

立法會
Legislative Council

LC Paper No. CB(1)1930/10-11
(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

Seventh meeting on
Monday, 31 January 2011, at 10:45 am
in Conference Room A of the Legislative Council Building

Members present : Hon Starry LEE Wai-king, JP (Chairman)
Hon CHAN Kam-lam, SBS, 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

Members absent : Hon Albert HO Chun-yan
Hon James TO Kun-sun
Hon Miriam LAU Kin-ye, GBS, JP
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

Hong Kong Monetary Authority

Ms Alice LEE
Acting Head
Banking Conduct Department

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

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

I Meeting with the Administration

Follow-up to issues raised at the meeting on 20 January 2011

(LC Paper No. CB(1)1192/10-11(01) — List of follow-up actions arising from the meeting on 20 January 2011 prepared by the Legislative Council Secretariat

LC Paper No. CB(1)1192/10-11(02) — Hong Kong Monetary Authority's paper on "Comparison between the Banking Ordinance and the Securities and Futures Ordinance on investor protection with regard to unlisted investment products sold by authorized institutions and not regulated under the Securities and Futures Ordinance")

Clause-by-clause examination of the Bill (starting at clause 5)

- (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)1093/10-11(02) — Summary of views submitted by organizations/individuals on the Securities and Futures and Companies Legislation (Structured Products Amendment) Bill 2010 and the Administration's response
- 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)

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

Admin

Follow-up actions to be taken by the Administration

2. The Administration was requested to take the following actions:
 - (a) to provide information on the outstanding issues raised at previous meetings; and
 - (b) to submit the draft Committee Stage Amendments (CSAs) for consideration by the Bills Committee.

ALA6

Follow-up action to be taken by Assistant Legal Adviser

3. The Assistant Legal Adviser was requested to review the Chinese version of the Bill, and report the outcome to the Bills Committee.

II Any other business

Next meeting

4. The Chairman said that the Bills Committee had completed the clause-by-clause examination of the Bill and would consider the information to be provided by the Administration regarding the outstanding issues raised at previous meetings, and the Administration's draft CSAs at the next meeting on 17 February 2011.
5. There being no other business, the meeting ended at 12:15 pm.

Council Business Division 1
Legislative Council Secretariat
15 April 2011

**Proceedings of the
Bills Committee on Securities and Futures and Companies Legislation
(Structured Products Amendment) Bill 2010
Seventh meeting on Monday, 31 January 2010, at 10:45 am
in Conference Room A of the Legislative Council Building**

Time Marker	Speaker	Subject(s)	Action Required
000021 – 000201	Chairman	Opening remark	
000202 – 000321	Hong Kong Monetary Authority (HKMA)	Briefing by HKMA on LC Paper No. CB(1)1192/10-11(02))	
000322 – 000521	Chairman Mr WONG Ting-kwong	Mr WONG Ting-kwong and the Chairman opined that the protection for investors afforded by the Banking Ordinance (Cap. 155) (BO) and the Securities and Futures Ordinance (Cap. 571) (SFO) for investors of unlisted structured products should be the same.	
000522 – 000754	ALA6	ALA6 observed that the BO only empowered HKMA to regulate the operation of Authorized Institutions (AIs) but not the behaviour of their staff individually, whereas under the SFO, the Securities and Futures Commission (SFC) might exercise power to forge settlement between complainants and the financial institutions concerned. ALA6 opined that the issue would more appropriately be pursued at the Panel on Financial Affairs.	
000755 – 002209	Administration Mrs Regina IP Chairman Securities and Futures Commission (SFC)	<p>The Administration advised that based on the Department of Justice (DoJ)'s advice, it would be legally in order to use a Committee Stage amendment (CSA) to prescribe the fees to be charged by SFC for the authorization of structured products. The SFC had had communications with the industry on this issue. The current proposal was to rationalize the fee structure by introducing a product fee to correspond to the new power to authorize structured products. The overall fee levels would be broadly in line with the existing fee levels in respect of application for SFC's authorization for public offers. Therefore the industry had no objection to the proposed fees.</p> <p>The Administration remarked that members' previous concern regarding the purposes and scopes of the exemption provisions in section</p>	The Administration was required to

