

立法會
Legislative Council

LC Paper No. CB(1)1088/10-11
(These minutes have been seen
by the Administration)

Ref : CB1/BC/11/09/2

Bills Committee on Securities and Futures and Companies Legislation
(Structured Products Amendment) Bill 2010

Third meeting on
Monday, 6 December 2010, at 4:30 pm
in the Chamber of the Legislative Council Building

Members present : Hon Starry LEE Wai-king, JP (Chairman)
Hon Albert HO Chun-yan
Hon James TO Kun-sun
Hon CHAN Kam-lam, SBS, JP
Hon Miriam LAU Kin-ye, GBS, JP
Hon Audrey EU Yuet-mee, SC, JP
Hon WONG Ting-kwong, BBS, JP
Hon Ronny TONG Ka-wah, SC
Hon Mrs Regina IP LAU Suk-ye, GBS, JP

Member absent : Hon CHIM Pui-chung

Public officers attending : Financial Services and the Treasury Bureau

Mr Anthony LI
Principal Assistant Secretary (Financial Services)

Ms Jane LEE
Assistant Secretary (Financial Services)

Department of Justice

Mr Paul O'BRIEN
Senior Assistant Law Draftsman

Ms Karmen KWOK
Government Counsel

**Attendance by
invitation**

: Securities and Futures Commission

Mr Brian HO
Executive Director, Corporate Finance

Ms Alice LAW
Senior Director
Policy, China and Investment Products

Ms Alexandra YEONG
Director, Corporate Finance

Civic Party

Ms Jacqueline NG
Member

The Hong Kong Society of Financial Analysts

Mr Jimmy JIM
President

Ms Cheri WONG
Chief Executive Officer

Clifford Chance

Ms Charlotte ROBINS
Consultant

Mr Francis EDWARDS
Consultant

Hong Kong Securities Professionals Association

Mr CHAN Hung-ling
Committee Member and Vice-Secretary General

Mr WU Kwok-leung
Committee Member

Hong Kong Financial Planners General Union

Mr CHAN Chak-sum
Vice Chairman

Mr Ken LEE Wai-ming
Representative

Hong Kong Bar Association

Mr Laurence LI
Counsel

Ms Elizabeth CHEUNG
Counsel

Clerk in attendance : Ms Anita SIT
Chief Council Secretary (1)5

Staff in attendance : Mr KAU Kin-wah
Assistant Legal Adviser 6

Mr Noel SUNG
Senior Council Secretary (1)4

Ms Haley CHEUNG
Legislative Assistant (1)8

I Meeting with deputations and the Administration

Meeting with deputations

(LC Paper No. CB(1)617/10-11(02) — Submission from The Hong Kong Society of Financial Analysts

LC Paper No. CB(1)617/10-11(03) — Submission from Clifford Chance

Submissions from organizations not attending the meeting

- (LC Paper No. CB(1)617/10-11(01) — Submission from Baker & McKenzie
- LC Paper No. CB(1)617/10-11(04) — Submission from The Law Society of Hong Kong
- LC Paper No. CB(1)617/10-11(05) — Submission from Mr YEUNG Wai-sing, MH, member of the Eastern District Council
- LC Paper No. CB(1)617/10-11(06) — Submission from Allen & Overy
- LC Paper No. CB(1)648/10-11(01) — Submission from Chinese Securities Association of Hong Kong
- LC Paper No. CB(1)648/10-11(02) — Submission from The Hong Kong Association of Banks
- LC Paper No. CB(1)648/10-11(03) — Submission from International Swaps and Derivatives Association, Inc. / Asia Securities Industry and Financial Markets Association

The Chairman welcomed representatives of the Administration and deputations to the meeting. She reminded the deputations that their views presented at the meeting would not be covered by the protection and immunity provided under the Legislative Council (Powers and Privileges) Ordinance (Cap. 382).

