

**Subcommittee on Draft Subsidiary Legislation  
for commencing the Securities and Futures Ordinance**

**Proposed work plan**

This paper sets out the proposed work plan to take forward subsidiary legislation to be made under the newly enacted Securities and Futures Ordinance for commencing it.

**Present position**

2. The Securities and Futures Ordinance passed by the Legislative Council on 13 March 2002 will come into force as soon as the relevant subsidiary legislation is in place. This includes some 38 sets of rules and regulations. Our target is to bring the new legislation into operation by end 2002.

3. Of the 38 sets of subsidiary legislation –

- (a) the public have been consulted on the draft of 11 sets;
- (b) 15 sets are adapted from existing law with no major change, and will be released for public consultation shortly; and
- (c) the remaining 12 sets will be issued for public consultation in the next couple of months.

**Engaging the market**

4. In preparing the subsidiary legislation, we are committed to working in partnership with the financial market participants to facilitate their compliance. This will be achieved through consultation with the market and the public in general.

5. Specifically, the Securities and Futures Commission (SFC) invites the public to give comments on the exposure draft of all the subsidiary legislation referred to in the **Annex** within a specified consultation period. Where appropriate, the SFC would form working groups to tap market expertise in the formative stage of drawing up the exposure drafts. On complex rules, the Commission plans to conduct technical briefing sessions for the stakeholder groups at the beginning of the consultation period. This will facilitate meaningful exchange of views at an early stage. Any comments received during the public consultation will be summarised and presented in the form of a table attached to the Subcommittee papers for Members' consideration (see paragraph 9).

### **General principles**

6. To reduce the cost of compliance, we have started a critical review of all existing rules and regulations that are to be re-enacted under the Securities and Futures Ordinance with a view to removing any unnecessary or obsolete regulatory requirements and identifying room for streamlining existing procedures. This pro-compliance and user-friendly principle will also apply to the new subsidiary legislation to ensure that the new regulatory regime as a whole can be cost-effective for both compliance and enforcement.

7. Some of the subsidiary legislation provides for exemptions and waivers, and stipulates "safe harbours", in order to facilitate market development and increase market liquidity. We are inviting views from concerned market players to identify specific types of concerned products or transactions, or classes of persons, where regulatory requirements could be adjusted in a transparent and consistent manner to encourage market innovation and facilitate users, and without compromising investor protection.

### **Proposed work schedule**

8. We propose to submit subsidiary legislation in draft to the Subcommittee in four batches, and to meet with the Subcommittee in end April, end May, July and September 2002. To facilitate discussion with Members, we have set out in the **Annex** the subsidiary legislation in each batch, with a brief description of the coverage, progress of consultation, and tentative timetable for Subcommittee meetings.

## **Modus operandi**

9. We suggest that for each piece of subsidiary legislation, we issue to Members a Subcommittee discussion paper which contains –

- (a) a covering note with an analysis of the enabling provision in the Securities and Futures Ordinance under which we propose to make the subsidiary legislation;
- (b) a copy of the consultation paper issued by the SFC, which explains the objectives and contents of the subsidiary legislation;
- (c) a copy of the conclusion report prepared by the SFC, which summarises the comments received during the consultation period and SFC's responses thereto. Explanations would be given as a matter of rule for those public comments not accepted by the SFC; and
- (d) the subsidiary legislation in draft, incorporating amendments to address public comments as appropriate.

10. We shall issue the discussion papers to Members as soon as they are ready so as to allow Members more time to consider them. We shall aim to issue the papers at least a week in advance of the meeting of the Subcommittee convened to consider them.

11. The grouping of subsidiary legislation for each Subcommittee meeting may be adjusted in the light of progress made in drafting, public consultation and deliberations by Members.

## **Advice sought**

12. Members may wish to endorse in principle –

- (a) the proposed work schedule in the Annex; and
- (b) the proposed modus operandi in paragraphs 9 to 11.

