

**LEGISLATIVE COUNCIL PANEL  
ON FINANCIAL AFFAIRS**

**Information Note on Policy Initiatives of  
the Financial Services and the Treasury Bureau**

**INTRODUCTION**

This information note highlights the new and on-going policy initiatives relating to the Financial Services and the Treasury Bureau under the 2009-10 Policy Agenda issued on 14 October 2009.

**FINANCIAL SERVICES**

**Overview**

2. In the past year, we have witnessed the worst-ever financial crisis since the Great Depression and its devastating impacts on international financial institutions as well as the global economy. Many governments worldwide have taken unprecedented fiscal and other measures to maintain the proper functioning of the monetary system, to restore financial stability and to arrest a major economic recession.

3. In Hong Kong, we have taken swift actions to, amongst others, anchor public confidence in and promote stability and liquidity of our financial system. Examples of contingency measures taken include provision of full guarantee for bank deposits and establishment of the Contingent Bank Capital Facility, both to continue until end 2010. The financial authorities have also stepped up regulatory oversight of financial institutions to identify, in particular, any possible excessive risk-taking that might create stability and solvency concerns. Thanks to the solid foundation laid by our robust regulatory regime, our financial systems have survived this severe crisis and remained stable, and none of the financial institutions in Hong Kong had required active Government intervention to sustain their operations.

4. Repercussions of the financial crisis have however led us to review the need for additional investor protection measures and ways to further

improve our regulatory framework. In February 2009, we presented to the Panel an Action Plan for taking forward the various recommendations put forth by the Hong Kong Monetary Authority (“HKMA”) and the Securities and Futures Commission (“SFC”). A phased approach has been adopted to improve our regulatory framework and enhance investor protection. Some of the improvement measures had already been implemented<sup>1</sup>. Some are undergoing public consultation<sup>2</sup>. We plan to consult the public by year end on the establishment of a cross-sector investor education council and a financial dispute resolution scheme (commonly referred to as “Financial Services Ombudsman” in overseas jurisdictions), as well as codifying in statute certain disclosure requirements on price sensitive information by listed companies. Our aim is to provide a continuum of protection to investors at various stages of investment. In addition, we will put in place enhancements to the Deposit Protection Scheme (“DPS”) to strengthen protection for depositors.

5. In parallel with our efforts to optimize the regulatory framework, we will continue to consolidate and enhance our strengths as an international financial centre by fostering market development. In this regard, the vast Mainland market has provided us with immense opportunities to expand the scope of our financial activities, and the breadth and depth of our financial markets. We will continue to attract the listing of quality Mainland enterprises in Hong Kong and encourage the investment of Mainland capital through Hong Kong’s sophisticated asset management infrastructure. We will sustain on-going efforts to press ahead the further expansion of Renminbi (“RMB”) business in Hong Kong. We will also identify further opportunities for financial services cooperation through various platforms including the Mainland and Hong Kong Closer Economic Partnership Arrangement (“CEPA”) and the Hong Kong / Guangdong Co-operation Joint Conference.

6. Moreover, to diversify our financial markets, we will forge ahead

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<sup>1</sup> For example, banks are required to attach “health warnings” to retail derivative products, implement internal mystery shopper programme, audio-record the sales process, etc. The SFC had also launched a series of unlisted authorised products on its investor education website, and issued a circular to remind intermediaries who make investment recommendations or solicitations to clients about the suitability obligations in the Code of Conduct for Persons Licensed by or Registered with the SFC.

<sup>2</sup> For instance, the SFC launched a consultation in late September 2009 on proposals to enhance the regulation of the sale of unlisted securities and futures products to the public, such as the requirement of key facts statements, introduction of cooling-off period, disclosure of commercial interest involving in the sales process (like commissions and fees), etc.

with the implementation of the Government Bond Programme (“GBP”) and development of Islamic finance. To ensure that our legislation governing companies’ operation meets the modern day needs of businesses, we have commenced a major exercise to rewrite the Companies Ordinance (“CO”) and will start consulting the public on the draft provisions of the Companies Bill by the end of this year. At the same time, we have revisited the introduction of a corporate rescue procedure to help companies facing financial difficulties to turn themselves around and will issue a consultation paper on the legislative proposals shortly. We believe that the above targeted efforts will provide us with the necessary impetus to capitalize on the development opportunities upon the recovery of the global economy and to sharpen our competitive edge as the leading international financial centre in our country and the Asian time zone.

## **2009-10 Policy Agenda**

7. We set out in the ensuing paragraphs our plan for and the progress in implementing major policy initiatives, which are designed to meet two major objectives, namely improving the regulatory framework and investor protection, and facilitating market development.

