

**立法會**  
***Legislative Council***

LC Paper No. CB(1)2392/02-03  
(These minutes have been seen  
by the Administration)

Ref : CB1/PL/FA/1

**Panel on Financial Affairs**

**Minutes of meeting**  
**held on Monday, 7 July 2003 at 10:45 am**  
**in the Chamber of the Legislative Council Building**

**Members present** : Hon Ambrose LAU Hon-chuen, GBS, JP (Chairman)  
Hon Henry WU King-cheong, BBS, JP (Deputy Chairman)  
Hon Kenneth TING Woo-shou, JP  
Hon James TIEN Pei-chun, GBS, JP  
Hon Albert HO Chun-yan  
Hon LEE Cheuk-yan  
Dr Hon Eric LI Ka-cheung, GBS, JP  
Dr Hon David LI Kwok-po, GBS, JP  
Hon NG Leung-sing, JP  
Hon Bernard CHAN, JP  
Hon CHAN Kam-lam, JP  
Hon SIN Chung-kai  
Dr Hon Philip WONG Yu-hong, GBS  
Hon Jasper TSANG Yok-sing, GBS, JP  
Hon MA Fung-kwok, JP

**Non-Panel member attending** : Dr Hon David CHU Yu-lin, JP

**Members absent** : Hon James TO Kun-sun  
Hon Emily LAU Wai-hing, JP  
Hon Abraham SHEK Lai-him, JP

**Public officers  
attending**

**: Agenda Item IV**

Miss Susie HO  
Deputy Secretary for Financial Services and the Treasury  
(Financial Services) 2

Mr G W E JONES, JP  
Registrar of Companies

Mr T C HO  
Business Manager  
Companies Registry

Mr Felix S P LAM  
Development Manager  
Companies Registry

**Agenda Item V**

Mr Tony MILLER  
Permanent Secretary for Financial Services and  
the Treasury (Financial Services)

Ms Kinnie WONG  
Principal Assistant Secretary for Financial Services and  
the Treasury (Financial Services)

**Attendance by  
invitation**

**: Agenda Item V**

Mrs Alexa LAM  
Executive Director, Intermediaries and Investment Products  
Securities and Futures Commission

Mr Stephen PO  
Senior Director, Intermediaries Supervision  
Intermediaries & Investment Products  
(Planning and Resources)  
Securities and Futures Commission

**Clerk in attendance :** Miss Salumi CHAN  
Chief Assistant Secretary (1)5

**Staff in attendance :** Ms Pauline NG  
Assistant Secretary General 1

Ms Rosalind MA  
Senior Assistant Secretary (1)8

Mr Joey LO  
Senior Assistant Secretary(1)4 (Acting)

Ms May LEUNG  
Legislative Assistant

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## **I. Confirmation of minutes of meetings**

The following minutes of meetings were confirmed:

- (a) Minutes of meeting on 7 April 2003 (LC Paper No. CB(1)2046/02-03);
- (b) Minutes of special meeting on 23 April 2003 (LC Paper No. CB(1)2092/02-03);
- (c) Revised minutes of special meeting on 28 April 2003 (LC Paper No. CB(1)2047/02-03);
- (d) Minutes of meeting on 5 May 2003 (LC Paper No. CB(1)2017/02-03);  
and
- (e) Minutes of special meeting on 12 May 2003 (LC Paper No. CB(1)2123/02-03).

## **II. Information papers issued since last meeting**

2. Members noted the following information papers issued since the last meeting -

- (a) Letter dated 29 May 2003 from the Commissioner of Insurance on the “Proposal to review the Institutional Set-up of the Office of the Commissioner of Insurance” (LC Paper No. CB(1)1881/02-03);

- (b) Information note on the “Enhancement of Automated Communication, Technical Information and Operations Network System for Architectural Services Department” (LC Paper No. CB(1)1945/02-03); and
  - (c) Exchange of letters between the Financial Secretary and the Monetary Authority on the functions and responsibilities in monetary and financial affairs (LC Paper No. CB(1)2111/02-03).
3. The Chairman informed members that Ms Emily LAU proposed that the item in paragraph 2(c) above be discussed at a meeting of the Panel. Members agreed that arrangements for discussion of the item be made in the next legislative session.