Financial Services Bureau  
22 March 2002

**Proposed grouping of subsidiary legislation for Subcommittee's deliberations**

**Batch 1**

**Proposed for Subcommittee's consideration at end April 2002**

<b>Enabling provision in Securities and Futures Ordinance</b>	<b>Subsidiary legislation</b>	<b>Authority to make Sub Leg</b>	<b>Remarks</b>	<b>Consultation</b>
Section 148(1)	Client Securities Rules	SFC	Technical operational requirements regarding the manner in which intermediaries and their associated entities must treat client securities and securities collateral received or held in Hong Kong. These include a requirement for registration or deposit, circumstances in which withdrawal is permitted and the extent of the right of disposal of such securities and collateral. Most of the requirements are currently in primary legislation.	Completed
Section 149(1)	Client Money Rules	SFC	Technical operational requirements regarding the manner in which licensed corporations and certain associated entities must treat and deal with client money received or held in Hong Kong. There are provisions for the payment of client money into segregated trust accounts or client accounts, payments out of such accounts and payment of interest. Most of the requirements are now in primary legislation.	Completed
Section 151(1)	Keeping of Records Rules	SFC	Technical operational requirements regarding the accounting and other records that intermediaries and their associated entities must keep e.g. to explain transactions undertaken; account for client assets; reflect their financial positions; enable true and fair profit and loss accounts and balance sheets to be prepared. The requirements are now being treated differently – under primary law primarily in the case of securities and commodities but by way of subsidiary legislation for leveraged foreign exchange trading. Efforts will also be made to streamline the procedures where appropriate.	Completed

<b>Enabling provision in Securities and Futures Ordinance</b>	<b>Subsidiary legislation</b>	<b>Authority to make Sub Leg</b>	<b>Remarks</b>	<b>Consultation</b>
Sections 174(3)(d) & 397(1)	Unsolicited Calls – Exemption Rules	SFC	Based on new rules on cold calling made by the UK Financial Services Authority.	Completed
Section 397(1)	Licensed Persons and Registered Institutions Rules	SFC	Adapted from existing subsidiary legislation.	Completed
Section 397(1)	Recognized Counterparty Rules	SFC	Provisions prescribing certain institutions as recognized counterparties for the purposes of paragraph (c) of the definition of “recognized counterparty” in Part 1 of Schedule 1 to the SF Ordinance.	Completed

**Batch 2****Proposed for Subcommittee's consideration at end May 2002**

<b>Enabling provision in Securities and Futures Ordinance</b>	<b>Subsidiary legislation</b>	<b>Authority to make Sub Leg</b>	<b>Remarks</b>	<b>Consultation</b>
Section 35(1)	Contracts Limits and Reportable Positions Rules	SFC	Adapted from existing subsidiary legislation with no significant policy change.	March
Section 80(1)	Transfer of Functions – Recognized Investor Compensation Company Order	CE in Council	Provisions transferring certain functions in connection with the Investor Compensation Fund from SFC to a recognized investor compensation company.	March
Section 118(2)	Leveraged Foreign Exchange Trading – Arbitration Rules	SFC	Adapted from existing subsidiary legislation with no significant policy change.	March
Section 152(1)	Contract Notes, Statements of Account and Receipts Rules	SFC	Technical operational requirements prescribing the manner in which contract notes, statements of account and receipts must be prepared by and delivered to clients by intermediaries or their associated entities. In particular, the rules set out the detailed information that must be included in such documents and the periods within which they must be delivered to clients. The requirements will be adapted from existing law.	Completed
Sections 156(1) & 397(1)	Accounts and Audit Rules	SFC	Adapted from existing subsidiary legislation.	Completed
Sections 165(1) & 397(1)	Associated Entities Rules	SFC	Technical provisions prescribing the particulars that must be contained in a notice given to the Commission by an associated entity when it becomes such an entity and when it ceases to be one.  Consultation conducted with the HKMA which regulatees would be most affected, in mid 2001.	March

<b>Enabling provision in Securities and Futures Ordinance</b>	<b>Subsidiary legislation</b>	<b>Authority to make Sub Leg</b>	<b>Remarks</b>	<b>Consultation</b>
Sections 194(5) & 397(1)	Registration of Disciplinary Orders Rules	SFC	Adapted from existing subsidiary legislation with no significant policy change.	March
Section 244(1)	Investor Compensation Rules	CE in Council	Technical provisions specifying among other matters the framework for funding the compensation fund.	March
Section 244(1)	Investor Compensation Limits Rules	CE in Council	To provide for the maximum amount of compensation for each investor.	March
Section 244(2)	Investor Compensation – Miscellaneous Rules	SFC (FS to be consulted on certain items)	Technical provisions specifying among other matters the circumstances where a claim may be made on the compensation fund, those who may not make a claim and the procedure for making a claim by those entitled to do so.	March
Sections 282(1) & 306(1)	Price Stabilization Rules	SFC (after consultation with public and FS)	Based on new price stabilization rules made by the UK Financial Services Authority. The provisions define permitted price stabilization activities (to match those adopted internationally).	Completed
Section 393	Gold Purchase Notice	FS	Adapted from existing subsidiary legislation with no significant policy change.	March
Section 394(1)	Levy Order (on levy payable to SFC)	CE in Council	Adapted from existing subsidiary legislation with no significant policy change.	March
Section 394(6)	Levy Rules (on payment, collection etc. of levy in item 28)	CE in Council	Adapted from existing subsidiary legislation with no significant policy change.	March
Section 397(1)	Professional Investor Rules	SFC	Provisions prescribing classes of persons who will be considered as professional investors for the purposes of paragraph (i) of the definition of “professional investor” in Part 1 of Schedule 1 to the SF Ordinance	Completed
Section 397(1)	Information Rules	SFC	Adapted from existing legislation with no significant policy change.	March

