

**For discussion
on 15 July 2002**

Paper No. 19/02

**Subcommittee on Draft Subsidiary Legislation to be made
under the Securities and Futures Ordinance**

**Securities and Futures
(Leveraged Foreign Exchange Trading - Exemption) Rules**

This paper sets out the proposals of the Securities and Futures Commission (SFC) to prescribe the acts carried on by certain classes of persons that are excluded from the definition of “leveraged foreign exchange trading” in Part 2 of Schedule 5 to the Securities and Futures Ordinance (SFO) (5 of 2002).

Proposal

2. The SFC proposes to make the Securities and Futures (Leveraged Foreign Exchange Trading - Exemption) Rules, now in draft at **Annex 1**, under section 397(1) of the SFO.

Power to make the Rules and major features of the Rules

3. The term “leveraged foreign exchange trading” in Part 2 of Schedule 5 is described in broad terms but a range of acts and transactions are excluded from the definition. The acts excluded include, under paragraph (xiii) of the definition, acts performed for or in connection with any contract or arrangement by any person belonging to a class of persons, or carrying on a type of business, as prescribed by rules made by the SFC under section 397 of the Ordinance.

4. The draft Rules now prescribe that certain acts performed by a person belonging to any of the qualifying classes are to be excluded from the definition. This means that persons belonging to any of the qualifying classes, if they perform these acts, need not be licensed for carrying on a business in activities that may constitute leveraged foreign exchange trading.

5. The first qualifying class consists of corporations that have, or whose parent company has, a qualifying credit rating, provided that either (a) the principal business of the corporation is not in leveraged foreign exchange spot transactions; or (b) the average principal amount in each leveraged foreign exchange spot transaction entered into by the corporation is not less than \$7.8 million. The second and third qualifying classes are basically licensed corporations or clients of such corporations who are performing an act in connection with the sale, purchase or transfer of a listed currency warrant; as well as issuers, and corporations in the same group of companies as the issuer, of a listed currency warrant.

6. The SFC is of the view that the draft Rules would be *intra vires* if made as drafted.

Public consultation

7. The SFC released a consultation document and an exposure draft of the Rules on 5 June 2002 for comment by the public. Two submissions were received. The SFC considers that no major changes need to be made to the substance of the draft Rules in response to these submissions. The draft Rules have been further refined to better reflect the policy intention and to improve drafting. We attach the following documents for Members' reference -

- (a) Consultation Document on the draft Rules, at **Annex 2**, which sets out the underlying policy, together with the exposure draft of the Rules. The revised draft of the Rules are at Annex 1 for Members' consideration; and
- (b) Consultation Conclusions and Summary of Comments and SFC's Responses, at **Annex 3**, which set out the conclusions from the consultation and the SFC's responses, in the form of a table, to the comments received. A list of respondents is attached to the Consultation Conclusions.

Way forward

8. Subject to Members' views, the SFC will proceed to make the Rules under the authority vested with it and publish the Rules so made in the Gazette for tabling before the Legislative Council in the normal manner. The intention is that the Rules shall come into operation on the commencement of the SFO.

Securities and Futures Commission
Financial Services and the Treasury Bureau
8 July 2002

[*cf : section 397(1) of the Securities and Futures Ordinance and Part 2 of Schedule 5 thereto in respect of the definition of "leveraged foreign exchange trading"]*

SECURITIES AND FUTURES (LEVERAGED FOREIGN EXCHANGE TRADING - EXEMPTION) RULES

(Made by the Securities and Futures Commission under section 397(1) of the Securities and Futures Ordinance (5 of 2002))

1. Commencement

These Rules shall come into operation on the day on which Part XVI of the Securities and Futures Ordinance (5 of 2002) comes into operation.

2. Interpretation

In these Rules -

"listed currency warrant" () means a warrant -

- (a) that gives the holder of the warrant a right to receive from the issuer of the warrant a cash payment, on exercise, in the event that one specified currency is worth more or less (as the case may be) in relation to another specified currency on a specified date; and

(b) that -

- (i) is listed; or
- (ii) is not listed, but it is reasonably foreseeable will be listed within 14 days

after the day on which the warrant is first offered for sale.