### III. Date of next meeting and items for discussion

(LC Paper No. CB(1)2109/02-03(01) — List of outstanding items for discussion

LC Paper No. CB(1)2109/02-03(02) — List of follow-up actions)

4. The Chairman advised that pursuant to the Panel’s decision at its meeting on 2 June 2003, a special meeting would be held in July to further discuss the governance of the Hong Kong Monetary Authority (HKMA), and that the Financial Secretary (FS) and the Chief Executive of HKMA would be invited to the meeting. Members agreed that the special meeting be scheduled for Thursday, 31 July 2003 from 11:30 am to 1:00 pm.

*(Post-meeting note: Following the resignation of Mr Antony LEUNG on 16 July, the Chairman, after consulting members of the Panel, agreed to the suggestion of Mr Stephen IP, Acting FS, that the special meeting scheduled for 31 July be postponed until after the new FS was in post.)*

### IV. Progress update on the Strategic Change Plan of the Companies Registry

(LC Paper No. CB(1)2109/02-03(03) — Information paper provided by the Administration)

#### Briefing by the Administration

5. At the Chairman’s invitation, the Registrar of Companies (RC) advised that the paper provided by the Administration aimed to brief members on the latest position regarding the implementation of the Strategic Change Plan (SCP) of the Companies Registry (CR) and the proposals to amend statutory fees to cater for the new search services upon implementation of the Integrated Companies Registry Information System (ICRIS). He pointed out that in 2002, CR had awarded tenders

for the ICRIS development project and the conversion services project, and that these projects were making good progress. It was expected that Phase One of ICRIS would be implemented at the end of November 2003. RC also pointed out that under ICRIS, searches of imaged records would be conducted on a “per document” basis as opposed to the existing “per microfiche” basis. To cater for the new search services under ICRIS, the Administration proposed to amend the search fees in Part V of the Eighth Schedule to the Companies Ordinance (Cap. 32). Details of the proposals were set out in Enclosure 4 to the paper.

6. The Development Manager, CR (DM/CR) then gave a power-point presentation on the search services currently provided by CR and those to be provided under ICRIS. He pointed out that there were three categories of search services currently available, namely, database search at CR’s premises, search on microfilmed documents and CR on-line public search system. The current search services would be completely replaced by ICRIS search services, which would be available on-site during office hours and could be accessed through the internet 24 hours a day. DM/CR also briefed members on the search products available to customers free of charge and those provided with search fees payable, as well as the benefits of ICRIS.

*(Post-meeting note: The power-point presentation material provided by the Administration was issued to members vide LC Paper No. CB(1)2195/02-03 on 10 July 2003.)*

## Discussion

### *Charging proposals for the search services under ICRIS*

7. Mr Kenneth TING supported the implementation of ICRIS to facilitate users in searching company records kept by CR. He enquired about the difference in the level of search fees payable before and after the implementation of ICRIS. Referring members to Enclosure 4 to the paper, RC pointed out that CR aimed to achieve an income level under ICRIS that was more or less the same as the existing level, i.e. the “revenue neutral” approach. On the basis of this principle, CR proposed no changes to the fee levels for the existing search services which would continue to be available under ICRIS. For the new search services to be introduced under ICRIS, the fees would be set on the basis that customers on average would not pay more to CR than as present. The Business Manager, CR (BM/CR) added that as reflected in the summary of the charging proposals set out in Enclosure 5 to the paper, the fees for a majority of the service items would remain unchanged.

