

**For discussion
on 15 July 2002**

Paper No. 22/02

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

**Securities and Futures
(Disclosure of Interests – Exclusions) Regulation**

This paper sets out the proposals of the Securities and Futures Commission (SFC) to provide certain exclusions from the disclosure requirements under Part XV of the Securities and Futures Ordinance (SFO) (5 of 2002).

Proposal

2. We propose to recommend the Chief Executive in Council to make the Securities and Futures (Disclosure of Interests – Exclusions) Regulation, now in draft at **Annex 1**, under section 376 of the SFO.

Power to make the Regulation

3. Part XV of the SFO requires the disclosure of interests in securities by persons who are interested in 5% or more of the relevant share capital of a listed corporation and by directors and chief executives of listed corporations.

4. Section 323(1)(j) of the SFO provides that interests in shares that are prescribed by regulations for the purpose of that section are to be disregarded for the purposes of Divisions 2 to 4 of Part XV (the principal provisions affecting shareholders holding 5% or more of shares of a listed company). Similarly, section 346(1)(e) of the SFO provides that interests in shares that are prescribed by regulations for the purpose of that section are to be disregarded for the purposes of Divisions 7 to 9 of Part XV (the principal provisions affecting directors and chief executives of listed corporation). Under section 376 of the SFO, the Chief Executive in Council may make regulations covering a range of matters including prescribing interests for the purposes of sections 323 and 346 to provide exclusions from the requirements of Part XV.

5. The SFC and the Department of Justice have been consulted on the vires of the draft Regulation. The advice is that the draft Regulation would be *intra vires* if made as drafted.

Major features of the draft Regulation

6. The draft Regulation at Annex 1 is adapted from the existing Securities (Disclosure of Interests) (Exclusions) Regulations modified suitably to promote market transparency, facilitate compliance and remove superfluous clauses.

7. The draft Regulation is proposed to be made by the Chief Executive in Council under section 376 of the SFO. It prescribes specific interests for the purposes of sections 323 and 346 so as to exclude such specific interests from the disclosure obligations under Part XV of the SFO. The Regulation excludes those circumstances where certain persons¹ would come to have disclosure obligations technically but such disclosure would be onerous to the persons concerned and generally not useful in enhancing market transparency.

Public consultation

8. The SFC released a consultation document (**Annex 2**) and an exposure draft of the Regulation on 16th May 2002 for public comments. One submission representing a group of eight financial institutions was received. The SFC has considered the comments and met further with the group. The draft Regulation has been revised to expand the scope of the exemption for intermediaries.

9. The submission called for a widening of the exemptions to include three new areas—

- (a) the interest of intermediaries entering in an exchange-traded options and futures contracts solely for a client;

¹ For example, such persons include an official trustee, a trustee of a trust constituted exclusively for the purpose of a recognised occupational retirement scheme, an intermediary entering in a stock options or stock futures contract solely for a client, etc.

- (b) “Client facilitation” transactions²; and
- (c) Underwriting commitments, price stabilisation and ancillary transactions in relation to initial public offerings³.

10. The SFC has agreed to provide the exemption in respect of the interest of intermediaries entering in exchange-traded options and futures contracts solely for a client. However, the SFC considers that for the “client facilitation” transactions and IPOs related transactions, the intermediary/manager will acquire an economic interest in the shares and as such it would not be appropriate to provide the proposed exemption. The points raised in the submission and the SFC’s responses are set out in the Summary of Comments at the Appendix to Annex 3 attached.

11. As reported by the Legislative Council Bills Committee on the Securities and Futures Bill and Banking (Amendment) Bill 2000 to the House Committee in February 2002, the new disclosure regime under Part XV of the SFO will be reviewed at an appropriate time in the light of its actual implementation, in consultation with the Legislative Council Panel on Financial Affairs. These issues could be revisited in the light of the experience gained.