3. Persons prescribed for the purposes of paragraph (xiii) of definition of "leveraged foreign exchange trading"

For the purposes of paragraph (xiii) of the definition of "leveraged foreign exchange trading" in Part 2 of Schedule 5 to the Ordinance, a person described in -

- (a) section 4(1);
- (b) section 5; or
- (c) section 6,

is prescribed as a person referred to in that paragraph for the purposes of any provision of the Ordinance.

4. Person referred to in section 3(a)

(1) The person referred to in section 3(a) is a corporation that -

- (a) satisfies the conditions set out in subsection (2); and
- (b) complies with the requirement in subsection (3).

(2) The conditions referred to in subsection (1)(a) are that -

- (a)
 - (i) the corporation has a qualifying credit rating or has such a rating for any of its debt instruments; or
 - (ii) the shares of the corporation are wholly owned, directly or indirectly, by another corporation, or by a partnership, which

has a qualifying credit rating or has such a rating for any of its debt instruments; and

- (b)
 - (i) the principal business of the corporation is not in leveraged foreign exchange spot transactions; or
 - (ii) the average principal amount of each leveraged foreign exchange spot transaction entered into by the corporation, calculated for each financial year of the corporation, is not less than \$7.8 million.

(3) The corporation shall, annually, within 4 months after the end of its financial year -

- (a) notify the Commission in writing that it satisfies the conditions set out in subsection (2); and
- (b) provide the Commission with such information as the Commission may reasonably require to enable the Commission to verify that the corporation does satisfy the conditions set out in subsection (2).

(4) If a corporation ceases to satisfy the conditions set out in subsection (2)(a) it shall within 7 days thereof notify the Commission in writing of the cessation.

(5) For the purposes of this section, the average principal amount of each leveraged foreign exchange spot transaction entered into by a corporation shall be computed by dividing the aggregate of all principal amounts of leveraged foreign exchange spot transactions entered into by the corporation during the relevant

financial year by the total number of such transactions entered into by the corporation during that financial year.

5. Person referred to in section 3(b)

The person referred to in section 3(b) is -

- (a) a licensed person in so far as the licensed person performs an act for or in connection with a contract or arrangement or a proposed contract or arrangement for the sale, purchase or transfer of a listed currency warrant; or
- (b) a client of a licensed corporation in so far as the client performs an act for or in connection with a contract or arrangement or a proposed contract or arrangement between the licensed corporation and the client for the sale, purchase or transfer of a listed currency warrant.

6. Person referred to in section 3(c)

The person referred to in section 3(c) is a corporation which is the issuer of any listed currency warrant or a corporation in the same group of companies as the issuer of any listed currency warrant in so far as the corporation performs an act for or in connection with a contract or arrangement or a proposed contract or arrangement for the sale, purchase or transfer of the listed currency warrant -

- (a) between a corporation (whether or not it is the corporation first referred to in this section) which is the issuer of the listed currency warrant

or a corporation in the same group of companies as the issuer of the listed currency warrant, and a licensed corporation;

- (b) between a corporation (whether or not it is the corporation first referred to in this section) which is the issuer of the listed currency warrant and a corporation in the same group of companies as the issuer of the listed currency warrant; or
- (c) between corporations which are both in the same group of companies as the issuer of the listed currency warrant but are not themselves the issuer.

Chairman,
Securities and Futures
Commission

2002

Explanatory Note

These Rules are made by the Securities and Futures Commission under section 397(1) of the Securities and Futures Ordinance (5 of 2002). They prescribe certain persons as belonging to a class of persons for the purposes of paragraph (xiii) of the definition of "leveraged foreign exchange trading" in Part 2 of Schedule 5 to the Ordinance. This means that any act performed by such persons

for or in connection with any contract or arrangement or a proposed contract or arrangement is excluded from the definition of "leveraged foreign exchange trading" in Part 2 of Schedule 5 to the Ordinance. A consequence is that the prescribed persons need not be licensed for such activities.



**SECURITIES AND
FUTURES COMMISSION**
證券及期貨事務監察委員會

**A Consultation Paper on the Securities and
Futures (Leveraged Foreign Exchange Trading
– Exemption) Rules**

《證券及期貨(槓桿式外匯交易 — 豁免)規則》
諮詢文件

Hong Kong
JUNE 2002

香港
2002年6月

Consultation

This consultation document invites public comments on the draft **Securities and Futures (Leveraged Foreign Exchange Trading - Exemption) Rules** (“the draft Rules”) which the Securities and Futures Commission (“SFC”) proposes to make under section 397(1) of the Securities and Futures Ordinance (No. 5 of 2002) (“the Ordinance”) when it commences.