**Batch 3**  
**Proposed for Subcommittee's consideration in July 2002**

<b>Enabling provision in Securities and Futures Ordinance</b>	<b>Subsidiary legislation</b>	<b>Authority to make Sub Leg</b>	<b>Remarks</b>	<b>Consultation</b>
Section 25(1)	Transfer of Functions – Stock Exchange Company Order	CE in Council	Adapted from existing subsidiary legislation – may need some change.	April
Section 36(1)	Stock Market Listing Rules	SFC	Adapted from existing subsidiary legislation – may need some change.	April
Sections 170(3)(e) & 397(1)	Short Selling Exemptions Rules	SFC	Adapted from existing subsidiary legislation. Inviting market input on exemptions to reduce compliance burden.	May
Sections 226 & 233(b)	Appeals Tribunal – Registration of Orders Rules	Chief Justice	Adapted from existing subsidiary legislation with no significant policy change.	May
Section 233(d)	Securities and Futures Appeals Tribunal Rules	Chief Justice	To provide for operational procedures for the Securities and Futures Appeals Tribunal in handling applications for reviews.	May
Sections 264 & 269(b)	Market Misconduct Tribunal – Registration of Orders Rules	Chief Justice	Adapted from existing subsidiary legislation with no significant policy change.	May
Section 376(1)(b)	Disclosure of Interests – Exclusions Regulations	CE in Council	Updated on the basis of existing subsidiary legislation to reflect changes required in the proposed regime for disclosure of securities interests.  Market consultation started in 1998 and is an on-going process in the context of the overall package of proposals.	April



Enabling provision in Securities and Futures Ordinance	Subsidiary legislation	Authority to make Sub Leg	Remarks	Consultation
Section 377	Disclosure of Interests – Securities Borrowing and Lending Rules	SFC (after consultation with FS)	Provisions prescribing (a) the circumstances in which persons lending shares are exempt from the duty of disclosure under Divisions 2 to 4 of Part XV of the SF Bill; and (b) interests and short positions, in shares held by regulated persons, that are to be disregarded under section 323 of the SF Ordinance. The Rules also provide for approval of custodians and others as approved lending agents; and the keeping of records of dealings in interests in shares that are exempt from the duty of disclosure for the purposes of Divisions 2 to 4 of Part XV or disregarded for the purpose of section 323.  Market comments being considered with a view to facilitating stock borrowing and lending as appropriate.	Completed
Section 395	Fees Rules (on payment of fees to SFC)	CE in Council	Adapted from existing subsidiary legislation.	April
Section 397	Annual Returns Rules (on timing, particulars, manner, circumstances, etc. of submission of returns to SFC)	SFC	Adapted from existing subsidiary legislation with no significant policy change.	April
Sections 397 & 173	Miscellaneous Rules	SFC	Adapted from existing subsidiary legislation with no significant policy change involved.	May
Section 397(8)	Offence and Penalty Regulations	CE in Council	Adapted from subsidiary legislation.	May
Section 397(1)	Leveraged Foreign Exchange Trading – Exemption Rules	SFC	Adapted from existing subsidiary legislation with no significant policy change.	April
Section 397(1)	Corporation Rules	SFC	Adapted from existing legislation – no significant policy change involved.	May

**Batch 4**  
**Proposed for Subcommittee's consideration in September 2002**

<b>Enabling provision in Securities and Futures Ordinance</b>	<b>Subsidiary legislation</b>	<b>Authority to make Sub Leg</b>	<b>Remarks</b>	<b>Consultation</b>
116(4)/4A	Security Deposits Rules/ Insurance Rules	SFC	Adapted from existing subsidiary legislation and exchange rules, the latter of which concerns the taking out and maintenance of fidelity insurance to cover specified risks, and related specified requirements.	June
145(1)	Financial Resources Rules	SFC (after consultation with FS)	Adapted from existing subsidiary legislation.	June