12. We attach the following documents for Members’ reference -

- (a) Consultation Document on the draft Regulation, at **Annex 2**, which sets out the underlying policy, together with the exposure draft of the Regulation. The draft Regulation as revised in the light of the comments received is at Annex 1 for Members’ consideration; and
- (b) Consultation Conclusions and Summary of Comments and SFC’s Responses in respect of the consultation exercise in May/June 2002 at **Annex 3**, which set out the conclusions

² Client facilitation activity refers to activities performed by a dealer to achieve a particular standard of execution for its clients. The dealer may enter into relevant transactions as principal and acquire an economic interest in shares in the process. See item 2 of Summary of Comments at the Appendix to Annex 3.

³ The submission called for exemptions for, effectively, all transactions in which managers of an initial public offering may be engaged. See item 3 of Summary of Comments at the Appendix to Annex 3 for more details.

from the consultation and the SFC's responses, in the form of a table, to the comments received.

Way forward

13. Subject to Members' views, we will submit the draft Regulation at Annex 1 to the Chief Executive in Council for approval. If approved, the Regulation will be published in the Gazette for tabling before the Legislative Council in the normal manner. The intention is that the Regulation shall come into operation on the commencement of the SFO.

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

DRAFT

[Cf: Sections 323, 344, 346 and 376 of the Securities and Futures Ordinance.]

**SECURITIES AND FUTURES (DISCLOSURE OF INTERESTS -
EXCLUSIONS) REGULATION**

(Made by the Chief Executive in Council under
section 376(1) of the Securities and
Futures Ordinance (5 of 2002))

1. Commencement

This Regulation shall come into operation on the day on which Part XV of the Securities and Futures Ordinance (5 of 2002) comes into operation.

2. Interpretation

In this Regulation, unless the context otherwise requires -
"back-to-back contract" (背對背合約) means a contract made -

- (a) between an intermediary and its client for the sale or purchase of a stock futures contract or a stock options contract;
- (b) pursuant to a previous agreement between the intermediary and the client;
- (c) on identical terms to an exchange contract entered into by the intermediary for the client; and
- (d) with the effect that -

(i) where the intermediary acts as a purchaser in an exchange contract, the intermediary acts as a seller under the first-mentioned contract; and

(ii) where the intermediary acts as a seller in an exchange contract, the intermediary acts as a purchaser under the first-mentioned contract;

"client" (客戶), in relation to an intermediary, means a person for whom the intermediary provides a service the provision of which constitutes a regulated activity;

"conditional offer" (有條件要約) means an offer to purchase shares in a listed corporation made by or on behalf of an offeror to the holders of all the shares or all the shares of a particular class in the listed corporation other than (in either case) shares held by or on behalf of -

(a) the offeror;

(b) the offeror's holding company, the offeror's subsidiary or a subsidiary of the offeror's holding company; or

(c) any person who has agreed that no such offer is to be made in respect of shares he holds,

and the offer is subject to the condition that acceptances are received in respect of such proportion of the shares for which the offer is made as specified in, or ascertained by reference to, the terms of the offer;

"exchange contract" (交易合約) means a contract made for the sale or purchase of a stock futures contract or a stock options contract and entered into by an intermediary with another intermediary, through the trading facilities provided by, and subject to the rules of, the relevant exchange company;

"listed corporation" (上市法團) has the meaning assigned to it by section 308 of the Ordinance;

"Official Trustee" (法定受託人) means the Official Trustee appointed under section 66 of the Trustee Ordinance (Cap. 29);

"recognized occupational retirement scheme" (認可職業退休計劃) has the meaning assigned to it by section 2(1) and (2A) of the Inland Revenue Ordinance (Cap. 112);

"relevant exchange company" (有關交易所公司), in relation to -

(a) dealings in a stock futures contract, means the Futures Exchange Company;

(b) dealings in a stock options contract, means the Stock Exchange Company;

"short position" (淡倉) has the meaning assigned to it by section 308 of the Ordinance;

"stock futures contract" (股票期貨合約) means a stock futures contract specified in column 2 of Schedule 1 to the Securities and Futures (Contracts Limits and Reportable Positions) Rules (L.N. of 2002);

"stock options contract" (股票期權合約) means a stock options contract specified in column 2 of Schedule 2 to the

Securities and Futures (Contracts Limits and Reportable Positions) Rules (L.N. of 2002).