2. The deputations presented their views on the Bill.

Meeting with the Administration

- (LC Paper No. CB(1)429/10-11(02) — Administration's paper on comparison between the existing and the proposed arrangements for regulation of public offers of structured products

- LC Paper No. CB(1)466/10-11(01) — Administration's paper on regulation of currency-linked, interest rate-linked and currency and interest rate-linked instruments
- LC Paper No. CB(1)486/10-11(01) — Administration's paper on definitions of key terms
- LC Paper No. CB(1)429/10-11(03) — Administration's paper on analysis of the market development of structured products in Hong Kong
- LC Paper No. CB(1)466/10-11(02) — Administration's paper on whether the principles in the Code on Unlisted Structured Investment Products could be specified in the legislation
- LC Paper No. CB(3)877/09-10 — The Bill
- LC Paper No. CB(1)199/10-11(01) — Marked-up copy of the Bill prepared by the Legal Service Division
- LC Paper No. CB(1)199/10-11(02) — Administration's first batch replies dated 21 September 2010 to the questions raised by Assistant Legal Adviser on Securities and Futures and Companies Legislation (Structured Products Amendment) Bill 2010
- LC Paper No. CB(1)199/10-11(03) — Administration's second batch replies dated 4 October 2010 to the questions raised by Assistant Legal Adviser on Securities and Futures and Companies Legislation (Structured Products Amendment) Bill 2010

3. The Committee deliberated (Index of proceedings attached at the **Appendix**).

II Any other business

Date of next meeting

4. The Chairman reminded members that the next meeting would be held on 16 December 2010.
5. There being no other business, the meeting ended at 6:35 pm.

Council Business Division 1
Legislative Council Secretariat
17 January 2011

**Proceedings of the
Bills Committee on Securities and Futures and Companies Legislation
(Structured Products Amendment) Bill 2010
Third meeting on Monday, 6 December 2010, at 4:30 pm
in the Chamber of the Legislative Council Building**

Time Marker	Speaker	Subject(s)	Action Required
000102 – 000459	Chairman	Opening remark	
000500 – 000859	Civic Party	Presentation of views	
000900 – 001314	The Hong Kong Society of Financial Analysts	Presentation of views	
001315 – 001830	Clifford Chance	Presentation of views	
001831 – 002053	Hong Kong Securities Professionals Association	Presentation of views	
002054 – 002242	Hong Kong Financial Planners General Union	Presentation of views	
002243 – 002805	Hong Kong Bar Association (HKBA)	Presentation of views	
002806 – 003736	Administration Securities and Futures Commission (SFC)	<p>The Chairman invited the Administration to give a preliminary response to the deputations' views.</p> <p>The Administration made the following points -</p> <p>(a) The Bill introduced the concept and definition of "structured products", and empowered SFC to regulate public offers of all structured products (including those in the form of debentures) under the offers of investments regime in the Securities and Futures Ordinance (Cap. 571) (SFO).</p> <p>(b) Under the existing Companies Ordinance (Cap.32) (CO) prospectus regime, the</p>	

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		<p>disclosure requirements regarding the prospectuses of shares and debentures focussed on the financial performance and prospects of the company concerned as the offers were considered to be for the purposes of equity or debt capital-raising.</p> <p>(c) For structured products, investors would also need to know the issuers' creditworthiness, the reference assets,, and other relevant information including features and risks as set out in the Code on Unlisted Structured Investment Products promulgated under the SFO.</p> <p>(d) As regards the concern on SFC's authorization power, the proposed section 104A was replicated from section 104 of the SFO which had already empowered the SFC to authorize collective investment schemes.</p> <p>(e) To cater for financial innovation, the Bill empowers the Financial Secretary to prescribe products as being or not being structured products.</p> <p>(f) After the transfer of the regulation of public offers of structured products in the form of shares or debentures from the CO to the SFO, the safe harbours in the CO would not be applicable to structured products. The SFO offers of investments regime had its own safe harbours and once the transfer was effective, structured products in the form of debentures would follow the SFO safe harbours instead. Furthermore, public offers of non-security based structured products would also be subject to regulation under the offers of investments regime in SFO.</p> <p>SFC remarked that the safe harbours under the CO prospectus regime, notably the "no more than 50 persons" safe harbour and the "minimum denomination HK\$500,000" safe harbour, were not introduced into the SFO offers of investments regime, because SFC considered that from an investor protection perspective, the authorization requirement should apply to all structured products regardless of the subscription size. In addition, it had always been clear that the SFO only regulated</p>	