Introduction

1. Under the existing Leveraged Foreign Exchange Trading Ordinance (“LFETO”), the term “leveraged foreign exchange trading” is initially described in broad terms and then a range of acts and transactions are excluded from the definition. A similar approach is followed in the Ordinance where items excluded from the definition of “leveraged foreign exchange trading” include:

- a transaction executed solely for the purpose of an insurance business by an authorized insurer;
- a contract executed on a specified futures or stock exchange through a licensed person;
- a transaction in an authorized collective investment scheme; and
- an act performed for or in connection with any contract or arrangement by any person belonging to a class of persons, or carrying on a type of business, as prescribed by rules made under section 397 of the Ordinance.

2. The draft Rules set out the acts carried on by certain classes of persons that the SFC proposes should be excluded from term “leveraged foreign exchange trading”.

3. There are controls built into the legislative system, whereby any rules made by the SFC must be subject to negative vetting by the Legislative Council. In addition, a mandatory consultation requirement is stipulated in section 398 of the Ordinance for such rules. The SFC therefore now releases the draft Rules (see Attachment 1) for public consultation.

4. The public may obtain copies of the consultation document and the attachment free of charge at the SFC’s office and on the SFC’s Internet website at <http://www.hksfc.org.hk>.

5. The SFC invites interested parties to submit written comments on the draft Rules or to comment on related matters that might have a significant impact upon the draft Rules **no later than 26 June 2002**. Any person wishing to comment should provide details of any organization whose views they represent. In addition, persons suggesting alternative approaches are encouraged to submit proposed text to amend the draft Rules.

The draft Rules

6. The draft Rules prescribe, for the purposes of the definition of “leveraged foreign exchange trading” in Part 2 of Schedule 5 to the Ordinance, that certain acts (except cold calling) performed by any person belonging to three qualifying classes are to be excluded from the definition. This means that persons belonging to the qualifying classes, if they perform these acts, need not be licensed for carrying on a business in activities that may constitute leveraged foreign exchange trading.

7. The first qualifying class consists of corporations that carry on any form of leveraged foreign exchange trading but whose principal business is not in leveraged foreign exchange spot transactions, provided:

- the average principal amount in such transactions is not less than \$7.8 million; and
- the corporation or its sole holding corporation or partnership has a qualifying credit rating.

8. Persons constituting the second qualifying class are licensed persons who are performing an act in connection with the sale, purchase or transfer of a currency warrant that is to be listed, and clients of the licensed persons undertaking such transactions through the licensed persons.

9. The third class consists of:

- issuers of such a currency warrant; and
- corporations belonging to the same group of companies as the issuer

who are undertaking the above transactions through licensed persons, or undertaking intra-group purchases, sales or transfers of such a currency warrant.

New Policy Initiatives

10. While the first qualifying class replicates that of the Leverage Foreign Exchange Trading (Exemption) Rules prescribed under the LFETO, the latter qualifying classes constitute a new policy initiative. The aim is to facilitate the development of the listed currency warrant market by removing unnecessary technical obstacles. As with the exclusion for the non-retail end of the foreign exchange market in the first qualifying class, the Commission believes that the extension of this exclusion to the second and third qualifying classes should not pose a material regulatory concern. Further, investor protection should not suffer, as the exempted classes of persons are limited to licensed persons and their clients carrying out a limited category of transactions, and certain companies with a defined relationship with an issuer carrying out intra-company transactions not involving investors.

Other matters

11. Please note that the names of the commentators and the contents of their submissions may be published on the SFC website and in other documents to be published by the SFC. In this connection, please read the Personal Information Collection Statement attached to this consultation paper.

12. You may not wish your name to be published by the SFC. If this is the case, please state that you wish your name to be withheld from publication when you make your submission.

13. Written comments may be sent -

By mail to: SFC (LFET Exemption Rules)
12/F, Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

By fax to: (852) 2293-5755

By on-line submission at: <http://www.hksfc.org.hk>

By e-mail to: LFET_Exemption_Rules@hksfc.org.hk

14. The draft Rules should be read in conjunction with the Securities and Futures Ordinance itself.

Personal Information Collection Statement

1. This Personal Information Collection Statement (“PICS”) is made in accordance with the guidelines issued by the Privacy Commissioner for Personal Data. The PICS sets out the purposes for which your Personal Data¹ will be used following collection, what you are agreeing to with respect to the SFC’s use of your Personal Data and your rights under the PDPO.