3. Prescribed interests and short positions to be disregarded for the purpose of notification by substantial shareholders

(1) The following interests and classes of interests, and short positions, in shares comprised in the relevant share capital of a listed corporation are prescribed for the purposes of section 323 of the Ordinance -

- (a) an interest or short position of a person in his capacity as a beneficiary under a trust constituted exclusively for the purposes of a recognized occupational retirement scheme;
- (b) an interest or short position of an Official Trustee held in his official capacity;
- (c) an interest or short position acquired by the offeror as a result of the acceptance of a conditional offer by other shareholders in the listed corporation, being an interest subsisting while the condition of the offer remains unfulfilled; and
- (d) subject to subsection (2), an interest or short position of an intermediary licensed or registered for Type 1 or Type 2 regulated activity where the interest or short position is acquired by the intermediary when the intermediary -

(i) enters into an exchange contract in the ordinary course of its business as such an intermediary, pursuant to the instructions of a client who is a person other than a related corporation of the intermediary; and

(ii) designates the exchange contract as being for the account of a client.

(2) An intermediary shall enter into a back-to-back contract with its client on the same day as it enters into an exchange contract on the instructions of the client.

4. Prescribed interests and short positions to be disregarded for the purpose of notification by director and chief executive

The following interests and classes of interests in shares in or debentures of, and short positions and classes of short positions in shares in, a listed corporation or any associated corporation of the listed corporation, are prescribed for the purposes of section 346 of the Ordinance -

(a) an interest in shares or debentures, or short position in shares, of a person in his capacity as a trustee of any trust or as a personal representative of any estate, of which the Official Trustee is also a trustee (otherwise than as a custodian trustee) or (as the case may be) a personal representative;

- (b) an interest in shares or debentures, or short position in shares, of a person in his capacity as a trustee of, or as a beneficiary under, a trust constituted exclusively for the purposes of a recognized occupational retirement scheme; and
- (c) an interest in shares or debentures, or short position in shares, which a person is taken to have under section 344(3) of the Ordinance where the corporation referred to in that section is interested in those shares in or debentures of, or has those short positions in the shares of, the listed corporation or any associated corporation of the listed corporation, in its capacity as a trustee of any such trust as is referred to in paragraph (b).

Clerk to the Executive Council

COUNCIL CHAMBER

2002

Explanatory Note

Part XV of the Securities and Futures Ordinance (5 of 2002) ("the Ordinance") empowers the Chief Executive in Council to make regulations to prescribe anything permitted by any provision

of that Part. This Regulation prescribes certain interests and short positions which are to be disregarded, in addition to the interests or short positions listed under sections 323(1) and 346(1) of the Ordinance, for the purpose of notification by substantial shareholders and directors or chief executives of a listed corporation.



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

Annex 2

A Consultation Paper on the Securities and Futures (Disclosure of Interests - Exclusions) Regulation

《證券及期貨(披露權益 – 免除)規例》
諮詢文件

Hong Kong
May 2002

香港
2002年5月

Consultation

This consultation document invites public comments on the draft **Securities and Futures (Disclosure of Interests - Exclusions) Regulation** (“the draft Regulation”) which the Chief Executive in Council proposes to make under section 376 of the Securities and Futures Ordinance (5 of 2002) (“the Ordinance”) when it commences.

Introduction

1. Part XV of the Ordinance requires the disclosure of interests in securities by persons who are interested in 5% or more of the relevant share capital of a listed corporation (referred to in this paper as “substantial shareholders”) and by directors and chief executives of listed corporations (“directors”). Part XV builds upon the provisions of the existing Securities (Disclosure of Interests) Ordinance (Cap. 396) (the “S(DI)O”).

2. Under section 323 of the Ordinance certain interests in shares are to be disregarded for the purposes of Divisions 2 to 4 of Part XV (the principal provisions affecting substantial shareholders). Under section 346 of the Ordinance certain interests in shares are to be disregarded for the purposes of Divisions 7 to 9 of Part XV. Each of these sections provides that interests in shares, that are prescribed by regulations, are also to be disregarded.