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		<p>offers to the public. An introduction of the CO safe harbours into the SFO could lead to abuse and also affect products such as collective investment schemes currently regulated under Part IV of the SFO.</p>	
003737 – 004147	Mrs Regina IP Administration	<p>Mrs Regina IP remarked that the fact had shown that unsophisticated small investors had bought structured products via the CO safe harbours, the marketing materials of which were not authorized by the SFC. Given the emergence of highly complicated structured products and the problems with such products in recent years, Mrs IP supported the arrangement of not replicating the CO safe harbours in the SFO.</p> <p>The Administration responded that the safe harbours were introduced into the CO in 2004 as part of the measures to facilitate the development of retail bonds and other financial products. At that time, those safe harbours were not envisaged for use by complicated products like the structured products. With the significant development of the structured products markets in recent years and from the investor protection perspective, the Administration did not consider it appropriate to introduce the CO safe harbours into the SFO.</p>	
004148 – 005136	Mr Albert HO HKBA SFC	<p>Mr Albert HO enquired whether structured products issued by overseas companies and disposed of in Hong Kong, and structured products issued in Hong Kong but disposed of in other jurisdictions were exempted from authorization by SFC. He sought Mr Laurence LI of HKBA's view on the exemptions.</p> <p>Mr Laurence LI of HKBA remarked that there were exemptions in the CO and SFO for structured and other financial products disposed of only to persons outside Hong Kong. Mr LI noted that as the "act" was not committed in Hong Kong, it was commonly believed that it would be beyond the control of Hong Kong law. Mr LI noted that this type of exemption was common. Mr LI said that securities and bonds sold to the Hong Kong public by companies incorporated overseas were regulated by Hong Kong legislation.</p> <p>SFC advised that under section 103(3)(j) of SFO, exemption was given to advertisement, invitation</p>	

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		<p>or document made in respect of securities, etc that were or were intended to be disposed of only to persons outside Hong Kong. SFC remarked that securities, etc issued by companies incorporated overseas and disposed of to the Hong Kong public were not given exemption, and the Bill did not propose to provide for such exemption for structured products.</p> <p>Mr Albert HO opined that structured products originated in Hong Kong and disposed of to persons outside Hong Kong should also be subject to regulation by SFC. Mr HO sought Mr Laurence LI of HKBA's view on the issue.</p> <p>Mr Laurence LI of HKBA responded that the main-stream approach was for the regulatory regime to afford protection to investors within the jurisdiction concerned. It was theoretically possible to enact legislation to regulate investment products originated in Hong Kong and disposed of to persons outside Hong Kong. This was however not the main-stream regulatory arrangement in the world. In addition, it would involve a change in the regulatory approach as the current approach (whether in existing law or the Bill) was premised on the public offer, not where the product was originated. To regulate investment products originated in Hong Kong and disposed of to persons outside Hong Kong would be beyond the scope of this legislative amendment and would involve a major change of policy in the regulation of investment products. The existing legislation and the Bill aimed to regulate the offers of structured products to the public in Hong Kong.</p> <p>Mr Albert HO enquired, in anticipation of possible structured products originated in Hong Kong being disposed of to persons in neighbouring areas such as the Mainland and Taiwan only, whether the Administration would consider regulating such public offers of structured products to persons outside Hong Kong.</p> <p>The Administration remarked that in response to members' concern raised at the previous meeting on the same issue, the Administration was preparing a relevant paper for the Bills Committee.</p>	