Time Marker	Speaker	Subject(s)	Action Required
		<p>103(2), (5) and (6) of SFO and the proposed section 103(11A) was noted, and a response would be provided at the next meeting.</p> <p>SFC remarked that the notion of an "invitation to the public" was brought down from the repealed Protection of Investors Ordinance to the SFO when the SFO was enacted. The concept of "an invitation to the public" was discussed at the Bills Committee for the Securities and Futures Bill in 2001. At those meetings, it was agreed that a broad notion of "invitation to the public" was necessary in order to protect the interests of investors and the court should be the ultimate authority to interpret and decide whether an advertisement or a document contained an invitation to the public, based on the facts of individual cases. Preliminary research conducted by SFC showed that there was no case law in Hong Kong regarding the interpretation of "offer to the public". In the United Kingdom and Australia, there was no numerical bright-line test case for defining "public" but that an invitation does not have to be "universal" but had to be general in its nature. In the United States, there was case law which suggested that certain considerations had to be taken into account in deciding whether an offer was made to the public. The factors that would be taken into account included the number of offerees, their relationship with one another and the issuer, the nature of the offerees (for example their degree of sophistication), the offerees' ability to have access to information, and the manner and the size of the offer, etc. Hence there could be no simplistic bright-line test.</p> <p>Mrs Regina IP was concerned that there was not a clear demarcation between private placement and public offer of investment products in legislation, thereby causing confusion to investors and creating loopholes for abuse. Mrs IP enquired about the sanction to be imposed for contravention of provisions under section 103.</p> <p>SFC responded that the notion of "offer to the public" had existed for a long time under the SFO for regulation of public offer of products. In 2004, the "no more than 50 persons" safe harbour provision was introduced into the Companies Ordinance (Cap. 32) (CO). While a</p>	take action as per paragraph 2 of the minutes.

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		<p>numerical criterion, such as "offering to 50 persons or more" could provide a "bright-line test", an issuer might abuse the system by offering financial products with slight variance to different groups of 49 investors. SFC did not consider it appropriate to alter the concept of "offer to the public" in the existing SFO under the current Bill. SFC pointed out that the issue of the advertisements and/or documents for public offers of securities and structured products were already subject to authorization by SFC. Issuers should be aware that various relevant factors would need to be taken into account in determining whether an offer was a public offer or a private placement, and should avail themselves of legal advice if needed. SFC added that any offence committed under section 103 of SFO was a criminal offence.</p> <p>Chairman asked in different scenarios where an intermediary solicited selected clients, whether each of those scenarios would constitute an offer to the public that required authorization.</p> <p>SFC responded that issuers would be fully aware during the "product manufacture process" who the end-target for the product would be. If the product was offered to the public and no SFC authorization was sought, the issuer would commit an offence under section 103 of the SFO. Once the offering documents had been authorized by the SFC for public offering, the next issue would be the manner and approach adopted by an intermediary in providing an authorized offering document to the public, which was a separate conduct issue. It was important to differentiate between the regime in Part IV which applies to "public offers" and should be dealt with at the product manufacturing stage and the intermediary's conduct obligations during the sale process.</p>	
002210 – 002520	Mr WONG Ting-kwong SFC	<p>Mr WONG Ting-kwong enquired whether the SFC could issue any guidelines to specify the number of offerees for public offer.</p> <p>SFC responded that Guidelines could not prevail over the relevant Ordinance, and the number of offerees was only one of factors for determining whether an offer was made to the public.</p>	

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002521 – 003017	Administration	<p><u>Clause-by-clause examination of the Bill</u></p> <p><u>Clause 6 – Section 106 amended (Withdrawal of authorization under section 104 or 105, etc.)</u></p> <p><u>Clause 7 – Section 107 amended (Offence to fraudulently or recklessly induce others to invest money)</u></p> <p><u>Clause 8 – Section 108 amended (Civil liability for inducing others to invest money in certain cases)</u></p> <p><u>Clause 9 – Section 111 amended (Service of notices, etc. on approved persons)</u></p> <p>Members raised no question on clauses 6 to 9.</p>	
003018 – 004701	ALA6 Mr Ronny TONG Administration SFC	<p><u>Clause 10 – Section 182 amended (Investigations)</u></p> <p>ALA6 drew members' attention to the proposed scope of the amended section 182 empowering SFC to investigate into offences relating to all structured products, including those that would not require authorization under the SFO, such as structured products which were not securities and were not offered to the public.</p> <p>SFC explained that sections 107 and 108 of SFO covered offences involving fraudulent misrepresentation or reckless misrepresentation for the purpose of inducing another person to invest in a financial product regulated under the SFO and a proposal had been made to extend these provisions to cover structured products that were not securities and were not offered to the public. When there was a breach of these provisions, the SFC would need to exercise its investigatory powers under section 182 to look into such breaches. Since sections 107 and 108 had been extended to cover misrepresentations in respect of structured products that would not require SFC authorization, it followed that section 182 should be expanded to cover these structured products as well. The SFC explained that the current scope of sections 107 and 108 already cover products which were not SFC authorized and therefore there is no change in policy with the proposed amendment. The policy intent was to provide the same protection for investors of all financial products when misrepresentations were used to induce the investments.</p>	

