

立法會
Legislative Council

LC Paper No. LS29/10-11

**Paper for the House Committee Meeting
on 25 February 2011**

**Legal Service Division Report on
Subsidiary Legislation Gazetted on 18 February 2011**

Date of tabling in LegCo : 23 February 2011

Amendment to be made by : 16 March 2011 (or 13 April 2011 if extended
by resolution)

Securities and Futures Ordinance (Cap. 571)

**Securities and Futures Ordinance (Amendment of Schedule 5) Notice 2011
(L.N. 28)**

**Securities and Futures (Financial Resources) (Amendment) Rules 2011
(L.N. 29)**

Under the Securities and Futures Ordinance (Cap. 571) (SFO), corporations must be licensed and authorized financial institutions must be registered if they carry on a business in a regulated activity or hold themselves out as doing so in Hong Kong, or actively market whether in Hong Kong or outside Hong Kong to the public any services they provide that would constitute a regulated activity if provided in Hong Kong. In addition, an individual performing a regulated function in relation to a regulated activity carried on as a business or holding himself out as performing such function, or actively marketing whether in Hong Kong or outside Hong Kong to the public any function the individual performs which would constitute a regulated function if performed in Hong Kong must be a licensed representative accredited to the licensed corporation or an individual whose name is registered by the Monetary Authority as engaged by a registered institution in respect of a regulated activity.

2. Schedule 5 to the SFO sets out 9 types of activities regulated by the Securities and Futures Commission (SFC) (under Part 1) and the related definitions concerning the licensing and registration matters of those regulated activities (under Part 2).

L.N. 28

3. L.N. 28, which is made by the Financial Secretary under section 142 of the SFO, amends Schedule 5 to the SFO by adding a new type of regulated activity to Part 1 of the Schedule- "Type 10 : providing credit rating services". The effect of this amendment is that the existing regulatory regime under the SFO will apply to corporations, authorized financial institutions and individuals providing credit rating services in Hong Kong.

4. Under L.N. 28, Type 10 regulated activity relates to the preparation of opinions, expressed using a defined ranking system, primarily regarding the creditworthiness of a person other than an individual, debt securities, preferred securities or an agreement to provide credit. It does not include the following activities:

- (a) preparing, pursuant to a request made by a person, a credit rating which is exclusively prepared for, and provided to, the person and that is neither intended for dissemination to the public or distributed by subscription, whether in Hong Kong or elsewhere, nor reasonably expected to be so disseminated or distributed; or
- (b) gathering, collating, disseminating or distributing information concerning the indebtedness or credit history of any person.

L.N. 29

5. L.N. 29 is made by SFC under section 145 of the SFO (after consultation with the Financial Secretary) to amend the Securities and Futures (Financial Resources) Rules (Cap. 571 sub. leg. N) (FR Rules) to provide for paid-up share capital requirements and liquid capital requirements for corporations licensed for Type 10 regulated activity and connected matters. The major amendments are as follows:

- (a) a reference to Type 10 regulated activity is added to section 5 of and Schedule 1 to the FR Rules so as to impose a duty on corporations licensed for Type 10 regulated activity to maintain a minimum paid-up share capital and required liquid capital as prescribed in Schedule 1 to the FR Rules; and
- (b) a reference to Type 10 regulated activity is added to section 56 of the FR Rules so as to impose a duty on corporations licensed for Type 10 regulated activity to submit periodic returns to SFC.

6. According to paragraphs 2 and 3 of the LegCo Brief issued by Financial Services Branch of the Financial Services and the Treasury Bureau on 18 February 2011 (Ref.: SUB/14/1/5 (2010)), L.N. 28 and L.N. 29 are introduced following G20's consensus on the need to subject credit rating agencies (CRAs) to a regulatory oversight regime. Further, the Administration considers that it would be in the public interest to establish such a regulatory oversight regime in Hong Kong to enhance investor protection and to enable credit ratings prepared by Hong Kong-based CRAs to continue to be serviceable in other jurisdictions. According to paragraph 5 of the LegCo Brief, in order to ensure that the credit ratings are independent, objective and of appropriate quality, SFC will impose minimum conduct standards for CRAs in Hong Kong and their rating analysts by means of a Code of Conduct for Persons Providing Credit Rating Services¹ (CRA Code of Conduct).

7. L.N. 28 and L.N. 29 will come into operation on 1 June 2011.

8. According to paragraph 11 of the LegCo Brief, SFC conducted a public consultation exercise from 19 July 2010 to 20 August 2010 on the proposal to establish a regulatory regime for CRAs and received support from members of the public to the proposal.

9. The Panel on Financial Affairs discussed at its meeting held on 19 July 2010 the Administration's proposal for establishing a regulatory regime for CRAs operating in Hong Kong. Various issues relating to the proposal were discussed at the meeting. These include the efficacy of the proposed regulatory regime, the liability of CRAs and regulatory sanction for breach of the future CRA Code of Conduct, international co-operation in regulating CRAs and mechanism to ensure independence and objectivity of CRAs. Members of the Panel did not raise objection to the proposal.

10. No difficulties in relation to the legal and drafting aspects of the above items of subsidiary legislation have been identified.

Prepared by

YICK Wing-kin
Assistant Legal Adviser
Legislative Council Secretariat
22 February 2011
LS/S/16/10-11

¹ According to the LegCo Brief, the CRA Code of Conduct would be based on the revised Code of Conduct Fundamentals for Credit Rating Agencies issued by the International Organisation of Securities Commissions in May 2008. These standards require credit rating activities to be conducted in accordance with the principles of integrity, independence, transparency and confidentiality.