

立法會
Legislative Council

LC Paper No. LS110/01-02

**Paper for the House Committee Meeting
on 7 June 2002**

**Legal Service Division Report on
Subsidiary Legislation Gazetted on 31 May 2002**

Date of Tabling in LegCo : 5 June 2002

Amendment to be made by : 3 July 2002 (or the 1st meeting of LegCo in the next session if extended by resolution)

Merchant Shipping (Limitation of Shipowners Liability) Ordinance (Cap. 434)
Merchant Shipping (Limitation of Shipowners Liability) (Rate of Interest) Order 2002 (L.N. 86)

Under paragraph 1 of Article 11 of the Convention on Limitation of Liability for Maritime Claims, 1976 ("the Convention") as applied by the Merchant Shipping (Limitation of Shipowners Liability) Ordinance (Cap. 434) ("the Ordinance"), shipowners and salvors may limit their liabilities for maritime claims by constituting limitation funds. Such limitation funds shall comprise the amounts set out in the Convention together with interest thereon from the date of the occurrence giving rise to the liability until the date of the constitution of the fund.

2. According to section 19 of the Ordinance, the Monetary Authority may from time to time prescribe the rate of interest to be applied for the purposes of paragraph 1 of Article 11 of the Convention. This Order -

(a) consolidates the various previous Orders which prescribed the rate of interest applied to different periods of time into one Order; and

(b) prescribes the new rate of interest applicable on or after 31 May 2002.

3. Members may refer to the LegCo Brief (Ref:M6/15/1) dated 31 May 2002 issued by the Financial Services Bureau for background information.

4. The legal and drafting aspects of the Order are in order.

Securities and Futures Commission Ordinance (Cap. 24)
Financial Resources (Amendment) Rules 2002 (L.N. 87)

5. The Financial Resources Rules (Cap. 24 sub. leg.) ("the principal Rules") set out the financial resources requirements imposed on persons registered with the Securities and Future Commission ("SFC"). The SFC has reviewed the business practice of the securities dealers and securities margin financiers and has identified two practices in their provision of securities margin financing which are considered to be particularly imprudent and risky. The purpose of these Rules is to amend the principal Rules to limit such financial and credit risks by the following means with effect on 1 October 2002:

- (a) At present the securities dealers and securities margin financiers accept as collateral for margin loans a large quantity of stocks that may be difficult to liquidate quickly. Section 2 of these Rules amends section 13 of the principal Rules to require, for the purpose of calculating liquid assets of the securities dealers and securities margin financiers, the application of a 80% discount on the stocks and warrants held by the securities dealers and securities margin financiers as margin collateral that are identified as "illiquid" (i.e. difficult to liquidate quickly due to the amount held in relation to market demand).
- (b) At present the securities dealers and securities margin financiers pool securities belonging to margin clients, including "non-borrowing or low-borrowing" margin clients (i.e. those clients who borrow very little or not at all, but have a relatively large amount of securities in their margin accounts), and repledge the more liquid items of such securities to banks in order to obtain bank loans. These borrowed funds are then used by the securities dealers and securities margin financiers to finance their business operation and loans to other margin clients against collateral that may not be acceptable as collateral to banks. Section 3 of these Rules amends section 21 of the principal Rules to require securities dealers and securities margin financiers to compare the total value of their margin loans to clients with the total value of borrowings they have obtained by re-pledging securities received from their margin clients (the "gearing adjustment"). If the borrowings obtained by any securities dealer or securities margin financier exceed 65% of the total margin loans extended by him, the excess must be included in his ranking liabilities.

6. Section 4 of these Rules amends Schedule 7 to the principal Rules by introducing consequential renumbering of references to section 21 of the principal Rules, and adding a new item relating to the gearing adjustment required under the new section 21(2).

7. Members may refer to the LegCo Brief (no reference number indicated) dated 30 May 2002 issued by the SFC for background information.

8. According to the LC Paper (Ref: CB(1) 1628/01-02(06)) dated 29 April 2002, the SFC has considered the market concerns and proposals raised in the public consultation and adjusted the discount level on illiquid collateral to 80% instead of 90% and the gearing adjustment to 35% instead of 50%.

