

**LegCo Panel on Financial Affairs**

**Major issues raised at the meetings  
on 31 July, 16 September and 20 September 2002**

<p align="center"><b>Issues raised at Panel meetings</b></p>	<p align="center"><b>Relevant recommendations (or remarks) in the report of the Panel of Inquiry on the Penny Stocks Incident</b> (see note 1)</p>	<p align="center"><b>Covered by review of Expert Group</b> (see note 2)</p>
<p><b>1. Government's role in the "three-tiered" regulatory framework</b></p> <ul style="list-style-type: none"> <li>- role of Government in the formulation, promulgation and implementation of proposals relating to the Listing Rules</li> <li>- Government as a “watchdog of the watchdog” or as a “facilitator and co-ordinator”</li> </ul>	<p>The Government should clearly reposition itself as a facilitator and a co-ordinator and not as a regulator, leaving the market forces to work within the broad policy framework and without political interference. The Government must communicate its role clearly to the industry and investing public to avoid false and unrealistic expectation. (para. 14.22)</p> <p>The Government should keep free from the day-to-day regulatory functions, focus on keeping the regulatory framework under review, ensure sufficient checks and balances, act as co-ordinator, keep reserve power for exercise in emergencies, and provide sound environment for the development of the financial market. (para. 3.14)</p>	<p align="center">Yes</p>

**Notes**

1. In its paper for the Panel meeting on 16 September 2002 (LC Paper No. CB(1)2537/01-02(02)), the Administration has pledged to study, together with the Securities and Futures Commission (SFC) and the Hong Kong Exchanges and Clearing Limited (HKEx), the findings and recommendations of the Inquiry Panel in detail, with a view to mapping out the implementation plan in a co-ordinated manner.
2. The terms of reference of the Expert Group to Review the Operation of the Securities and Futures Market Regulatory Structure are set out in **Appendix**. They are promulgated by the Administration through a press release on 26 September 2002, which were issued to Members vide LC Paper No. CB(1)2603/01-02 on the same day.

<b>Issues raised at Panel meetings</b>	<b>Relevant recommendations (or remarks) in the report of the Panel of Inquiry on the Penny Stocks Incident</b>	<b>Covered by review of Expert Group</b>
<p><b>2. Functions of and working relationship between SFC and HKEx</b></p> <ul style="list-style-type: none"><li>- roles and functions of SFC and HKEx in the formulation, promulgation and implementation of proposals relating to the Listing Rules</li><li>- extent of involvement and influence of SFC in the above processes</li></ul>	<p>HKEx and SFC should further clarify their roles in the Memorandum of Understanding Governing Listing Matters signed between SFC and HKEx on 6 March 2000, setting out clear provisions on their functions and responsibilities and the procedures for processing consultation papers and amendments to the Listing Rules. (para. 14.19)</p> <p>HKEx and SFC should strengthen the current liaison mechanism by introducing a new high level body. Both organizations should feel at liberty to propose topics for discussion. This should allow periodic review of systemic and policy issues. This body would be in addition to the working level meetings on operational issues. (para. 14.19)</p> <p>HKEx and SFC should clearly identify the areas for joint consultations by SFC and HKEx. (para. 14.19)</p>	<p>Yes</p>

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<p><b>3. Role and functions of the Listing Committee of HKEx in the regulatory framework</b></p> <ul style="list-style-type: none"> <li>- relationship between the Listing Committee and the Board of Directors of HKEx</li> <li>- relationship between the Listing Committee and SFC</li> </ul>	<p>The authorities should review how best to redefine the roles and functions over listing matters with a view to increasing effectiveness, efficiency, clarity, fairness and credibility of the regulatory system. The review should have regard to the suggestion by market practitioners and financial analysts that if a Listing Committee is to be retained, it cannot be housed under HKEx. Within the current structure, the only entity under which it can be accommodated is SFC. (para. 14.21)</p>	<p style="text-align: center;">Yes</p>
<p><b>4. Mechanisms to assess market reaction and to ensure adequate communication among the Government, SFC and HKEx over market sensitive matters</b></p>	<p>HKEx should engage other channels apart from the media to gauge market views and disseminate information to the market (para. 11.43)</p> <p>In seeking the approval of the Listing Committee for the issue of consultation papers, HKEx should provide its analysis of the likely effect of the proposals, particularly the effect on the investing public, in sufficient detail to enable the Committee to decide whether the consultation papers should be published and if so, on what terms. (para. 14.15)</p> <p>The assessment by HKEx of the likely market reaction to its consultation papers should be brought to the attention of both SFC and the Bureau at the earliest opportunity. (para. 14.16)</p>	<p style="text-align: center;">?</p> <p>(The Administration's confirmation is awaited.)</p>