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		<p>In response to ALA6's enquiry, SFC confirmed that persons selling structured products that were not offered to the public and which were not securities based would not require to be licensed or registered for Type 1 regulated activities under the SFO.</p> <p>ALA6 said that persons selling these structured products might on the one hand not be required to comply with SFC requirements on securities and might not even need to be licensed but on the other hand, these persons could be subject to civil and criminal proceedings under sections 107 and 108 of SFO for any fraudulent, reckless or negligent misrepresentation for the purpose of inducing another person in buying such products. ALA6 asked whether this was an appropriate arrangement.</p> <p>SFC responded that the existing section 107 already covered regulated investment agreements which were not securities and would be included in the definition of structured products.</p> <p>The Administration remarked that the requirements in the SFO applied on different levels. Sections 107 and 108 dealt with offences of fraudulent misrepresentation, reckless misrepresentation or negligent misrepresentation in relation to the sale of financial products regulated under the SFO, which included securities, regulated investment agreements, other structured products, and collective investment schemes irrespective of whether the products were publicly offered.</p> <p>Mr Ronny TONG remarked that under the common law, any offence involving fraudulent, reckless or negligent misrepresentation could be sued through civil proceedings.</p>	
004702 – 005005	Mrs Regina IP SFC	<p>Mrs Regina IP enquired about the type and amount of structured products in the market which were not securities and/or were not issued to the public.</p> <p>SFC responded that there were credit default swaps arranged between individuals or corporations bilaterally for business purposes. As these instruments were not offered to the public, they were not and it would not seem reasonable for them to be subject to regulation under the public offer regime or the licensing requirements of the SFO.</p>	

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005006 – 005433	Administration	<p><u>Clause 11 – Section 213 amended (Injunctions and other orders)</u></p> <p><u>Clause 12 – Section 379 amended (Avoidance of conflict of interests)</u></p> <p><u>Clause 13 – Section 392 substituted</u></p> <p><i>392 – Financial Secretary to prescribe interests, etc. as securities, etc.</i></p> <p><u>Clause 14 – Section 407 amended (Savings, transitional, consequential and related provisions, etc.)</u></p> <p>Members raised no question on clauses 11 to 14.</p>	
005434 – 010222	SFC Chairman ALA6	<p><u>Clause 15 – Schedule 1 amended (Interpretation and general provisions)</u></p> <p>Regarding the proposed amendment to the definition of "debenture" by replacing "securities" with "debt securities", the Chairman enquired about the interpretation of "debt securities" and whether there were any past cases involving arguments on the interpretation of the term.</p> <p>SFC responded that the term "debt securities" was already used in the SFO without a definition, and was interpreted in the general sense. There was no contention in the past concerning the definition of "debt securities". However, there was concern that the scope of the term "debenture" was too broad.</p> <p>ALA6 expressed concern that the lack of a clear definition of "debt securities" might give rise to loopholes, and asked whether the Administration would consider providing a legal definition of "debt securities" to avoid arguments between SFC and an issuer as to whether a particular investment product was a "structured product" or a "debt security".</p> <p>SFC responded that "debt securities" were not structured products. Given the wide scope of the definition of "structured products" in the Bill and that public offers of structured products were carved out from the CO and transferred into the SFO, there should be no problem in determining</p>	