9. At the meeting of the Panel on Financial Affairs on 6 May 2002, Members did not object to the amendments in general. One member raised the concern that the definition of "illiquid collateral" would create a negative labelling effect on some stocks or warrants. The Administration assured that no particular stock or warrant would be labelled as an 'illiquid collateral'. What would be regarded as illiquid collateral varied between individual securities dealer and securities margin financier as the analysis would only be applied to stocks and warrants identified as the three largest collateral holdings of the top 20 margin clients of each securities dealer and securities margin financier. The definition of 'illiquid collateral' applied to stocks or warrants that would likely take more than one month to liquidate, based on their respective trading volume in the market during the six months immediately preceding the month prior to the month in which calculation was made or those stocks and warrants that constituted 5% or more of the market capitalization of the shares or the issue size of the warrants at the end of the month immediately preceding the month prior to the month in which calculation was made.

10. The term "gearing adjustment" is to be inserted in item 29 of Schedule 7 of the Principle Rules. However, no reference of this term has been made in the Securities and Future Commission Ordinance or the principal Rules. We have clarified this issue with the SFC (**Annex A**) and its reply (**Annex B**) is enclosed with this report.

Tax Reserve Certificates Ordinance (Cap. 289)

Tax Reserve Certificates (Rate of Interest) (No. 6) Notice 2002 (L.N. 88)

11. This Notice fixes the rate of interest payable on tax reserve certificates issued on or after 3 June 2002 at 0.2812% per annum. The rate before this Notice was 0.5812% per annum.

Encl.

Prepared by

LAI Shun-wo, Monna
Assistant Legal Adviser
Legislative Council Secretariat
4 June 2002

LS/S/34/01-02
2869 9370
2877 5029

The Securities and Futures Commission
12/F Edinburgh Tower
Landmark
15 Queen's Road
Central
Hong Kong

3 June 2002

(Attn: Ms Thrity Mukadam, Senior Counsel)

BY FAX
Fax No. : 2521 7884
Total nos. of pages : (1)

Dear Ms Mukadam,

Financial Resources (Amendment) Rules 2002 (L.N. 87 of 2002)

We are scrutinising the legal and drafting aspects of the above rules. We note that no reference of the term "gearing adjustment" to be added in item 29 of Schedule 7 has been made in the Securities and Futures Commission Ordinance (Cap. 24) and the Financial Resources Rules (Cap. 24 sub. leg.). To avoid difficulties in reference, please consider whether there is a need to define the term "gearing adjustment" in the Ordinance or the Rules.

The Rules will be considered in the House Committee meeting to be held on 7 June 2002. It is appreciated that your reply in both languages could reach us by noon, 5 June 2002.

Yours sincerely,

(Monna Lai)
Assistant Legal Adviser

cc: LA

Thrity Mukadam
Senior Counsel

Our ref : 121/LG/1001/0200/0010
Your ref : LS/S/34/01-02

Annex B

6 June 2002

Ms Monna Lai
Assistant Legal Adviser
Legal Services Division
Legislative Council Secretariat
Government of HKSAR

BY FAX to 2877 5029
(2 pages including this sheet)

Dear Ms Lai

Financial Resources (Amendment) Rules 2002

Thank you for your fax of yesterday evening.

The term "gearing adjustment" is well understood by the market and hence we do not consider it necessary to define the same.

Additionally, you will see that Schedule 7 not only sets out the items to be included in the calculation of assets and liabilities, but also notes the particular section that requires its inclusion. Hence (for example), in the case of the new item 29 "gearing adjustment", reference is made to section 21(2) which sets out the gearing adjustment requirement. Accordingly, there should be no doubt as to what the term "gearing adjustment" means.

I hope the above clarifies your concern. Please let me know if you need further information or clarification.

Yours sincerely,

Thrity Mukadam
Senior Counsel

Encl



<<Date>>

<<Name of Recipient>>

<<Company>>

page 6

c c Mr Howard Yam, FSB (Fax No. 28611494)

l:\ls\thm\sub leg\sfc0\frs - 2002\letters\020529 - legco.doc