8. In response to Mr Kenneth TING’s further enquiry, BM/CR advised that free services for company name search, document index search and disqualification order index search would be provided to users through the internet upon the implementation of Phase One of ICRIS at the end of November 2003.

9. Whilst supporting the objective of SCP to establish a fully computerized CR for providing fast, cost-effective, user-friendly and high quality services to customers, Mr Henry WU considered that computerization should result in lower costs, and therefore lower fees. RC advised that customers would be paying more or less the same level of fees before and after the implementation of ICRIS. Referring to paragraph 5(a) of Enclosure 4 to the paper, he quoted an example that non-ICRIS subscribers searching on the internet for downloading an imaged record would be required to pay \$21 per search on average. After deducting service charges payable to financial institutions for electronic payment services (about \$1), the net revenue should be close to the existing fee of \$20 for inspecting the documents in the form of a microfiche. BM/CR added that CR had consulted its Customer Liaison Group (CLG) on the charging proposals for the ICRIS search services in June 2003. Members of CLG generally considered the charging proposals to be fair and reasonable. Nevertheless, CR had undertaken to review the ICRIS charging structure after implementation of the system and explore whether there was room for fee reduction. CR would also explore the commercial viability of introducing new services such as “document package” search to meet the needs of the high usage customers. Noting that CLG comprised representatives of CR’s major customers, Mr Henry WU was concerned whether representatives of small and medium enterprises (SME) had been consulted by CR. RC advised that there was a representative of SME customers in CLG.

10. In reply to Mr Henry WU’s enquiry, BM/CR explained that an imaged record was in fact a document which might have several images and the fees for downloading an imaged record would be charged on a “per document” basis.

#### *On-site search services under ICRIS*

11. Noting that CR intended to provide on-site searchers with only hard copies of documents after the implementation of ICRIS, Mr Henry WU asked for the reasons for the proposal. RC advised that the result of a survey conducted by CR suggested that majority of on-site searchers needed hard copies of the relevant documents. While it was technically feasible to allow on-site searchers to have on-line viewing of the imaged records at CR, this would not be cost-effective and might give rise to considerable operational problems, such as how to control their on-line viewing time and how to avoid possible security problems when they entered their personal identification numbers and account numbers for viewing and downloading of imaged records at CR which was a public area. It was considered more appropriate to provide the on-site searchers with hard copies only. DM/CR added that the average size of the images of a document was about 200 Kb and this very large document size made it not viable for customers to copy the images of several documents onto a floppy disk. Besides, according to the CR’s system developer, it was not advisable for CR to allow customers to use the floppy drives because this might create serious system security problems. Consequently, he was of the view that providing hard copies to on-site searchers was the most appropriate option.

12. In response to Mr Henry WU's enquiry, DM/CR said that 25 terminals would be provided at CR for on-site searchers after the implementation of ICRIS as compared with 55 terminals provided at present. As ICRIS would facilitate electronic service delivery to users, the need for them to visit CR in person should be reduced.

**V. Proposed consultation on Review of the Financial Regulatory Framework for stockbrokers**

(LC Paper No. CB(1)2109/02-03(04) — Information paper provided by the Administration)

Briefing on the Review of Financial Regulatory Framework

13. At the Chairman's invitation, the Permanent Secretary for Financial Services and the Treasury (Financial Services) (PSFS) briefed members on the background of the Review on the Financial Regulatory Framework for Securities Dealers and Securities Margin Financing Providers (the Review) conducted by the Working Group on the Review of the Financial Regulatory Framework for Intermediaries (the Working Group). He pointed out that when the Securities and Futures Commission (SFC) briefed the Panel on 6 May 2002 on its interim measures under the then Financial Resources Rules (FRR) for reducing the financial risk posed to securities margin financing providers and their clients, SFC had undertaken to review the regulatory framework for managing brokers' financial risks in other securities market jurisdictions and the adequacy of the existing regulatory framework in Hong Kong. The Administration had reported progress to the Legislative Council (LegCo) in the context of the FRR made under the Securities and Futures Ordinance in September and December 2002 that SFC had formed the Working Group to take forward the Review. The Executive Director of SFC would update members on the progress of the Review at this meeting; and the Government and the SFC would wish to seek Members' views on the broad direction.