### **I. Improving Regulatory Framework and Investor Protection**

#### *Enhancing disclosure and transparency*

##### *(a) Statutory codification of certain disclosure requirements on price sensitive information by listed companies*

8. We support the development of a continuous disclosure culture among listed companies. One of the means is to oblige timely disclosure of price sensitive information through amendments to Securities and Futures Ordinance (“SFO”). The objective is to enhance effectively the quality and reputation of our equity market without stifling market development. This would involve attaching proportionate sanctions to the statutory regime. We are working with the SFC and the Hong Kong Exchanges and Clearing Ltd (“HKEx”), and aim to consult the market on this legislative proposal by the end of 2009.

*(b) Improving the offering regime for structured products*

9. We are working with the SFC to improve the offering regime for structured products by transferring the authorization of offering documentation in relation to such products from the CO to the SFO. This will allow the SFC greater scope and flexibility in defining the appropriate documentation standards through the publication of codes and guidelines under the SFO<sup>3</sup>. The SFC aims to publish a consultation paper later this year.

*(c) Developing a scripless securities market*

10. The implementation of a scripless securities market would help improve transparency and enhance corporate communication, thus facilitating investors in making an informed investment decision and enhancing the competitiveness of Hong Kong as an international financial centre. With experience from past market engagement efforts and based on evolving market needs, the SFC is working with the HKEx and the Federation of Share Registrars on the preferred operational model for a scripless environment, and they plan to issue a consultation paper later this year.

***Strengthening investor protection and confidence***

*(d) Proposed establishment of an investor education council and a financial dispute resolution scheme*

11. The proposed establishment of an investor education council seeks to enhance the financial literacy of the investing public in Hong Kong. We are exploring ways to enhance and coordinate the existing efforts in providing education to the investors in Hong Kong. For the financial dispute resolution scheme, it aims to help investors settle their disputes through a simple and quick resolution mechanism. We plan to launch public consultation on these two proposals by the end of this year.

*(e) Review of the Deposit Protection Scheme*

12. With the assistance of the HKMA, the Hong Kong Deposit Protection Board (“HKDPB”) has conducted a review of the DPS with a view to enhancing protection for depositors. The public consultations for the review have been completed recently. We will introduce into the Legislative

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<sup>3</sup> The SFC is conducting its consultation on a new Code on Unlisted Structured Products via its September 2009 consultation paper on proposals to enhance protection for the investing public (see footnote 2).

Council (“LegCo”) the proposed legislative amendments for the recommendations concluded in the review within this legislative year. Our target is to effect the recommendations as soon as possible so that the public will benefit from an improved DPS as part of the financial infrastructure of Hong Kong.

(f) Proposed establishment of a Policyholders’ Protection Fund

13. We are preparing proposals for the establishment of a Policyholders’ Protection Fund (“PPF”) in Hong Kong to improve insurance market stability and safeguard the interest of policyholders in the event of insolvency of an insurer. We are making preparations, including the necessary tendering procedures, for the commencement of an actuarial consultancy study in early 2010, to examine the scope of coverage, levy rates, target fund size, and other detailed arrangements for the proposed PPF. We aim to consult this Panel on the detailed proposals within this legislative session.

(g) Proposed establishment of an independent Insurance Authority

14. In view of the international trend for financial regulators to be independent and in order to provide the Insurance Authority with more flexibility in operations and staff recruitment to meet the regulatory challenges, we have been looking into the establishment of an independent Insurance Authority. We will also take this opportunity to review the insurance regulatory regime and identify areas for improvement after the financial crisis. We plan to consult stakeholders on the proposals in the first half of 2010.

(h) Enhancing the anti-money laundering (AML) regulatory regime for the financial sectors

15. Pursuant to the new initiative announced in the 2008-09 Policy Address, we have scrutinized the AML regulatory regime for the financial sectors and drawn up a conceptual framework of a legislative proposal to enhance the regime by codifying the customer due diligence and record-keeping obligations, providing necessary regulatory powers for the regulatory authorities and proportionate sanctions against breaches, and putting in place a licensing regime for remittance agents and money changers. The objective is to bring our AML regulatory regime in line with the international AML standards in these aspects. Public consultation on the conceptual framework ended on 8 October. We are now examining the views received for formulating a detailed legislative proposal for a second-round consultation. Our aim is to introduce a bill into LegCo in the

second quarter of 2010.

(i) Reviewing and strengthening the supervisory framework for authorized institutions

16. The Basel Committee on Banking Supervision (“BCBS”) has recently completed the reform proposals concerning the Basel II regulatory capital framework e.g. on strengthening the risk coverage of the capital standards (primarily in respect of authorized institutions (“AIs”)’ trading books and securitization activity) and enhancing the disclosures made by AIs with regard to securitization exposures and associated risks. The HKMA will prepare and conduct consultations on the proposed amendments to the Banking (Capital) Rules and the Banking (Disclosure) Rules, which seek to reflect these reform proposals.