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		<p>whether an investment product was a "structured product" that would fall under the SFO if publicly offered. The proposal to amend the definition of "debenture" by limiting it to "debt securities" rather than "any other securities" was mainly based on the recommendation of the Standing Committee on Company Law Reform.</p>	
010223 – 010314	Chairman SFC	<p>Regarding Clause 15(8), Chairman enquired whether reference had been made to the regulatory regime in other jurisdictions in drawing up the definition of "structured product".</p> <p>SFC responded that Hong Kong was the first place to lay down a statutory definition of "structured product". The relevant parties such as the Hong Kong Association of Banks had been consulted on the proposed definition of "structured product".</p>	
010315 – 011322	SFC Chairman ALA6	<p>Regarding clause 15(7), ALA6 observed that a structured product could be merely interest-rate linked but at the same time so complicated that it could cause great losses to its holders. The exemption allow such be sold by unlicensed persons.</p> <p>SFC responded that as proposed in the Bill, authorized institutions' selling of investment products which were purely interest-rate linked, currency-linked or interest rate and currency-linked would continue to be regulated by HKMA under the BO, and HKMA might issue guidelines as appropriate. If the product was not purely linked to interest-rates, currency or interest rates and currency, it would not be exempted under the SFO.</p> <p>The Chairman remarked that to cater for product innovation, the Financial Secretary was empowered under the Bill to determine whether an investment product was a "structured product" or not.</p>	
011323 – 011802	Chairman SFC	<p><u>Clause 16 – Schedule 8 amended (Securities and Futures Appeals Tribunal)</u></p> <p>Members raised no question on clauses 16.</p> <p><u>Clause 17 – Schedule 10 amended (Savings, transitional, consequential and related provisions, etc.)</u></p>	

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		<p>The Chairman said that some deputations had expressed concern as to whether SFC would be able to process the applications and grant relevant licenses within the six-months transitional period.</p> <p>SFC responded that SFC would be able to process the applications within the transitional period.</p>	
011803 – 012006	Administration Chairman SFC	<p>Part 3</p> <p>Amendments to Companies Ordinance</p> <p><u>Clause 18 – Section 2 amended (Interpretation)</u></p> <p>The Chairman enquired whether "debt securities" issued by investment banks would be subject to regulation.</p> <p>SFC responded that "<u>debt securities</u>" offered to the public would most likely be a "debenture", such public offer of "debenture" was and would continue to be subject to regulation under the prospectus regime of the CO. If it was a public offer of "structured products", it would fall under the SFO regime.</p>	
012007 – 012142	Administration	<p><u>Clause 19 – Section 38AA added</u></p> <p><i>38AA – Exemption for structured products</i></p> <p><u>Clause 20 – Section 342AA added</u></p> <p><i>342AA – Exemption for structured products</i></p> <p>Members raised no question on clauses 19 to 20.</p>	
012143 – 012248	Administration	<p><u>Clause 21 – Third Schedule amended (Matters to be Specified in Prospectus and Reports to be set out therein)</u></p> <p><u>Clause 22 – Seventeenth Schedule amended (Offers specified for the purposes of paragraph (b)(ii) of the definition of "prospectus" in section 2(1) of this Ordinance)</u></p> <p><u>Clause 23 – Eighteenth Schedule amended (Warning, etc. Statements to be contained in certain documents)</u></p> <p><u>Clause 24 – Nineteenth Schedule amended (Contents and publication requirements of advertisements mentioned in section 38B(2)(e) of this Ordinance)</u></p>	

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		<p><u>Clause 25 – Twentieth Schedule amended (Amendment of prospectus consisting of one document)</u></p> <p><u>Clause 26 – Twenty-first Schedule amended (Provisions in accordance with which a prospectus may consist of more than one document)</u></p> <p><u>Clause 27 – Twenty-second Schedule amended (Persons specified for the purposes of section 40 of this Ordinance)</u></p> <p>Members raised no question on clauses 21 to 27.</p>	
012249 – 012323	Administration	<p>Part 4</p> <p>Inland Revenue Ordinance</p> <p><u>Clause 28 – Schedule 16 amended (Specified transactions)</u></p> <p>Members raised no question on clause 28.</p>	
012324 – 012458	Administration	<p>Securities and Futures (Short Selling and Securities Borrowing and Lending (Miscellaneous)) Rules</p> <p><u>Clause 29 – Section 2 amended (Interpretation)</u></p> <p>Members raised no question on clause 29.</p>	
012459 – 012607	Chairman	Date of next meeting	