3. Under section 376 of the Ordinance the Chief Executive in Council may make regulations covering a range of matters including prescribing interests to be disregarded. The draft Regulation (see Attachment 1) are the regulations that the Chief Executive in Council proposes to make under section 376.

4. There are controls built into the legislative system, whereby any regulations made by the Chief Executive in Council must be subject to negative vetting by the Legislative Council. The Chief Executive in Council first wishes to conduct a public consultation on the terms of the draft Regulation. The SFC therefore now releases the draft Regulation for public consultation.

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

6. The SFC invites interested parties to submit written comments on the draft Regulation or to comment on related matters that might have a significant impact upon the draft Regulation **no later than 8th 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 Regulation.

The draft Regulation

7. Like Part XV of the Ordinance the existing S(DI)O contains provisions permitting the Chief Executive in Council to prescribe interests to be disregarded by Regulations and the existing Securities (Disclosure of Interests)(Exclusions) Regulations (“the existing Regulations”) list a number of interests to be disregarded. The draft Regulation have been prepared having regard to the matters contained in the existing Regulations but reflect the conclusions set out in a Consultation Paper dated June 1998 and a Consultations Conclusions Paper dated April 1999.

8. The June 1998 Consultation Paper proposed that Regulation 3(1)(c), that disregards interests held by trust companies and their subsidiaries that are locally incorporated, should also be removed. The rationale was to promote market transparency, meet international standards and create a level playing field amongst trust companies. (see pages 34 to 37 of the Consultation Paper and pages 31 to 37 of the Consultation Conclusions Paper dated April 1999).

9. The SFC also proposed that the existing Regulation 3(2), that disregards interests held by an investment manager in certain circumstances, be removed. In practice, the scope of Regulation 3(2) is very limited. Since an interest in shares seldom arises exclusively because of an investment manager’s power to dispose of shares, the exemption is very rarely used. Investment management agreements usually contain provisions which give managers discretion to vote at general meetings (if clients fail to give instructions), take up rights issues, elect for scrip dividends or take certain other actions. The SFC decided that the existing exemption did not serve any useful purpose as few investment managers could in practice take advantage of it. Its removal would also level the playing field among investment managers.

10. The removal of these exemptions should not be viewed in isolation. There have also been significant changes to the disclosure regime in Part XV itself which include an enlargement of the exemption given to trustees and custodians under section 323(1)(b) and (c), section 346(1)(c), and the creation of an exemption from aggregation of interests of investment managers, trustees and custodians under section 316(5) of the Ordinance.

11. Regulation 4(1)(f) of the existing Regulations has not been replicated in the draft Regulation it appears to serve no purpose. We cannot think of any situation where an interest arises solely on account of a limitation on disposal. The acquisition of those shares would not be exempt because the interest does not arise solely because of a limitation on disposal. If a director can’t dispose of the shares we can’t see why such an interest should give rise to any obligation to file a notification.

12. Regulation 4(2) and (3) of the existing Regulations have not been replicated in the draft Regulation as they also appear to serve no purpose - there being no obligation in Part XV on directors to give notification of interests in shares and debentures to a corporation other than a listed corporation (and the Exchange Company).

New Policy Initiatives

13. No new policy changes have been incorporated into the draft Regulation beyond those proposed in the Consultation Paper of June 1998 and the Conclusions Paper of April 1999 and mentioned above.

Other matters

14. Please note that the names of the commentators and the contents of their submissions may be published on the SFC web site 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.

15. 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.

16. Written comments may be sent -

By mail to: SFC (Disclosure of Interests)
12/F, Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

By fax to: (852) 2868 0252

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

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

17. The draft Regulation 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, Notice, 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.

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.

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

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SECURITIES AND FUTURES (DISCLOSURE OF INTERESTS - EXCLUSIONS) REGULATION

(Made by the Chief Executive in Council under
section 376(1) of the Securities and
Futures Ordinance (5 of 2002))

1. Commencement

This Regulation shall come into operation on the day on which Part XV of the Securities and Futures Ordinance (5 of 2002) comes into operation.