17. The HKMA is also reviewing the liquidity risk regulatory framework for AIs and will be consulting the industry on the introduction of new qualitative liquidity risk management standards to bring Hong Kong in line with the BCBS’ sound principles for management and supervision of funding liquidity risk. The HKMA will also consult the industry on the introduction of any new minimum quantitative global liquidity standards as set by the BCBS in due course.

18. Looking forward, the HKMA will continue to contribute to the BCBS’ ongoing work to strengthen the quality, consistency and transparency of the capital base of banking institutions. Once international consensus is reached in the relevant regards, the HKMA will consult the industry and take necessary steps to implement the changes in Hong Kong in a manner appropriate to Hong Kong’s market. Supervisory guidance will also be issued by the HKMA to strengthen AIs’ corporate governance, risk management practices and accounting and provisioning standards.

## **II. Facilitating Market Development**

(a) Advancing financial cooperation with the Mainland

19. As always, we are committed to advancing financial cooperation with the Mainland and developing a mutually-assisting, complementary and interactive relationship between the two financial systems. We will make full use of the opportunities brought by “One Country, Two Systems” to continue to develop Hong Kong as a global financial centre, asset management centre and offshore RMB business centre pooling together

capital and talents from Mainland and overseas. In pursuing the above, we will bear in mind two overarching principles: first, any liberalisation initiatives should complement the overall development of our country and be mutually beneficial to both the Mainland and Hong Kong; and second, they should not compromise the “financial security” of our country.

20. Our vibrant and international stock market not only satisfies the need for fund-raising, but also provides an effective platform for Mainland companies to develop their corporate branding and enhance their international recognition. To reinforce Hong Kong’s status as Mainland enterprises’ preferred international capital raising centre outside the Mainland, we will continue to upgrade corporate governance standards as well as improving the rules governing listing in Hong Kong.

21. Hong Kong is best placed to serve as an effective channel for orderly capital outflows from the Mainland and for Mainland financial institutions to manage their overseas investments through Hong Kong. We encourage market innovation so as to provide a wide range of products and services for our investors. For instance, we are continuing to add to our offering of exchange-traded funds (“ETFs”). This is illustrated by the cross-listing of ETFs in Hong Kong and Taiwan in summer 2009. Under Supplement VI to CEPA (“CEPA VI”), the Mainland will actively explore the introduction of ETFs constituted by Hong Kong listed stocks. We are keeping close liaison with the relevant Mainland authorities and will provide all necessary support in this regard.

22. Given our robust risk management systems as well as our cultural affinities and close economic ties with the Mainland, Hong Kong is best placed to serve as a reliable and effective testing ground for the liberalisation of the Mainland’s capital accounts and the regionalisation and internationalisation of the RMB. We have been working with the relevant Mainland authorities, our financial regulators and the trade to attract more RMB liquidity and develop new RMB products and services in Hong Kong, so as to anchor our position as Mainland’s offshore RMB business centre. An array of initiatives have been recently implemented in Hong Kong. These include the launching of the RMB trade settlement pilot scheme, issue of RMB bonds by Hong Kong banks in the Mainland, and issue of RMB sovereign bonds in Hong Kong by the Central Government. In line with the State policy, we shall continue to press ahead with expanding the scope and facilitating the development of RMB business in Hong Kong, which will be beneficial to the financial developments of both the Mainland and Hong Kong.

23. The implementation of CEPA has strengthened the financial co-operation between the Mainland and Hong Kong. CEPA VI, which came into effect on 1 October 2009, has launched some further liberalisation measures with respect to the financial industry. On banking, branches established by a Hong Kong bank in Guangdong can set up “cross-location” sub-branches within Guangdong. On securities services, qualified Mainland and Hong Kong securities companies can set up joint venture companies in Guangdong to provide securities investment advisory service. On mutual recognition of professional qualifications, Hong Kong accountants will be exempted from the “Finance and Accounting” paper when sitting for Mainland’s Certified Tax Agent qualification examination. All of these measures will help expand the presence of our financial institutions and professionals in the Mainland. We look forward to the progressive implementation of these measures, and will continue our follow-up efforts.

24. The CEPA VI measures on the establishment of “cross-location” sub-branches by banks and joint venture securities investment advisory companies have been designated for implementation in Guangdong. This echoes the spirit of “early and pilot implementation” of Mainland-Hong Kong cooperation initiatives in the Pearl River Delta Region as enshrined in the “Outline of the Plan of the Development and Reform of the Pearl River Delta Region”. We will leverage on the “early and pilot implementation” policy to enhance the two-way flow of financial institutions, financial products, capital and talents between Hong Kong and the Pearl River Delta Region, so as to serve as the testing ground and bridgehead of our country’s financial development and innovation.