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005137 – 005627	Mr CHAN Kam-lam SFC	<p>Mr CHAN Kam-lam enquired whether the offering documents issued by an overseas issuer for structured products disposed of in Hong Kong required authorization by SFC.</p> <p>SFC responded that section 103 of the SFO stipulated that, subject to the exemptions provided in the SFO, a person committed an offence if he issued, without SFC's authorization, any advertisement, invitation or document which was or contained an invitation to the public to enter into an agreement in respect of certain investment product. This was irrespective of whether the issuer was overseas or local. The term "public" was defined in Schedule 1 to the SFO to mean "the public of Hong Kong, and includes any class of that public".</p>	
005628 – 005942	Mrs Regina IP SFC	<p>Mrs Regina IP enquired about the practices of overseas countries regarding the regulation of the sale of investment products outside the countries.</p> <p>SFC responded that while the United States (US) had certain extra-territorial elements in its regulatory approach, the regulatory authorities in the United Kingdom, Australia, and Singapore did not regulate the sale of investment products to persons outside their respective jurisdiction. The industry was very familiar with this and it was common for investment products to contain selling restrictions to US citizens.</p>	
005943 – 010605	Mr Albert HO SFC	<p>In response to Mr Albert HO's enquiry, SFC remarked that section 1(a) of the proposed Part 3 of Schedule 10 of SFO only referred to the transitional arrangements for authorization and registration under the CO of a programme prospectus and its addenda, and an issue prospectus and its addenda issued by a Hong Kong company, and section 1(b) referred to the same issued by a company incorporated outside Hong Kong. Both required authorization and registration under the CO.</p>	
010606 – 010846	Mr Albert HO SFC	<p>In response to Mr Albert HO's enquiry that Clause 20 of Part 3 of the Bill seemed to exempt companies incorporated overseas, SFC clarified that section 342AA was drafted to disapply the prospectus-related provisions in the CO (i.e., Part XII in respect of companies incorporated</p>	

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		overseas) in relation to structured products so as to move them across to the SFO.	
010847 – 011240	SFC	Briefing by the SFC on the paper (LC Paper No. CB(1)486/10-11(01))	
011241 – 011959	Mrs Regina IP SFC	<p>Mrs Regina IP enquired whether equity-linked instruments sold by banks would be regarded as structured products.</p> <p>SFC responded that under the existing legislative framework, the regulation of public offers of structured products depended on their legal form. Under the Bill, regulation would depend on whether it was a structured product. Equity-linked notes which were in the legal form of a debenture would be included in the definition of "structured products", the public offers of which would fall under the regulation of the offers of investments regime of SFO. Offering documents related to private placements of structured products and offers of structured products to PIs were exempted from SFC's authorization.</p> <p>Mrs Regina IP asked about the definition and the proposed coverage of "regulated investment agreements (RIAs)" in the offers of investments regime under the SFO.</p> <p>With reference to the definition of RIA in the SFO, SFC stated that there were certain similarities between the definition of RIA and that proposed for "structured products". The SFC explained that the definition and regulation of RIA was first provided in the Protection of Investors Ordinance in 1974, and was later transferred to the SFO in 2002. Although advertisements, invitations and documents inviting the Hong Kong public to invest in RIAs required SFC's authorization, RIAs were not "securities" and were therefore not subject to the licensing, conduct and other requirements in the SFO. Accordingly, the SFC was taking this opportunity to regulate the offer of RIAs by subsuming "RIA" into the definition of structured product so that RIAs would be regulated as structured products under the SFO offers of investments regime.</p> <p>In response to Mrs Regina IP's enquiry, SFC remarked that "collective investment scheme"</p>	

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		(CIS) was defined in the SFO, and the term covered investment instruments such as funds and certain investment-linked assurance schemes.	
012000 – 012423	Mr Albert HO SFC	<p>Mr Albert HO enquired under which regime convertible bonds issued by unlisted overseas investment banks would be regulated.</p> <p>SFC responded that convertible bonds were defined as "a debenture issued for capital fund raising purposes that is convertible into or exchangeable for shares of the issuer of the debenture or of a related corporation of the issuer", and was carved out from the definition of "structured product". The regulation of offer of convertible bonds, being a form of debenture, would be preserved under the CO prospectus regime.</p>	
012424 – 012842	Administration	Briefing by the Administration on the paper (LC Paper No. CB(1)429/10-11(03))	
012843 – 013046	Mrs Regina IP SFC	In response to Mrs Regina IP's enquiry about the marked decrease in applications for public offer of equity-linked investments under the offers of investments regime of SFO in 2009, SFC remarked that the significant drop in applications for authorization and applications for renewal of authorization in the first half of 2009 might be related to the financial crisis. The number of applications rose again in mid-2009, and in 2010, SFC had authorized four applications for offer documents of equity linked deposits, and six applications for equity linked investments.	
013047 – 013258	Chairman SFC	In reply to the Chairman's enquiry about the source of the statistics on authorizations, SFC responded that the authorization statistics were compiled based on SFC's records and information provided by banks, and the figures did not cover public offers which were exempted from SFC's authorization. During on-site inspections, SFC staff would also check whether the intermediaries had complied with the relevant codes and guidelines in offering products which were exempted from SFC's authorization. The Hong Kong Monetary Authority (HKMA) had conducted quarterly survey on the sale of investment products by retail banks.	