Purpose of Collection

2. The Personal Data provided in your submission to the SFC in response to this Consultation Paper may be used by the SFC for one or more of the following purposes:
 - to administer the relevant Ordinances, rules, regulations, codes and guidelines
 - made or promulgated pursuant to the powers vested in the SFC
 - for the purposes of performing the SFC’s statutory functions under the relevant Ordinances
 - for research and statistical purposes
 - other purposes permitted by law

Transfer of Personal Data

3. Personal Data may be disclosed by the SFC to the members of the public in Hong Kong and elsewhere, as part of the public consultation on the Consultation Paper. The names of persons who submit comments on the Consultation Paper together with the whole or part of their submission may be disclosed to members of the public. This will be done by publishing this information on the SFC web site and in documents to be published by the SFC throughout and at the conclusion of the consultation period.

Access to Data

4. You have the right to request access to and correction of your Personal Data in accordance with the provisions of the PDPO. Your right of access includes the right to obtain a copy of your Personal Data provided in your submission on the Consultation Paper. The SFC has the right to charge a reasonable fee for processing any data access request.

¹ Personal Data means personal data as defined in the Personal Data (Privacy) Ordinance, Cap 486 (“PDPO”)

Enquiries

5. Any enquiries regarding the Personal Data provided in your submission on the Consultation Paper, or requests for access to Personal Data or correction of Personal Data, should be addressed in writing to:

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

A copy of the Privacy Policy Statement adopted by the SFC is available upon request.

**SECURITIES AND FUTURES (LEVERAGED FOREIGN EXCHANGE
TRADING - EXEMPTION) RULES**

(Made by the Securities and Futures Commission
under section 397(1) of the Securities and
Futures Ordinance (5 of 2002))

1. Commencement

These Rules shall come into operation on the day appointed for the commencement of Part XVI of the Securities and Futures Ordinance (5 of 2002).

2. Interpretation

In these Rules, unless the context otherwise requires –
“listed currency warrant” (上市貨幣權證) means a warrant –

- (a) that gives the holder of the warrant a right to receive from the issuer of the warrant a cash payment, on exercise, in the event that one specified currency is worth more or less (as the case may be) in relation to another specified currency on a specified date; and
- (b) that -
 - (i) is listed; or
 - (ii) it is reasonably foreseeable will be listed within a period of 14 days from the date that the warrant is first offered for sale;

“foreign exchange trading” (外匯交易) and “leveraged foreign exchange trading” (槓桿式外匯交易) have the same meaning as in Part 2 of Schedule 5 to the Ordinance.

3. Exemption under paragraph (xiii) of the definition of “leveraged foreign exchange trading” in Part 2 of Schedule 5 to the Ordinance

For the purposes of the Ordinance, other than section 174(1) of the Ordinance, “foreign exchange trading” (外匯交易) and “leveraged foreign exchange trading” (槓桿式外匯交易) do not include any act performed for or in connection with a contract or arrangement or a proposed contract or arrangement by any person belonging to the class specified –

- (a) in section 4;
- (b) in section 5;
- (c) in section 6.

4. Qualifying class 1

(1) A person belongs to the class referred to in section 3(a) if it is a corporation that -

- (a) satisfies the conditions set out in subsection (2); and
- (b) complies with the provisions of subsection (3).

- (2) The conditions referred to in subsection (1)(a) are that -
 - (a) (i) the corporation has a qualifying credit rating; or
 - (ii) the shares of the corporation are wholly-owned, directly or indirectly, by another corporation, or by a partnership, which has such a rating; and
 - (b) (i) the principal business of the corporation is not in leveraged foreign exchange spot transactions; or
 - (ii) the average principal amount of each transaction in the corporation's leveraged foreign exchange spot trading, calculated for each financial year of the corporation, is not less than \$7.8 million.
- (3) The corporation must, annually, within 4 months after the end of its financial year -
 - (a) notify the Commission in writing that it satisfies the conditions referred to in subsection (2); and
 - (b) provide the Commission with sufficient information to enable the Commission to verify that the corporation does satisfy the conditions referred to in subsection (2).
- (4) If a corporation ceases to satisfy the conditions set out in subsection (2)(a) it shall within 7 days thereof notify the Commission in writing of the cessation.
- (5) For the purposes of this section, the average principal amount of each transaction shall be computed by dividing the aggregate of all principal amounts of leveraged foreign exchange spot transactions during the relevant financial year by the total number of such transactions for that year.