14. PSFS highlighted two points on Government policy. First, the Government attached primary importance to investor protection, and to minimizing systemic risks. The objective that the Government wished to achieve through the SFC was to put in place effective and balanced measures to address the risks facing both practitioners and investors in the securities market. Second, the Government wished to encourage the healthy development of the industry. It had been and remained Government policy that the regulatory regime should be as light as possible, and consistent with the principles of prudence and equity. The Government trusted that the measures eventually devised by SFC in consultation with the industry would be balanced and targeted, and would thus avoid overburdening responsible practitioners. The Government had confidence in SFC's ability to achieve these objectives.

15. At the Chairman's invitation, Mrs Alexa LAM, the Executive Director of SFC, briefed members on the progress of the Review. She said that the Working Group had identified two major reasons for brokers default under the current market structure and business model: integrity risk (misappropriation of client assets) and risky margin lending practices and pooling and re-pledging client collateral. In the last 15 months, there had been nine cases of misappropriation of client assets with total loss amounting to \$186.6 million. As regards margin financing and pooling risks, there were no restrictions on brokers pooling and re-pledging client collateral. If a broker failed, the loss to investors could be huge. The failure of CA Pacific was a good example. Moreover, current rules on financial resources of brokers were old rules. The current liquid capital level of \$3 million had been set in 1993 when the FRR was first introduced and the current required paid-up capital level of \$5 million (agency brokers) had been in place before SFC came into existence. Market conditions and risk levels had substantially changed since then but the required capital levels remained the same. It was therefore timely to conduct a review and introduce changes to protect investors and the integrity of the market. Mrs LAM also highlighted the following findings and recommendations of the Working Group:

- (a) After studying models adopted in the Mainland, Singapore and Taiwan, the Working Group concluded that it was international practice to require brokers to be well capitalized.
- (b) The capital level of brokers should be commensurate with their risks. Capital level should be lower for brokers who did not hold client assets (i.e. no integrity risks) and higher for those who did. The Working Group would continue to examine whether the present capital level should be increased. It recognized that if capital levels were increased for brokers holding client assets, there should be a solution for existing brokers who could not meet the new capital requirements. The Working Group would explore possible options, including the new Investor Participation Account (IP Account) model being developed by the Hong Kong Exchanges and Clearing Limited (HKEx).
- (c) On pooling and re-pledging client collateral, the Working Group agreed that it was international best practice to segregate non-borrowing margin client collateral. However, the Working Group could not reach a consensus on a workable model for segregation.
- (d) The Working Group had formed no definitive view on the capital level for share margin financing providers. However, there was broad consensus among members of the Working Group that the present capital requirements for share margin financing providers engaged in re-pledging should be strengthened and that the Working Group should continue to examine the following interim measures:

- Giving SFC a reserve power to require individual firms to reduce their risks (e.g. by retaining higher levels of shareholders equity in the firm itself);
- Tightening FRR to curb risky margin lending practices (e.g. imposing capital charge on the portion of a margin loan exceeding a prudent level).

- (e) Margin clients should be better informed regarding the re-pledging of the securities collateral. SFC should be requested to step up investor education on the risks of pooling and re-pledging.

16. Mrs Alex LAM said that SFC fully understood that the securities industry was undergoing a period of difficulty and stress as market conditions continued to change. However, under the Securities and Futures Ordinance (Cap. 571), the SFC had statutory obligation to put the interest of investors as priority. It was also in the industry's long term interest to protect investors. As such, SFC would work together with the Working Group, the industry, LegCo and the Administration to find a suitable solution as soon as possible.

