b) is required under section 161(6) to notify the Commission of any matter; or
- (c) is required by rules made pursuant to section 144(2)(i), 145(2)(k), 147(2)(d) or 148(2)(f) to notify the Commission of any matter.

and the notification might tend to incriminate the person, then the notification shall not be admissible in evidence against the person in criminal proceedings in a court of law other than those in which -

- (i) he is charged with an offence under Part V of the Crimes Ordinance (Cap. 200), or for perjury, in

respect of the notification;

(ii) in the case of paragraph (a), he is charged with an offence under section 142(12) in respect of the notification;

(iii) in the case of paragraph (b), he is charged with an offence under section 161(7) in respect of the notification; or

(iv) in the case of paragraph (c), he is charged with an offence under any rules made under section 144(4) or (5), 145(4) or (5), 147(5) or (6), 148(3) or (4) (as the case may be) in respect of a contravention taking place by reason of a failure to comply with a requirement to give the notification.