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<p><b>5. The consultative machinery adopted by SFC and HKEx for introducing changes to Listing Rules</b></p> <ul style="list-style-type: none"> <li>- sounding out with the industry and market participants in the course of mapping out proposals for consultation</li> <li>- adequacy and effectiveness of the existing consultative networks of SFC and HKEx</li> </ul>	<p>The authorities should :</p> <ul style="list-style-type: none"> <li>- make the most constructive and efficient use of the existing consultative network;</li> <li>- expand the network where possible to increase its efficiency;</li> <li>- ensure that the network is broadly representative; and</li> <li>- engage the consultative network at an early stage in discussing concept and framework and in formulating proposals.</li> </ul> <p><i>(para.14.7) (Further details of these recommendations are set out in paras. 14.8 to 14.14)</i></p>	<p style="text-align: center;">?</p> <p>(The Administration's confirmation is awaited.)</p>

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<p><b>6. Assessment of responsibilities under the Accountability System</b></p> <ul style="list-style-type: none"> <li>- the bases for assessment of responsibilities of concerned parties/persons in the incident</li> <li>- the manner in which the Inquiry Panel assessed the responsibilities of concerned parties/persons in the incident</li> </ul>	<p>The Inquiry Panel has suggested four categories of responsibilities, i.e. <b>policy responsibility, executive responsibility, systemic responsibility and personnel responsibility</b> for deliberation of the issue of responsibilities in this incident. (paras. 12.16 to 12.20)</p> <p>The Panel has stressed that its deliberation in this respect is subject to the caveat about its terms of reference, the exigencies of time and the relative lack of expertise. (para. 12.10)</p> <p>“This inquiry should not be taken as a fault finding exercise. We re-iterate that we have come to many of our views with the substantial benefit of hindsight, so that although we too were working against the clock, we had the good fortune of being able to reflect and discuss, to enquire and to seek, without being under the sort of practical pressures which both SFC and HKEx, and to a lesser extent the Bureau, must all have been under.” (para. 15.4)</p>	<p style="text-align: center;">No</p>

<b>Issues raised at Panel meetings</b>	<b>Relevant recommendations (or remarks) in the report of the Panel of Inquiry on the Penny Stocks Incident</b>	<b>Covered by review of Expert Group</b>
<b>7. Compensation for investors and other parties who have sustained financial losses in the incident</b>  - whether there is a case for seeking recompense for the financial losses sustained by investors in the incident  - the channels available for making claims	<i>(not covered in the report)</i>	No

**Expert Group to Review the Operation of the  
Securities and Futures Market Regulatory Structure**

Terms of Reference

1. With a view to increasing effectiveness, efficiency, clarity, fairness and credibility of the regulatory system for the securities and futures market of Hong Kong, and ensuring the integrity of the market and the proper protection of the investing public, to:
  - (a) review the roles and functions of the Government, the Securities and Futures Commission, and the Hong Kong Exchanges and Clearing Limited and its subsidiaries over matters relating to listing of securities and issuers with listed securities; and
  - (b) review the operation of the regulatory structure as regards listing matters;
  - (c) review the line of communications among the Government, the Securities and Futures Commission and the Hong Kong Exchanges and Clearing Limited; and
  - (d) recommend changes and improvements relating to issues in (a) to (c) above where appropriate.
  
2. In conducting the review, the Expert Group shall have regard to:
  - (a) the need to maintain the status of Hong Kong as an international financial centre;
  - (b) developments in the local and international securities and futures markets;
  - (c) the competitiveness of Hong Kong as a centre for listing companies from the Mainland, Asian time zone and global capital markets;
  - (d) the diversity of issuer and investor bases of the Hong Kong securities and futures market; and

- (e) the outcome of the deliberations in the Legislative Council in respect of the Securities and Futures Ordinance (Cap. 571); and
- (f) the findings and recommendations of the Panel of Inquiry on the Penny Stocks Incident;

3. The Expert Group should also:

- (a) invite submissions from interested parties and the public, including but not limited to representatives from issuers, stock brokers and investing public, Legislative Councillors and the Standing Committee on Company Law Reform;
- (b) consider the regulatory structures and systems in other major markets; and
- (c) use its best endeavours to submit its report before the end of March 2003.

*Source:* Press release titled "FS appoints Expert Group to Review the Operation of the Securities and Futures Market Regulatory Structure issued by the Administration on 26 September 2002