2. Interpretation

In this Regulation, unless the context otherwise requires -
"conditional offer" (有條件要約) means an offer for shares of a corporation made to the holders of all the shares or all the shares of a particular class other than (in either case) shares held by or on behalf of -

- (a) the offeror;
- (b) the offeror's holding company, the offeror's subsidiary or a subsidiary of the offeror's holding company; or
- (c) any person who has agreed that the offer should not be made in respect of shares he holds,

and subject to the condition that acceptances are received in respect of such proportion of the shares for which the offer

is made as specified in, or ascertained by reference to, the terms of the offer;

"recognized occupational retirement scheme" (認可退休計劃) has the meaning assigned to it by section 2(1) of the Inland Revenue Ordinance (Cap. 112).

3. Prescribed interests and short positions

(1) The following interests and classes of interest are prescribed for the purposes of section 323(1)(j) of the Ordinance

-

- (a) interests of a person in his capacity as beneficiary under a trust constituted exclusively for the purposes of a recognized occupational retirement scheme;
- (b) interests of the Official Trustee;
- (c) interests acquired as a result of the acceptance of a conditional offer being interests subsisting while the condition of the offer remains unfulfilled.

(2) The following interests and classes of interest, or short positions and classes of short position, are prescribed for the purposes of section 346(1)(e) of the Ordinance -

- (a) interests or short positions, in shares or debentures, of any person in his capacity as trustee or personal representative of any trust or estate of which the Official Trustee is also a

- trustee (otherwise than as custodian trustee) or, as the case may be, a personal representative;
- (b) interests or short positions, in shares or debentures, of a person in his capacity as trustee of, or as beneficiary under, a trust constituted exclusively for the purposes of a recognized occupational retirement scheme;
- (c) interests in shares or debentures, or short positions in shares, which a person is taken to have under section 344(3) of the Ordinance where the corporation referred to in that section is interested in those shares or debentures, or has those short positions, in its capacity as trustee of any such trust as is mentioned in paragraph (b).

Clerk to the Executive Council

COUNCIL CHAMBER

2002

Explanatory Note

Part XV of the Securities and Futures Ordinance (5 of 2002)(principal Ordinance) empowers the Chief Executive in Council to prescribe by regulations any exclusions from the requirement to give notification under that Part. This Regulation prescribes

exclusions in relation to certain interests and short positions for the purposes of sections 323(1)(j) and 346(1)(e) in Part XV of the principal Ordinance.



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

Annex 3

Consultation Conclusions on the draft Securities and Futures (Disclosure of Interests - Exclusions) Regulation

《證券及期貨(披露權益 - 免除)規例》草擬本諮詢總結

Hong Kong
July 2002

香港
2002年7月

INTRODUCTION

1. On 16th May 2002, the Securities and Futures Commission ("SFC") issued a consultation paper ("the Consultation Paper") to solicit comments on the draft **Securities and Futures (Disclosure of Interests - Exclusions) Regulation** ("the draft Regulation").
2. The draft Regulation creates certain exclusions from the disclosure obligations that may arise when a person acquires, or ceases to have, or there is a change in the nature of a person's interest in shares of a listed corporation under Part XV of the Securities and Futures Ordinance (5 of 2002) ("SFO").
3. The consultation exercise ended on 8th June 2002 but the SFC has subsequently conducted further consultation with the persons who submitted comments on the draft Regulation and proposes an enlargement of the draft Regulation in response to these submissions.
4. The purpose of this document is to provide interested persons with an analysis of the comments raised during the consultation exercise and the rationale for the SFC's conclusions. It is advisable to read this document in conjunction with the Consultation Paper itself.