5. Qualifying class 2

A person belongs to the class referred to in section 3(b) if it is—

- (a) a licensed person and the act performed is for or in connection with a contract or arrangement, or a proposed contract or arrangement for the sale, purchase or transfer of a listed currency warrant; or
- (b) a client of the licensed person and the act performed is for or in connection with a contract or arrangement, or a proposed contract or arrangement for the sale, purchase or transfer of a listed currency warrant through the licensed person.

6. Qualifying class 3

A corporation belongs to the class referred to in section 3(c) if it is the issuer of the listed currency warrant, or a member of the same group of companies as the issuer of the currency warrant, and the act performed is for or in connection with a contract or arrangement, or a proposed contract or arrangement for the sale, purchase or transfer of a listed currency warrant -

- (a) between the issuer of the listed currency warrant, or members of the same group of companies as the issuer of the currency warrant, and a licensed person referred to in section 5;
- (b) between the issuer of the listed currency warrant and members of its group of companies; or
- (c) between members of the same group of companies as the issuer of the listed currency warrant.

Chairman,
Securities and Futures
Commission

2002

Explanatory Note

These Rules are made by the Securities and Futures Commission under section 397(1) of the Securities and Futures Ordinance (5 of 2002). They prescribe certain persons as belonging to a qualifying class of persons for the purposes of paragraph (xiii) of the definition of “leveraged foreign exchange trading” in Part 2 of Schedule 5 to the principal Ordinance. This means that the foreign exchange trading and leveraged foreign exchange trading activities of such persons are excluded from the definitions of “leveraged foreign exchange trading” and “foreign exchange trading” in Part 2 of Schedule 5 to the principal Ordinance. As a consequence, persons belonging to the qualifying classes need not be licensed for such activities.



**SECURITIES AND
FUTURES COMMISSION**
證券及期貨事務監察委員會

**Consultation Conclusions on the Draft Securities
and Futures (Leveraged Foreign Exchange
Trading – Exemption) Rules**

證券及期貨(槓桿式外匯交易—豁免)規則》
草擬本諮詢文件總結

Hong Kong
July 2002

香港
2002年7月

INTRODUCTION

1. On 5 June 2002, the Securities and Futures Commission (“SFC”) published a Consultation Document on the Draft Securities and Futures (Leveraged Foreign Exchange Trading - Exemption) Rules (“Consultation Document”). The consultation period ended on 26 June 2002.
2. The draft Rules prescribe, for the purposes of the definition of “leveraged foreign exchange trading” in Part 2 of Schedule 5 to the Securities and Futures Ordinance, that certain acts performed by any person belonging to three qualifying classes are to be excluded from the definition. The three classes are:
 - corporations that carry on any form of leveraged foreign exchange trading but whose principal business is not in leveraged foreign exchange spot transactions or the average principal amount in such transactions is not less than \$7.8 million, and the corporation or its sole holding corporation or partnership has a qualifying credit rating;
 - licensed persons who are performing an act in connection with the sale, purchase or transfer of currency warrants that are listed or are to be listed, and clients of the licensed persons undertaking such transactions through the licensed persons; and
 - issuers of such currency warrants and corporations belonging to the same group of companies as the issuers who are undertaking the above transactions through licensed persons, or undertaking intra-group purchases, sales or transfers of such currency warrants.
3. The first qualifying class replicates that of the existing Foreign Exchange Trading (Exemption) Rules prescribed under the Leveraged Foreign Exchange Trading Ordinance, while the latter qualifying classes constitute a new policy initiative. The aim is to facilitate the development of the listed currency warrant market by removing unnecessary technical obstacles, while not compromising investor protection.

CONSULTATION EXERCISE

4. A press release regarding the consultation exercise was issued on 5 June 2002. The Consultation Document and the draft Rules were posted on the SFC’s website and distributed to all licensed firms through the FinNet.
5. Two submissions was received, from Messrs Allen and Overy and Messrs Linklaters respectively. These have been posted on the SFC’s website. Two other market practitioners have also informally commented on the draft Rules.

