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10 May 2012

Ms Yue Tin-po
Clerk to Bills Committee
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong

Dear Ms Yue,

**Bills Committee on
Trade Descriptions (Unfair Trade Practices) (Amendment) Bill 2012**

**Administration's Response to Bills Committee
arising from the Discussion at the meetings on 21 March and 12 April 2012**

I write to respond to two issues raised by Members of the Bills Committee on the Trade Descriptions (Unfair Trade Practices) (Amendment) Bill 2012 (the Bill) at its meetings held on 21 March and 12 April 2012.

Existing Investors Protection under Current Financial Regulatory Regimes

2. At the meeting on 21 March 2012, Members sought information on the protection under the current financial regulatory regimes against practices akin to those to be prohibited under the Bill.

3. We have proposed in the Bill that financial services products described in new Schedule 4 (introduced by clause 23) will not be brought under the ambit of the expanded Trade Descriptions Ordinance (Cap. 362). There are well-established and tailor-made regulatory regimes governing product authorization, intermediary regulation and the selling process under various Ordinances. They are enforced by relevant financial market regulators including the Securities and Futures Commission ("SFC"), the Hong Kong

Monetary Authority (“HKMA”), the Mandatory Provident Fund Schemes Authority (“MPFA”), the Insurance Authority (“IA”) and other market operators and professional bodies. Our financial regulatory regimes are on par with international practices. Under these regimes, the regulatory requirements are devised in the light of the nature of the financial services products with a view to ensuring a fair, orderly and open market to protect investors. Generally speaking, these regulatory requirements seek to protect investors from misleading or deceptive practices, and require the disclosure of information relevant for investors to make an informed decision. They seek to address problems similar to those that the Bill seeks to tackle.

4. We set out in the ensuing paragraphs some notable examples representative of the regulatory approach adopted for financial services products.

Product Authorisation

5. Before investment products are to be offered to the public of Hong Kong, they must be authorised by the SFC in accordance with the Securities and Futures Ordinance (Cap. 571) (“SFO”). Those products include unit trusts/mutual funds, investment-linked assurance schemes and unlisted structured investment products. Issuers of these products must ensure compliance with the Handbook for Unit Trusts and Mutual Funds, Investment-linked Assurance Schemes and Unlisted Structured Investment Products issued by the SFC (“the SFC Handbook”).

6. The SFC Handbook was introduced by the SFC in June 2010 after the global financial crisis, with a view to strengthening the regulatory regime of publicly offered investment products in Hong Kong. The SFC Handbook aims to enhance the transparency for various types of products so as to promote investor protection. It includes a requirement for issuers to provide product key facts statements that summarise the key features and risks of the investment products. It covers areas such as duties and obligations of product providers, disclosure requirements, ongoing monitoring of the product and disseminating information to investors. Besides, the SFC Handbook contains the new Product Code for Unlisted Structured Investment Products, which aims to strengthen the regulation of these products.

Regulation of Intermediaries

7. Intermediaries selling investment products to the public of Hong Kong are subject to licensing requirements. Under the SFO, dealing in securities and

futures contracts and advising on securities and futures contracts are “regulated activities”. Any person must be licensed by the SFC before they can engage in these regulated activities. Banks conducting business in Hong Kong are regulated by the HKMA. They must be authorised by the HKMA. If any bank wishes to carry on “regulated activities”, it must be registered with the SFC as well.

8. The SFC is guided by section 129 of the SFO and the Code of Conduct for Persons Licensed by or Registered with the SFC (“the SFC Code”) when considering whether a person is fit and proper to be or remain licensed or registered for conducting intermediary services for investors. In particular, sections 129(1)(c) and (d) of the SFO stipulate that the SFC will give due regard to the ability of the person to carry on the regulated activity competently, honestly and fairly; and his/her reputation, character, reliability and financial integrity. General principle 1 (honesty and fairness) of the SFC Code requires that, in conducting its business activities, a licensed or registered person should act honestly, fairly, and in the best interests of its clients and the integrity of the market. General principle 2 (diligence) of the SFC Code requires that, in conducting its business activities, a licensed or registered person should act with due skill, care and diligence, in the best interests of its clients and the integrity of the market.

