

LEGISLATIVE COUNCIL BRIEF

Securities and Futures Ordinance (Cap. 571)

SECURITIES AND FUTURES (PROFESSIONAL INVESTOR) RULES

INTRODUCTION

Pursuant to section 397(1) of the Securities and Futures Ordinance (Cap. 571) (the SFO), the Securities and Futures Commission (the SFC) has made the Securities and Futures (Professional Investor) Rules (the Rules) at the **Annex**.

BACKGROUND

The SFO

2. The SFO was enacted in March 2002. It consolidates and modernizes ten existing ordinances governing the securities and futures markets into a composite piece of legislation to keep the regulatory regime on a par with international standards and practices. For effective regulation, the SFO has already provided flexibility in addressing changing market practices and global conditions by empowering the Chief Executive in Council, the Financial Secretary, the Chief Justice and the SFC to prescribe detailed and technical requirements as necessary by way of subsidiary legislation, to supplement the regulatory framework laid down under the primary legislation.

3. On 22 February 2002, the House Committee of the Legislative Council established the Subcommittee on Draft Subsidiary Legislation to be made under the SFO (the Subcommittee) to study the subsidiary legislation necessary for commencing the SFO. From March 2002 to October 2002, the Subcommittee held 12 meetings and considered a total of 37 sets of subsidiary legislation, including the *vires* to make them.

THE PROPOSALS

Major policy considerations

4. There are provisions in the SFO including its subsidiary legislation that are designed especially for investor protection. On consideration that “professional investors”, the meaning of which is defined in Part 1 of Schedule 1 to the SFO (paragraph 5 below), are generally regarded as more capable of protecting their interests, the SFO including its subsidiary legislation disapply or modify certain of such investor protection provisions when the relevant regulated activities are targeted at them. By way of illustration, section 175 of the SFO generally prohibits an offer of securities to a person by an intermediary unless the offer is accompanied by an offering document with the detailed information prescribed under law. Such prohibition does not apply where the person is a professional investor as some of the information items prescribed may not be necessary for a more experienced or sophisticated investor, and the professional investor would be in a position to judge and request the information it or he needs. By providing the exception, a sufficient degree of investor protection would still be maintained while reducing the compliance burden to the market.

Major features of the Rules

5. “Professional investor” is defined in Part 1 of Schedule 1 to the SFO to include classes of persons such as intermediaries, authorized financial institutions, insurance companies and recognized exchange companies. Paragraph (j) of the definition empowers the SFC to prescribe by rules under section 397 to include additional classes of persons as “professional investors”, either generally or for the purposes of any provision of the SFO. Generally, the Rules prescribe four additional classes of persons in terms of the value of assets they manage or have, as professional investors for application throughout the SFO including its subsidiary legislation except Schedule 5 to the SFO.

THE RULES

6. Section 2 contains the interpretation provisions which apply throughout the Rules.

7. Section 3 prescribes the following four additional classes of persons as “professional investor” (including also the manner of ascertaining such status) for application throughout the SFO including its subsidiary legislation except Schedule 5 to the SFO –

- (a) any trust corporation having been entrusted under the trust or trusts of which it acts as trustee with total assets of at least HK\$40 million or its equivalent in any foreign currency;
- (b) any individual (either alone or with his spouse or children on a joint account) having a portfolio¹ of at least HK\$8 million or its equivalent in any foreign currency;
- (c) any corporation or partnership having either a portfolio¹ of at least HK\$8 million or total assets of at least HK\$40 million or its equivalent in any foreign currency; and
- (d) any corporation whose sole business is to hold investments and which is wholly owned by an individual who (either alone or with his spouse or children on a joint account) falls within the description in paragraph (b) above.

PUBLIC CONSULTATION

8. The SFC released a consultation document and an exposure draft of the Rules on 1 February 2002 for comment by the public. A total of ten submissions were received. The SFC has considered all the comments received and revised the Rules as appropriate.

9. A draft of the Rules was considered by the Subcommittee at its meetings held on 6 June 2002 and 24 October 2002. No major concerns were expressed by members of the Subcommittee at the meetings.

FINANCIAL AND STAFFING IMPLICATIONS

10. There are no financial or staffing implications for the Government.

¹ Defined to mean a portfolio comprising securities, certificates of deposit issued by an authorized financial institution or the overseas equivalent, and/or money held by a custodian for him.

COMMENCEMENT DATE

11. The Rules will come into operation on the day appointed for the commencement of the SFO, together with other subsidiary legislation necessary for the commencement. We expect this to take place shortly, after completion of the negative vetting procedure through the Legislative Council and allowing the industry a reasonable period of time for making necessary adjustments with reference to the subsidiary legislation. We aim to announce the commencement date by the end of 2002.

PUBLICITY

12. The Rules will be published in the Gazette on 29 November 2002. The SFC will issue a press release on the same day.

ENQUIRIES

13. For any enquiries on this brief, please contact Mr Alvin Lok of the Licensing Department of the SFC at 2842 7695 or Ms Vania Cheng of the Legal Services Division of the SFC at 2283 6166.