*(Post-meeting note: The speaking notes of the Executive Director of SFC were circulated to members vide LC Paper No. CB(1)2176/02-03 on 8 July 2003.)*

## Discussion

### *Impact of the Review on the securities industry*

17. Mr Henry WU expressed the concern of the securities industry over the Review. While recognizing the need for reviewing the current regulatory framework for brokers in order to strengthen investor protection, the industry was concerned how far the current framework would be tightened up and what impact the new measures would have on brokers. The industry considered that the Working Group, in formulating any proposed new regulatory measures for consultation, should strike a balance between investor protection and the additional burden to be imposed on the industry by the measures. As regards the need to increase the capital requirements for brokers, comparison of the capital requirements in Hong Kong with those in other places might not be appropriate because of the differences in market conditions. Mr WU urged the Working Group to examine the relevant issues thoroughly before putting forward any proposals for consultation, taking into account the impact of the proposals on brokers under the present unfavourable economic condition.

SFC

18. Mr CHAN Kam-lam saw the need to strengthen investor protection through tightening up the regulatory requirements on brokers. He however shared Mr Henry WU's view that the impact of the proposals on brokers under the present unfavourable economic condition should also be taken into consideration. He commented that increase in capital requirements for brokers might not necessarily strengthen protection for investors against risks resulted from brokers' engagement in aggressive and imprudent lending. Mr NG Leung-sing shared Mr CHAN's view.

19. Given that the industry was facing great difficulty under the present market condition, Mr SIN Chung-kai considered it more appropriate to introduce risk control measures than reform measures. He suggested that further discussion among SFC, the

Administration and the industry should be held with a view to reaching a consensus on the solutions to the problems identified. In response, PSFS said that given the complexity of the issues involved, it would take time to work out a balanced and practicable solution which would strengthen investor protection without imposing excessive burden on market practitioners.

*Representativeness of the Working Group*

20. Pointing out the contributions of small and medium brokers, Mr NG Leung-sing was concerned whether the interests of these brokers and their clients were adequately represented in the Working Group.

21. Mrs Alexa LAM responded that the 15-member Working Group included 11 broker representatives of different sizes. The remaining four members included representatives of the Hong Kong Investment Funds Association, academia, the media and the Consumer Council. The representative of the Consumer Council represented the interests of investors as a whole. While SFC aimed to balance views from market participants and investors through appointing members of different background to the Working Group, the membership might not be able to represent all the industry's views. Hence, after collecting Members' views on the Review, SFC would report back to the Working Group and finalize the proposals for public consultation. The submissions received during the consultation period would be made available to the public through the SFC website. In response to Mr NG Leung-sing's concern over the collection of views from clients of small and medium size brokers, Mrs LAM undertook to explore means to gauge the views of these clients during the consultation period.

SFC

*Proposed Investors' Participation Account*

22. Mr CHAN Kam-lam opined that the implementation of the IP Account should be able to address some of the problems identified in the current system. Noting that HKEx had been developing a new IP Account model for some time, Mr CHAN enquired whether SFC and the Administration would support the implementation of the model, and the timing for implementation.

23. Mrs Alexa LAM responded that as far as she knew, the IP Account model being developed by HKEx would be ready for consultation in two months' time. Despite that various IP Account models were currently being provided by banks in the form of global custodian, market practitioners were in support of the development of an IP Account model by HKEx. Mrs LAM said that the priority of SFC was investor protection. Having identified the integrity risk posed to investors under the current market structure and business model, SFC considered that the problems should be resolved through appropriate improvement measures. SFC would explore all proposed options, including the IP Account model being developed by HKEx or any other models proposed by the industry.

Admin  
SFC

24. Mr CHAN Kam-lam requested the Administration and SFC to urge HKEx for the early completion of its IP Account model.

**VI. Any other business**

25. There being no other business, the meeting ended at 12:05 pm.

Council Business Division 1  
Legislative Council Secretariat  
29 August 2003