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013259 – 013722	Administration	Briefing by the Administration on its response to questions on whether the regulatory principles should be specified in the legislation (LC Paper No. CB(1)466/10-11(02))	
013723 – 014907	Mr Albert HO SFC	<p>The Administration explained that it was unnecessary to specify the general regulatory principles in the SFO and that the issue of codes and guidelines provided flexibility for SFC in regulating public offers of structured products. Mr Albert HO expressed his reservation on the Administration's views and opined that the basic, broad and concrete regulatory principles should be specified in the SFO or its subsidiary legislation, as issuers would design products based on the rules and regulations laid down by the regulators, which should not be easily revised at the discretion of the regulators. It was also undesirable to rely on the regulators to exercise their discretion as to whether and when they should consult the market players in revising the codes/guidelines. Mr HO had reservation on the arrangement of making authorization decision with reference to codes and guidelines, which were drawn up, interpreted and revised by the regulators. Mr HO said that there were complaints from businessmen in other fields that their business were disrupted due to the sudden change of the regulatory rules in the codes and guidelines issued by the regulator concerned.</p> <p>SFC responded that it had considered members' suggestions regarding the statutory codification of the regulatory principles, and had critically reviewed the existing arrangement of issuing regulatory codes/guidelines. SFC pointed out that the incorporation of the general regulatory principles in the primary and/or subsidiary legislation might give rise to undue arguments and even lawsuits regarding the interpretation and/or implementation of such principles. This could be subject to abuse by the product issuers. For instance, a very sound principle specified in CO which required the issuers of investment products to make sufficient disclosure on the products to enable investors to make an informed investment decision might still be subject to challenges by parties concerned. Therefore SFC believed that it was better to resort to the "public interest" ground as currently under the law. SFC added that the practice of using codes and guidelines to regulate</p>	

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		<p>public offers of investment products, including collective investment schemes, had been adopted since the inception of SFC and had proved to be effective. Invariably the relevant stakeholders were consulted before the codes/guidelines were revised, in order to meet the need of the changing market and emergence of new financial products, and protect the public interest.</p>	
014908 – 015252	Mrs Regina IP SFC	<p>Mrs Regina IP supported the use of codes and guidelines for the regulation of the financial market, as the codification of the rules and regulations might lead to unnecessary arguments and litigation actions. Mrs IP enquired about the frequency in revising the codes and guidelines for the offering documents of financial products, and the international practice in relation to the issue of codes and guidelines for setting out the regulatory policies.</p> <p>SFC responded that in general, revision of an existing code or set of guidelines had been conducted every two to three years. The time taken to revise an existing code or set of guidelines, including the consultation exercise involved, usually ranged from three to nine months, depending on the complexity of the issue/product involved. The financial regulators in the United Kingdom and Singapore also issued non-statutory codes/guidelines within their broad legal frameworks. The financial regulators in Australia adopted a disclosure-based and post-vetting approach and issued policy statements to specify the rules and regulations.</p>	
015253 – 015456	Chairman SFC	<p>The Chairman enquired whether it was a statutory requirement on SFC to consult the relevant parties before revising the codes and guidelines pursuant to its regulatory functions; and how the dissenting or non-main stream views would be handled in revising the codes and guidelines.</p> <p>SFC responded that in the past, SFC had consulted the relevant stakeholders on all major changes in the codes and guidelines, and would continue to do so. It was SFC's policy to consult the public on any revision of the codes and guidelines in respect of public offers of investment products. SFC would initiate further review of the code and guidelines concerned if there were substantial</p>	

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		dissenting views on the proposed revisions. Apart from supervision by the SFC Board of Directors, SFC's decisions on authorization of offering documents were subject to review by the Securities and Futures Appeals Tribunal.	
015457 – 015516	Chairman	Date of next meeting and schedule of further meetings	

Council Business Division 1
Legislative Council Secretariat
17 January 2011