The Securities and Futures Commission
25 November 2002

SECURITIES AND FUTURES (PROFESSIONAL INVESTOR) RULES

(Made by the Securities and Futures Commission under section 397(1) of the Securities and Futures Ordinance (Cap. 571))

1. Commencement

These Rules shall come into operation on the day appointed for the commencement of the Securities and Futures Ordinance (Cap. 571).

2. Interpretation

In these Rules, unless the context otherwise requires -
"associate" (有聯繫者), in relation to an individual, means the spouse or any child of the individual;

"custodian" (保管人) means -

(a) a corporation the principal business of which is to act as a custodian of securities or other property for another person, whether on trust or by contract;
or

(b) any of the following persons -

(i) an authorized financial institution;

(ii) a bank which is not an authorized financial institution but is regulated under the law of any place outside Hong Kong;

(iii) a licensed corporation;

(iv) a person carrying on the business of the provision of investment services and regulated under the law of any place outside Hong Kong,

whose business includes acting as a custodian of securities or other property for another person, whether on trust or by contract;

"custodian statement" (保管人結單) means a statement of account issued by a custodian;

"portfolio" (投資組合) means a portfolio comprising any of the following -

(a) securities;

(b) a certificate of deposit issued by -

(i) an authorized financial institution; or

(ii) a bank which is not an authorized financial institution but is regulated under the law of any place outside Hong Kong;

(c) in relation to an individual, corporation or partnership, money held by a custodian for the individual, corporation or partnership;

"relevant date" (有關日期) -

(a) in the case of an advertisement, invitation or document described in section 103(3)(k) of the

Ordinance, means the date on which the advertisement, invitation or document is issued, or possessed for the purposes of issue;

(b) in the case of a call described in section 174(2) (a) of the Ordinance, means the date on which the call is made;

(c) in the case of an offer described in section 175(5) (d) of the Ordinance, means the date on which the offer is made; or

(d) in any other case which, by virtue of any rules made under the Ordinance, requires compliance with an obligation, means the date by or on which the obligation is required to be complied with;

"trust corporation" (信託法團) means -

(a) any trust company registered under Part VIII of the Trustee Ordinance (Cap. 29); or

(b) any other corporation which -

(i) carries on a business which is of a nature similar to that of a trust company referred to in paragraph (a); and

(ii) is regulated under the law of any place outside Hong Kong.

3. Persons prescribed as professional investors

For the purposes of paragraph (j) of the definition of "professional investor" in section 1 of Part 1 of Schedule 1 to

the Ordinance, the following persons are prescribed as within the meaning of that definition for the purposes of any provision of the Ordinance other than Schedule 5 -

(a) any trust corporation having been entrusted under the trust or trusts of which it acts as a trustee with total assets of not less than \$40 million or its equivalent in any foreign currency -

(i) as stated in the most recent audited financial statement prepared -

(A) in respect of the trust corporation;
and

(B) within 16 months before the relevant date;

(ii) as ascertained by referring to one or more audited financial statements, each being the most recent audited financial statement, prepared -

(A) in respect of the trust or any of the trusts; and

(B) within 16 months before the relevant date; or

(iii) as ascertained by referring to one or more custodian statements issued to the trust corporation -

(A) in respect of the trust or any of the trusts; and

(B) within 12 months before the relevant date;

(b) any individual, either alone or with any of his associates on a joint account, having a portfolio of not less than \$8 million or its equivalent in any foreign currency -

(i) as stated in a certificate issued by an auditor or a professional accountant of the individual within 12 months before the relevant date; or

(ii) as ascertained by referring to one or more custodian statements issued to the individual (either alone or with the associate) within 12 months before the relevant date;

(c) any corporation or partnership having -

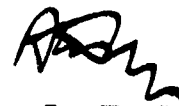
(i) a portfolio of not less than \$8 million or its equivalent in any foreign currency; or

(ii) total assets of not less than \$40 million or its equivalent in any foreign currency,

as ascertained by referring to -

(iii) the most recent audited financial statement prepared -

- (A) in respect of the corporation or partnership (as the case may be);
and
- (B) within 16 months before the relevant date; or
- (iv) one or more custodian statements issued to the corporation or partnership (as the case may be) within 12 months before the relevant date; and
- (d) any corporation the sole business of which is to hold investments and which is wholly owned by an individual who, either alone or with any of his associates on a joint account, falls within the description in paragraph (b).



Andrew Len Tso SHENG

Chairman,
Securities and Futures Commission

25th November, 2002

Explanatory Note

These Rules are made by the Securities and Futures Commission under section 397(1) of the Securities and Futures Ordinance (Cap.

571) for the purposes of paragraph (j) of the definition of "professional investor" in section 1 of Part 1 of Schedule 1 to the Ordinance. Persons prescribed as professional investors by these Rules are exempted in relation to certain prohibitions in the Ordinance. However, such persons are not regarded as professional investors for the purposes of Schedule 5 to the Ordinance.