*(b) Implementing the GBP*

25. We are implementing the GBP to promote further and sustainable development of the local bond market by issuing Hong Kong Dollar-denominated government bonds for both institutional and retail investors on an ongoing basis. The first institutional issue under the GBP was launched in early September with positive response as evidenced by over-subscription. The second institutional issue will be conducted in early November. We are closely monitoring the market conditions and will decide on the timing and details for the first retail issue.

*(c) Developing the Islamic bond (sukuk) market*

26. Development of Islamic finance in Hong Kong will help consolidate Hong Kong’s status as an international financial centre and capitalize on the market niche offered by this relatively new sphere of financial services.

Following consultation with the industry and trade bodies, and having drawn reference to the experience of other Islamic finance centres, we plan to level the playing field for sukuk vis-a-vis conventional bonds in terms of taxation arrangements. For this purpose we shall introduce into LegCo proposed amendments to the Inland Revenue Ordinance and the Stamp Duty Ordinance in this legislative session.

*(d) Promoting asset management business*

27. Hong Kong's asset management business has remained robust despite the global financial crisis. As of end 2008, our combined fund management business amounted to HK\$5,850 billion, with over 64% of funds sourced from overseas investors. In the past year, we saw the rapid development of Hong Kong's ETF business, both in terms of the number of ETFs listed and their diversity in geographical exposure. The cross-listing of Hong Kong ETFs on the Taiwan Stock Exchange, as referred to in para. 21, has provided an additional channel to facilitate regional fund flows to our market. Looking ahead, the Government and the financial regulators will continue to promote Hong Kong's asset management industry and enhance our position as a major asset management centre in Asia.

*(e) Rewrite of the Companies Ordinance*

28. Phase I of the CO rewrite exercise which commenced in mid-2006 covers mainly the core company provisions that affect the operation of more than 750,000 live companies in Hong Kong. We have completed three topical public consultations on the more complex subjects and are preparing a draft bill for further public consultation. Given that numerous issues are involved and some of them are complex, we will conduct public consultation on draft provisions of the Bill in two rounds in late 2009/early 2010. The first round, mainly covering provisions on enhancing corporate governance, is scheduled for December 2009. Our aim is to introduce the Companies Bill into LegCo by the end of 2010.

*(f) Review of the Trustee Ordinance*

29. We are reviewing the Trustee Ordinance ("TO") and related matters with a view to modernising the provisions in the TO for the purposes of strengthening the competitiveness of our trust services industry and facilitating financial market development in Hong Kong. We launched a three-month public consultation which ended on 21 September. Most of the reform proposals are generally supported by the respondents. We are studying the feedback and aim to issue the consultation conclusions in late

2009/early 2010 and introduce legislative amendments into LegCo in 2010-11.

*(g) Revisiting corporate rescue*

30. We have revisited the proposal to introduce a corporate rescue procedure for companies in financial troubles to provide a statutory “grace period” for companies facing short-term financial difficulties but are viable in the longer term, so that they can restructure their business or debts, or seek capital injection to turn themselves around. We will issue a consultation paper on the proposed legislative proposals shortly. Subject to the outcome of the consultation, we plan to prepare draft legislation for introduction into LegCo in 2010-11.

*(h) Broadening the source of listed companies*

31. In March 2007, HKEx published a joint statement with the SFC aiming at facilitating the listing of overseas companies by clarifying requirements in the Listing Rules and providing a clear roadmap for potential issuers and their advisers to refer to regarding key shareholder protection matters. Since then, the Listing Committee of the Stock Exchange of Hong Kong (“SEHK”) has continuously expanded the list of approved jurisdictions of incorporation for overseas companies seeking a listing on the SEHK<sup>4</sup>. In September 2009, HKEx issued a Guidance Letter on listing of overseas companies, introducing market facilitating vetting practices in the IPO listing process. The HKEx is also conducting a consultation on proposals to strengthen Hong Kong’s role as an important listing centre for mineral and exploration companies. HKEx will continue its marketing efforts in attracting Mainland and overseas companies to list in Hong Kong.

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<sup>4</sup> As of September 2009, eight jurisdictions (ie Australia, Canada (British Columbia), Canada (Ontario), Cyprus, Germany, Luxembourg, Singapore and United Kingdom) have been accepted for this purpose, which are in addition to the four jurisdictions recognised under the Listing Rules (ie Hong Kong, the PRC, Bermuda and the Cayman Islands).