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April 3, 2003

Hon Ambrose Lau Hon-chuen, GBS, JP
Chairman
Panel on Financial Affairs
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Mr. Lau,

Panel on Financial Affairs
Enhancement on the regulations on listed companies and
corporate governance of companies

I refer to the letter of 27 March from Ms. Connie Szeto (Clerk to the Panel) to my colleague Ms. Albers. We are pleased to have the opportunity to respond in writing but, as previously advised, will not be making an oral presentation at your meeting on 7 April.

We believe that the questions of regulation of listed companies and enhancement of corporate governance of companies are important topics for Hong Kong if it is to remain a premier financial center. In that context, we made a detailed submission to the Expert Group recently appointed by the Government to consider the Operation of the Securities and Futures Market Regulatory Structure and have since reviewed the Report published by that Expert Group. We are supportive of many of the Expert Group's Recommendations, although the detailed implementation of those Recommendations will require further consideration. In particular, we are supportive of moving the listing function from the HKEx to a new division of the SFC. Whilst we believe that the current system contains appropriate "checks and balances" through the inter-relationship between the SEHK and the SFC, the relationship thereby created is complex and introduces elements of uncertainty, delay and duplication both in the listing process and in the application of the Listing Rules. We believe that, in the longer term, the proposed realignment of responsibilities will provide more effective regulation of listed companies, with better monitoring and investigative powers.

We are also aware of the various Consultation Papers which the HKEx has put out in relation to (i) proposed amendments to the Listing Rules relating to Corporate Governance Issues and (ii) Continuing Listing Criteria and Related Issues. We recently responded to the latter consultation exercise and have reviewed the Conclusions issued on 17 January of this year in relation to the former. Again, we are broadly supportive of the general direction in which the HKEx is moving and believe that, in general, they will both encourage and necessitate better corporate governance standards consistent with international best practices.

One area, however, where we do have concerns is in relation to the regulation of intermediaries, particularly in their role as sponsor of listed companies. Under the new Securities and Futures Ordinance, the powers of the SFC in relation to intermediaries are already materially enhanced. The Expert Group would seem to recommend further strengthening of those powers and we understand that the SFC is looking at revising sponsors' obligations under the Listing Rules for the Main Board to bring them more into line with those for the Growth Enterprise Market (GEM). Whilst we accept that sponsors should bear appropriate responsibility for initial listing matters (including the relevant disclosure documents), we are very much of the view that primary responsibility should properly lie with the directors and senior management of the listed company, most particularly in terms of compliance with ongoing listing requirements. Our concern is that any different proposal will seek to place an unrealistic burden on intermediaries, and will do so simply for the practical reason that they are based in Hong Kong and are a relatively easy target. An appropriate balance needs to be struck between, on the one hand, the role of the regulator as "policeman" and, on the other, the responsibilities of the sponsor. Over-regulation of sponsors will discourage the top-tier international houses from participating in the Hong Kong market which will likely have an overall detrimental effect on the standard of intermediaries participating in the market and, most likely, thereby, on the standard of conduct in the market itself.

That said, we do recognize that listed companies need ongoing advice on listing requirements and corporate governance matters. One idea, therefore, which we have raised in various circles is the idea of a "corporate governance advisor" which need not necessarily be the same firm as the sponsor and indeed could be any of lawyers, accountants, management consultants, brokers or investment banks. The idea would be to split out the initial sponsor role from the ongoing corporate governance advisory role, thus enabling the roles to be separately priced and undertaken by different firms, as appropriate. We believe that this is worthy of further consideration (and possibly wider consultation) since we believe it would alleviate the concerns which sponsors may otherwise feel about their on-going role post-listing whilst at the same time providing the necessary comfort to the regulator that listed companies have access to appropriate advice in relation to their listing obligations. Whilst this may not be an approach which has been adopted in other jurisdictions, such an approach would, we suggest, demonstrate Hong Kong's willingness to be forward-thinking in the area of corporate governance.

If you would like to discuss further, please contact the undersigned at 2848-5565.

Yours sincerely,

David Graham
Managing Director and General Counsel