CONSULTATION CONCLUSIONS

6. Messrs Allen and Overy expressed support for the addition of the two new qualifying classes, while Messrs Linklaters commented on specific provisions of the Rules. A summary of the comments from the two firms as well as the SFC's responses are set out in the Attachment. The other two practitioners believed that the exemptions provided in the draft Rules should address the concerns of the market in the listed currency warrant area.
7. In view of the comments received during the consultation exercise, the SFC concludes that no material changes to the draft Rules are required.

FINAL NOTE

8. The SFC would like to thank Messrs Allen and Overy, Messrs Linklaters and the industry participants for their comments in response to the Consultation Document.

**Summary of comments received on the Draft
Securities and Futures (Leveraged Foreign Exchange Trading - Exemption) Rules**

	Section Reference	Details of the Rules	Respondent's Comments	SFC's Responses
1	Rule 3 (Exemption under paragraph (xiii) of the definition of "leveraged foreign exchange trading" in Part 2 of Schedule 5 to the SF Ordinance)	This Rule prescribes, for the purposes of the SF Ordinance, "foreign exchange trading" and "leveraged foreign exchange trading" do not include any act performed for or in connection with a contract or arrangement or a proposed contract or arrangement by any person belonging to the three classes specified in Rules 4, 5 and 6.	[Linklaters] The classes referred to in this Rule should be alternatives, therefore, we suggest that the word "or" appears at the end of (a) and (b).	We have added the word "or" to Rule 3 for clarity. (Please note that the reference to section 174(1) of the SF Ordinance on cold calling activities has been removed. There is no policy change. This carve-out is not necessary as the draft Rules should not affect the operation of section 174(1) of the SF Ordinance in respect of prohibition of cold calling on leveraged foreign exchange contracts.)
2	Rule 4 (Qualifying class 1)	Qualifying class 1 refers to corporations whose principal business is not in leveraged foreign exchange spot transactions or the average principal amount in such transactions is not less than \$7.8 million, and the corporations or their sole holding corporations or partnerships have a qualifying credit rating.	[Linklaters] According to paragraph 7 of the Consultation Paper, the exemption applies if the corporation's principal business is not in leveraged foreign exchange spot transactions provided the average principal amount of each transaction meets a threshold test <u>and</u> there is a qualifying credit rating. However, Rule 4 states that a corporation must meet the qualifying credit rating and either its principal business is not in leveraged foreign exchange spot transactions or the average principal amount of each transaction meets a threshold test. We assume that the position in the Rules is the one to be followed.	Yes, the position as set out in the draft Rules is correct. This qualifying class refers to corporations – (a) whose principal business is not in leveraged foreign exchange spot transactions or the average principal amount in such transactions is not less than \$7.8 million; and (b) (b) the corporations or their sole holding corporations or partnerships have a qualifying credit rating.

	Section Reference	Details of the Rules	Respondent's Comments	SFC's Responses
			<p>[Linklaters] There is no definition in the draft Rules of "leveraged foreign exchange spot transactions".</p> <p>[Linklaters] The requirement to annually notify the SFC that a corporation satisfies the exemption conditions has become a condition of being able to rely on the exemption from the definition of leveraged foreign exchange trading (LFET). This means that if a corporation inadvertently fails to notify the SFC within 4 months after the end of its financial year, but continues to carry on LFET, it will have committed a criminal offence. This appears unduly harsh.</p>	<p>This term is not defined in the current Leveraged Foreign Exchange (Exemption) Rules prescribed under the Leveraged foreign Exchange Trading Ordinance ("LFETO"). The SFC takes the view that in the interests of simplicity, such a definition should not be added to the Rules. The term is well understood by the market, and that this arrangement has worked well for the past 7 years.</p> <p>The SFC is of the view that the notification requirement is not unduly harsh as the corporations concerned have a four-month period to make the notification. Moreover, the SFC has a practice of issuing reminders to existing exempt corporations reminding them of the notification requirements prior to their respective annual due dates.</p> <p>A failure to file an annual notice is not a criminal offence under the draft Rules. The failure simply means that the exemption will no longer be available.</p>