9. The Mandatory Provident Fund Schemes (Amendment) (No. 2) Bill 2011 now being scrutinized by a Bills Committee in the Legislative Council requires an MPF intermediary to act honestly, fairly, in the best interests of the client, and with integrity, among others. The MPFA is empowered to issue guidelines in this regard to cover the said situations should the need arise in future.

10. In other words, the financial services intermediaries are subject to a fit and proper test not only at the entry point, but also on an ongoing basis. Regulators, through routine inspections, maintain their market surveillance efforts over their licencees. They will investigate into any suspected breach of the relevant requirements and follow up with disciplinary/prosecution proceedings as appropriate.

Selling Process

11. Requirements in respect of steps before, during and after the selling process are in place to protect retail investors. For “pre-selling”, section 93(1)(a) of the Banking Ordinance (Cap. 155) (“BO”) provides that it is an offence for any person who, by any fraudulent or reckless misrepresentation,

induces another person to make a deposit. Under section 95(1) of the BO, where the Monetary Authority is of the opinion that any advertisement issued in connection with the business of an authorized institution (including a bank) makes a statement or any representation that is false, misleading or deceptive, he may, by written notice served on the institution, require the institution to withdraw or remove, and to cease issuing such advertisements. Section 107 of the SFO also prohibits the making of fraudulent or reckless misrepresentation for the purpose of inducing another person to enter into or offer to enter into an agreement to acquire, dispose of, subscribe for or underwrite certain financial services products. Making false, misleading or deceptive statements or dishonest concealment of material facts with a view to inducing another person to enter into any contract of insurance is also an offence under section 56 of the Insurance Companies Ordinance (Cap. 41).

12. During the selling process, the SFC Code requires that licensees should take reasonable steps to establish the true and full identity of each of its clients, and of each client's financial situation, investment experience, and investment objectives. Licensees should, as part of the “Know Your Client” (“KYC”) procedures, assess the clients’ knowledge of derivatives and characterize the clients based on his knowledge of derivatives. Having regard to information about a particular client, licensees should, when making a recommendation, ensure the suitability of the recommendation for that client is reasonable.

13. On “post-selling” requirements, protective measures for potential policyholders are set out in the guidelines issued by the Hong Kong Federation of Insurers. For example, policyholders are given a 21-day cooling-off period to review the terms and conditions of their life insurance policies. For investment-linked assurance schemes, insurers are required to make a post-sale call to vulnerable customers to seek their confirmation before the end of the cooling-off period and the call should be recorded. Written communication should be sent where phone contact cannot be established. These measures were introduced after discussion with the IA.

Conclusion

14. We believe that our financial regulatory regimes, and specific measures like those described above, provide reasonable protection to retail investors on par with international practices. The Administration and our financial regulators will continue to improve our financial regulatory regimes in light of evolving local market needs and international regulatory agenda with a view to maintaining our competitiveness as an international financial centre.

Puff

15. At the meeting on 12 April 2012, Members asked if there were case law to illustrate whether mere opinions or trade puff (as opposed to factual statements) about goods or services would amount to “trade descriptions” as defined under the Bill.

16. In respect of the UK Trade Descriptions Act 1968 on which the provisions on false trade descriptions of goods in the Trade Descriptions Ordinance are modelled, it was held in *Cadbury Limited v Halliday* [1975] 1 WLR 649 that the term “trade descriptions” is limited to matters the truth or falsity of which can be established as a matter of fact. Likewise, the British Court has held that “the traditional rule is that a misrepresentation must be a false statement of fact, past or present, as distinct from a statement of opinion.”¹ On the other hand, a statement is treated as a mere puff “if the court considers that it was not seriously meant and that this should have been obvious to the person to whom it was made.”² It follows that a mere puff should not be regarded as a trade description.

Yours sincerely,



(Daniel Fong)

for Secretary for Commerce and Economic Development

c.c. Secretary for Financial Services and the Treasury

(Attention: Ms Sara Tse)

Commissioner of Customs and Excise (Attention: Mr SY Cheung)

Secretary for Justice

(Attention: Mr Eamonn Moran

Miss Ada Chen

Mr Peter Sze

Mr David Grover)

¹ *Chitty on Contract: Volume I – General Principles (29th edition)* p. 431 as cited with approval in *Hummingbird Motors Ltd. v Hobbs* [1986] R.T.R. 276

² *Chitty on Contract: Volume I – General Principles (29th edition)* p. 202