PUBLIC CONSULTATION

Consultation process

5. In addition to the public announcement inviting comments, the Consultation Paper was distributed to various interested parties and professional bodies. The Consultation Paper and the draft Regulation were posted on the website of the SFC and distributed to all registrants through FinNet.
6. A single submission was received on 7 June 2002 from Linklaters & Alliance for a group of eight financial institutions -
 - (a) Credit Suisse First Boston (Hong Kong) Ltd
 - (b) Goldman Sachs (Asia) L.L.C.
 - (c) Morgan Stanley Dean Witter Asia Ltd
 - (d) Salomon Smith Barney Hong Kong Ltd
 - (e) Deutsche Securities Asia Ltd
 - (f) J.P.Morgan
 - (g) Merrill Lynch (Asia Pacific) Ltd.
 - (h) UBS Warburg.
7. No comments were made on the text of the exemptions contained in the draft Regulation. However, Linklaters & Alliance called for a widening of the exemptions provided in the draft Regulation.

Consultation Conclusion

8. Having regard to the comments received the SFC proposes to create an additional exemption for intermediaries who enter into transactions in Exchange traded stock futures contracts and stock options contracts for their clients. The SFC considers that the exemption can be compared with the existing exemption, in section 323(1)(i) of the SFO, for an intermediary who acquires an interest in shares of a listed corporation as an agent for a client. The exemption can be justified on a similar basis – that the intermediary does not acquire an economic interest in the underlying shares if the intermediary, for all intents and purposes, entered into the futures or options contract for a client.
9. The changes to the draft Regulation extend the exemptions with a view to minimizing unnecessary disclosures, whilst maintaining adequate transparency in the disclosure regime to protect the interests of investors. The draft Regulation has also been further refined to better reflect the policy intention and to improve drafting.

SUMMARY OF COMMENTS AND SFC'S RESPONSES

10. A summary of the comments received together with the SFC's responses is set out in the Appendix.

Summary of Comments Received on Securities and Futures (Disclosure of Interests –Exclusions) Regulation

	Section No.	Respondent’s comments	SFC’s response
1.	Request for new exemption (Intermediary interest in stock option and futures.)	<p>[Linklaters & Alliance]</p> <p>Where a dealer buys or sells shares for its client, it is arguable that the dealer acquires an “interest” in the shares pending settlement. For the avoidance of doubt, an exemption has been introduced in Section 323(1)(i) of the FSO to exempt the dealer from any duty of disclosure in such circumstances.</p> <p>However, this exemption will not apply where a dealer which is an Exchange participant is entering into transactions in Exchange-traded stock options or stock futures relating to underlying shares in a Hong Kong listed corporation. In summary, when an Exchange participant opens a position for a client, this involves two contracts, one buy and a matching sell, being entered into:</p> <ul style="list-style-type: none"> • between the Exchange participant and (by novation) the clearing house, and • between the Exchange participant and the client. <p>Under the Exchange Rules, all transactions effected by an Exchange participant in options and futures will be clearly designated as either being for the account of a client or for the Exchange participant’s own account. Where transactions are effected for clients, the Exchange participant has no “economic” interest in the positions created. The role of the dealer is analogous to that of an agency broker in the cash market, even though (because of the way in which the clearing system operates) the transactions are effected as back to back principal positions.</p> <p>We therefore propose an exemption to enable an Exchange participant to disregard for disclosure purposes interests and</p>	<p>Viewed strictly, the position of an intermediary who enters into a stock futures contract or a stock options contract is different from the position of an intermediary who buys shares as agent for his client. An intermediary who enters into a stock futures contract, or a stock options contract, is (1) acting as principal rather than as agent; and (2) will hold the position until the end of the contract – up to three months, as opposed to 3 days in the case of the exemption under section 323(1)(i) of the SFO.</p> <p>Nevertheless, where in reality the exchange participant is entering in the transaction solely for a client, and has no real economic interest in the underlying shares, we agree that the interest, or short position, of the exchange participant should be disregarded. In the same way that the exemption under section 323(1)(i) of the SFO is not available for contracts entered into for clients that are related corporations, we propose that the new exclusion should be similarly limited. The new provisions appear in clause 3(1)(d) of the draft Regulation.</p>