	Section Reference	Details of the Rules	Respondent's Comments	SFC's Responses
3	Rules 5 and 6 (Qualifying classes 2 and 3)	<p>Qualifying class 2 refers to licensed persons who perform an act for or in connection with the sale, purchase or transfer of currency warrants that are listed or are to be listed, and clients of the licensed persons undertaking such transactions through the licensed persons.</p> <p>Qualifying class 3 refers to issuers of such currency warrants and corporations belonging to the same group of companies as the issuers who undertake the above transactions through licensed persons, or undertaking intra-group purchases, sales or transfers of such currency warrants.</p>	<p>[Allen & Overy] Issuers of Hong Kong listed warrants have previously been hampered in the issuing of currency warrants in the Hong Kong market due to uncertainty as to whether these types of warrants are technically caught by the current legislation, particularly in respect of any pre-listing activity in the currency warrants. By exempting any act in connection with the purchase, sale and transfer of listed currency warrants from the definition of leveraged foreign exchange trading, the current uncertainty will be removed and will give issuers of derivative warrants more flexibility to bring these products to the market. The addition of the two new qualifying classes relating to currency warrants is supported. The new Rules are presumably intended to cover any pre-listing grey market activity in the currency warrants as well as any post-listing activity.</p> <p>[Linklaters] Although the SFC has accepted in the past that there is an argument that currency warrants are "securities" and therefore do not fall within the provisions of the Leveraged Foreign Exchange Trading Ordinance, as the SFC has now specifically excluded "listed currency warrants" from the definition of LFET, this exemption should also be extended to non-listed currency warrants and currency warrants listed on exchanges other than the Hong Kong Stock Exchange.</p>	<p>The assumption is correct in the context. "Listed currency warrants" has been defined in Rule 2 to include a currency warrant that is listed, and not listed but is reasonably foreseeable that it will be listed within a period of 14 days from the date that the warrant is first offered for sale.</p> <p>While the SFC has accepted in the past that certain currency warrants may constitute "securities", the SFC does not accept that all currency warrants are necessarily "securities" and therefore do not fall within the provisions of the LFETO. It may be noted that section 2(2) of the LFETO provides that "foreign exchange trading" and "leveraged foreign exchange trading" exclude, amongst others, any act performed for or in connection with a contract or an arrangement or a proposed contract or arrangement that is a transaction executed on a recognized stock exchange by</p>

	Section Reference	Details of the Rules	Respondent's Comments	SFC's Responses
			<p>[Linklaters] As there are no filing requirements for qualifying classes 2 and 3, we assume this means that entities satisfying the requirements in Rules 5 and 6 would be automatically exempt.</p>	<p>or through a registered securities dealer.</p> <p>We do not agree that the exemption should be extended to non-listed currency warrants out of investor protection concerns. To so extend may unnecessarily enlarge the scope of exemption. As regards currency warrants listed on exchanges other than the Hong Kong Stock Exchange, it may be noted that such an exemption is already provided for in the SF Ordinance. In Schedule 5 of the SF Ordinance, the definition of "leveraged foreign exchange trading" excludes, among others, any act performed for or in connection with any contract or arrangement or a proposed contract or arrangement that is a transaction executed on a specified stock exchange (or futures exchange) by or through a licensed person. The exclusions proposed under the draft Rules essentially aim to supplement these exemptions and cover transactions in currency warrants that are to be listed, and transactions in listed currency warrants that are carried out during non-exchange trading hours through licensed persons.</p> <p>The assumption is correct. There are no filing requirements for qualifying classes 2 and 3.</p>

	Section Reference	Details of the Rules	Respondent's Comments	SFC's Responses
4	General	Transitional arrangements.	[Linklaters] What happens to institutions that are currently exempt under the Leveraged Foreign Exchange Trading (Exemption) Rules? We assume that they would continue to be regarded as exempt until they are required to renew the exemption, rather than have to reapply under the draft Rules.	The assumption is correct. Section 91 of Schedule 10 to the SF Ordinance provides that any document or information given or served to the SFC under any provision of an Ordinance repealed by the SF Ordinance shall be deemed to have been served under any provision in the SF Ordinance. We take the view that section 91 covers the notification requirements imposed on existing exempt institutions.

List of Respondents

Date received	Respondent
25 June 2002	Allen and Overy
28 June 2002	Linklaters (on behalf of 2 firms)