

**Re: Bills Committee on Securities and Futures and Companies Legislation
(Uncertificated Securities Market Amendment) Bill 2014 (Bill)**

We refer to your letter of 23 July 2014 to The Hong Kong Institute of Chartered Secretaries (HKICS) calling for comments on the above Bill which is being considered by a Legislative Council (**LegCo**) Bills Committee with Hon Christopher Cheung as chair.

Introduction

HKICS is the industry organisation representing Chartered Secretaries as governance professionals in Hong Kong and China. HKICS is rooted with the Institute of Chartered Secretaries and Administrators (ICSA) in the United Kingdom with 9 divisions and some 33,000 members. It is also a founder member of the Corporate Secretaries International Association (CSIA) an international organisation comprising 19 national member organisations to promote good governance globally.

General Support

At the outset, we wish to express our general support for the introduction by the Administration of the Bill to LegCo to align Hong Kong with the practices of jurisdictions like Australia, China, Japan and the UK that have already implemented an uncertificated securities market. Specifically we support the move from a paper certificated regime to an uncertificated securities market regime as this will enhance: (1) Hong Kong's reputation as a world class international financial centre; (2) the overall efficiency of the securities market; (3) the development of cross border products, including with China under the Shanghai-Hong Kong Stock Connect; and (4) investor protection with the ability of investors to take legal title to their securities, as against only having a beneficial interest. All these are consistent with good governance and best practices which we serve to promote.

SFC Regulatory Role

We also welcome the Securities and Futures Commission's (SFC's) oversight of the regulatory and operational matters relating to the new uncertificated securities market environment, including the implementation of an authorisation regime in respect of share registrar services. These will provide strong regulatory oversight over the uncertificated securities market regime, and international attention of Hong Kong's development through SFC's membership with IOSCO.

The Concerns

As our members are involved in company administration, we have identified a number of concerns, which may need to be dealt with under the current amendment or further subsidiary legislations:

1. **Paper Costs.** The assumption with the proposal is that there will be a reduction of paper, and hence consequently, costs to listed issuers. This assumption needs to be revisited.

Under the current regime, beneficial shareholders holding their shares with CCASS are not recorded in the register of members of a listed company as members. With the implementation of the uncertificated regime, the number of registered members will in all likelihood significantly increase, along with the quantities of (a) printed corporate communications, e.g. annual and interim reports, circulars and notification letters, to be sent to shareholders under Listing Rule 2.07 (*Delivery of Information and Documents* http://www.hkex.com.hk/eng/rulesreg/listrules/mbrules/documents/chapter_2.pdf); and (b) printed dividend cheques and advices to be sent to shareholders by post.

Individual consent (including individual deemed consent) is required under Listing Rule 2.07 and section 833 of the Companies Ordinance (*on communication by means of website* http://www.cr.gov.hk/en/companies_ordinance/companies_ordinance.htm) for a listed company to send corporate communications to shareholders by electronic means (including by publication on a website). Even if a shareholder has consented to receiving corporate communications by electronic means, the listed company will still be required to send a letter informing the shareholder every time a corporate communication has been published on its website in relation to those shareholders that have not provided an email address for communication, which from experience would be significant. This is notwithstanding that many shareholders already read corporate communications on a listed issuer's website without the need to be individually informed by a printed letter through the post.

Thus, the uncertificated regime, with its increase in the number of registered shareholders, would most probably result in an increase in printed papers, along with additional costs to listed issuers.

In order to resolve the problem, consideration should be given to mandating shareholders holding shares in uncertificated form to (a) provide email addresses for recording in the members register (uncertificated shares); (b) be deemed to have given consent to receive corporate communications by electronic means; (c) receive their dividends via autopay to bank account (for shareholders holding bank accounts in Hong Kong); (d) receive their dividend advices by electronic means; and (e) to complete and send proxy forms for voting at shareholders' meetings by electronic means (or to vote their shares via an online voting facility to be provided by the Hong Kong Stock Exchange). Please note that the Shanghai Stock Exchange provides an online voting facility for shareholders to vote on their A shares.