	Section No.	Respondent's comments	SFC's response
		short positions arising from transactions effected, for the account of clients, in stock options and stock futures traded on a recognized exchange company in Hong Kong.	
2.	Request for new exemption (Client facilitation activities)	<p>[Linklaters & Alliance]</p> <p>When a dealer receives an order from a client to buy or sell Hong Kong shares, or a basket of shares, the dealer may commit to achieve a particular standard of execution (for example, no worse than the value-weighted average price for transactions in the market on the trading day). While the dealer will effect the purchases or sales as the client's agent, if this does not achieve the agreed execution price, part of the trade will be rebooked as a principal trade, to achieve that price. Similarly, a dealer may buy a block of shares from a client at an agreed price for immediate on-sale into the market, or may "go short" in order to fill an order from a client or from the market (for example, when acting as a liquidity provider in respect of structured products).</p> <p>To the extent that the dealer is not acting as agent, the "agency brokerage" exemption in Section 323(1)(i) will not apply. However, we consider that an equivalent exemption from Part XV should be available in respect of interests/short positions temporarily arising in the course of effecting a transaction resulting from the instructions of a client, where the transaction is effected in the ordinary course of the dealer's business, and the interest or short position is held for no more than 3 business days and ceases on settlement of the transaction with the client.</p>	<p>In the circumstances outlined by Linklaters & Alliance, the dealer is not really acting as agent for a client but is acquiring an economic interest in the shares itself. We are concerned that this will unduly enlarge the "agency exemption" in s. 323(1)(i). In practice, it would not be possible to distinguish between a situation where the dealer is intending to buy/sell for a client and the situation where the dealer is buying on his own behalf.</p>
3.	Request for new exemption (IPOs-related transactions)	<p>[Linklaters & Alliance]</p> <p>In relation to Initial Public Offerings ("IPOs") and follow-on offerings Linklaters & Alliance ask for exemptions for, effectively, all transactions in which managers might be engaged. Specifically they sought an exemption from Part XV for interests/short positions of the managers of an issue of securities potentially arising as a result of activities carried out for or on behalf of the syndicate of managers, during the period of 30 days after the date of the offering. The exemption would cover :</p>	<ol style="list-style-type: none"> 1. We believe that the difficulties of compliance are overstated. Managers who undertake underwriting commitments, borrowing stock and carrying out stabilising activities must know their positions. The requirement for completing a disclosure form at the end of each trading day will not be unduly onerous and we do not think that this is a sound reason for creating an exemption. 2. In all disclosure regimes there are certain elements of double counting but despite this it is

	Section No.	Respondent's comments	SFC's response
		<ul style="list-style-type: none"> • Underwriting commitments • Greenshoe options (15% over-allotment option); • Agreements among managers; • Stock borrowing to cover over-allocations; • Stabilising activities, (i.e. purchases within certain price levels fixed by the Securities and Futures (Price Stabilising) Rules) • Ancillary stabilising activities (under the draft Stabilising Rules this would include over-allotments, short selling and exercise of options to purchase shares) <p>In support of their request Linklaters submitted that –</p> <ol style="list-style-type: none"> 1. To report the interests/short positions of the syndicate members prior to the offering taking place, and during the stabilisation period, could be very onerous. 2. There could be “double counting” among the various syndicate members, and the resulting information could be misleading. 3. Disclosures under Part XV could make it more difficult to carry out legitimate stabilising activities and undermine the maintenance of an orderly market. 	<p>not difficult for analysts to grasp the full picture. In contrast, if substantial information were not disclosed, it would be impossible to form an opinion on the full picture. The non-disclosure of transactions surrounding an IPO could therefore undermine market transparency.</p> <p>3. We do not think that secrecy is a precondition for the success of stabilising action. The stabilising effect comes from the purchases and sales themselves – and the immediate market response. It is worthwhile to note that the disclosures are only made 3 business days after the day of the transaction and the Exchange publishes the following day. Hence a trade on Monday will not be made public until Friday. We do not think that disclosure of stabilising activities will undermine the maintenance of an orderly market.</p> <p>The new disclosure regime under Part XV of the SFO will be reviewed at an appropriate time in the light of its actual implementation. These issues could be revisited in the light of the experience gained.</p>