2. Clearing Costs. As stated under paragraph 16 of the Administration's LegCo Brief: *"The guiding principles with respect to fees under the proposed regime are that fees should be reasonable (for all parties concerned), commensurate with services provided, conducive to encouraging innovation and market development, and should not offset the longer term benefits of an uncertificated securities market environment. To that end, we propose to amend section 76 of the SFO to provide that the fees charged by an [Recognized Clearing House] RCH which is the system operator of an uncertificated securities market system are subject to the SFC's approval."*

In this connection, we subscribe to the principle that “user pays”. As such, we submit that the costs relating to the funding of an RCH, and increased costs of share registration services, by reason of Share Registrars as custodians of certificated securities having to maintain two sets of registrars relating to traditional certificated securities and uncertificated securities with the RCH should not be pushed down to listed issuers but spread amongst investors as users of the uncertificated securities regime. The important point is that listed issuers should not be disallowed to recover costs from the implementation of the uncertificated securities market regime. It may well be that there needs to be some form of transaction levy or funds from market activities to deal with such additional costs incurred under the uncertificated securities market regime.

3. Dispute Resolution. We have a concern relating to the timing for resolution of disputes under the uncertificated securities market regime. For example, under the draft provisions of s.158A of the Companies Ordinance, the traditional timings of 28 days and 2 months were referred to in relation to certain procedural matters. We submit that there may be need to develop a speedy and cost effective mechanism to resolve disputes, for example through some panel mechanism prior to any recourse to the Court system. If the uncertificated regime professes to enhance efficiencies, there must be supporting infrastructures to achieve the objective, instead of a traditional fall back to the Court system in the first instance for dispute resolutions.

4. Privacy. In accordance with the Company Records (Inspection and Provision of Copies) Regulation (Cap 622I), the public may inspect the register of members of listed companies at the offices of the share registrars. The information of the register of members available for public inspection include the shareholders’ names, residential addresses and numbers of shares held. This may cause concern to certain investors who would like to maintain their privacy, in particular their residential addresses. The Privacy Commissioner may need to be consulted in regard to the privacy issue.

5. Implications for H shares. An H share issuer is obliged to withhold and pay PRC enterprise income tax on behalf of non-resident enterprise shareholders at a tax rate of 10% from 2008 onwards when the H share issuer distributes any dividends to non-resident enterprise shareholders whose names appear on the register of members of H shares of the H share issuer (*in accordance with the “Enterprise Income Tax Law of the People’s Republic of China” (《中華人民共和國企業所得稅法》) and the “Rules for the Implementation of the Enterprise Income Tax Law of the People’s Republic of China” (《中華人民共和國企業所得稅法實施條例》), both implemented on 1st January 2008 and the “Notice of the State Administration of Taxation on Issues Relevant to the Withholding of Enterprise Income Tax on Dividends Paid by PRC Enterprises to Offshore Non-resident Enterprise Holders of H Shares” (Guo Shui Han [2008] No. 897) (《關於中國居民企業向境外H股非居民企業股東派發股息代扣代繳企業所得稅有關問題的通知》(國稅函[2008]897 號)) promulgated on 6th November 2008).*

As such, any H shares of the H share issuer which are not registered in the names of individuals (which, for this purpose, includes shares registered in the name of HKSCC Nominees Limited, other nominees, trustees, or other organisations or groups) are deemed to be H shares held by non-resident enterprise shareholders, and the PRC enterprise income tax is withheld from any dividends payable thereon.

Individual shareholders holding H shares in their portfolio are therefore expected to opt for holding securities in uncertificated form rather than in the name of nominees so that they will receive their H share dividends in full potentially without the 10% PRC enterprise income tax deduction. This issue needs to be dealt with for the proper development of the uncertificated securities market regime.

6. Shares Held on Trust and Intra Group Relief. There may be need for special arrangements for stamp duty adjudication, payment and refund in respect of the transfer of shares in uncertificated form from: (a) trustee to beneficial shareholder; (b) beneficial shareholder to trustee; and (c) where stamp duty relief for intra group transfer of shares under section 45 of the Stamp Duty Ordinance (Cap 117) (*"Intra Group Relief - Transfer or Sale of Hong Kong Stock and Immovable Property"*) <http://www.ird.gov.hk/eng/pdf/irsd124.pdf>).

7. Attendance at Shareholders' Meetings. A significant increase in the number of persons on the register of members of a listed company will pose certain logistical challenges. There is a limitation of suitable conference venues in Hong Kong, and costs are going up. If the uncertificated regime is to be implemented, there is a need for Hong Kong to follow Shanghai Stock Exchange which provides an online voting facility for shareholders to vote on their A shares.

Should you have any questions, please feel free to contact Mohan Datwani, Director, Technical and Research at 2881 6177 or mohan@hkics.org.hk

Yours faithfully,

For and on behalf of
The Hong Kong Institute of Chartered Secretaries

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