

立法會
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**Bills Committee on
Securities (Margin Financing) (Amendment) Bill 1999**

**Minutes of meeting held on
Tuesday, 29 June 1999, at 4:30 pm
in Conference Room A of the Legislative Council Building**

- Members present** : Hon Ronald ARCULLI, JP (Chairman)
Hon Albert HO Chun-yan
Hon SIN Chung-kai
Hon FUNG Chi-kin
- Members absent** : Hon Bernard CHAN
Hon Jasper TSANG Yok-sing, JP
- Public officers attending** : Mr Bryan CHAN
Principal Assistant Secretary for Financial Services
- Miss Hinny LAM
Assistant Secretary for Financial Services
- Mr William MADDAFORD
Senior Assistant Law Draftsman
Department of Justice
- Ms Vicki LEE
Government Counsel
Department of Justice

Attendance by : Securities and Futures Commission
Invitation

Mr Andrew PROCTER
Executive Director of Intermediaries and
Investment Products

Mr Richard YIN
Director of Intermediaries Supervision

Mrs Yvonne MOK
Associate Director of Intermediaries Supervision

Mr Leo LEE
Director of Licensing

Mr CHUNG Hing-hing
Associate Director of Licensing

Clerk in attendance : Ms Estella CHAN
Chief Assistant Secretary (1)4

Staff in attendance : Mr KAU Kin-wah
Assistant Legal Adviser 6

Ms Connie SZETO
Senior Assistant Secretary (1)1

I Meeting with the Administration

Clause-by-clause examination of the Bill

Clause 2 - Interpretation

The Chairman pointed out that the word "registered" was already defined in the existing Securities Ordinance (SO) (Cap. 333) and that definitions of the terms "securities margin financier" and "securities margin financier's representative" were also provided in the proposed section 2(1). Since the meaning of "financier" and "securities margin financier" was identical for the purpose of the Bill, for the sake of drafting clarity, he suggested that the Administration should consider deleting definitions of "registered financier" and "registered financier's representative" from the Bill.

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2. Responding to members' enquiries, the Executive Director of Intermediaries and Investment Product, Securities and Futures Commission (ED/IIP(SFC)) explained that only incorporated entities could apply for registration as a "securities margin financier" (SMF). "Securities margin financier's representatives" were either directors of the financier who were directly responsible for supervising the business, or employees or agents (e.g. the account executives) of the financier who were directly involved in providing securities margin financing service to clients. Section 121H(4) specified the fit and proper criteria that a person had to satisfy for registration as a SMF's representative. A registered SMF was prohibited from carrying on securities margin financing business unless at least one of its directors was approved by SFC under section 121I. As such, there might be more than one directors working for the financier but at least one of them had to be an "approved director". ED/IIP(SFC) added that it would be proposed under the composite Securities and Futures Bill to require at least two "approved directors" for a registrable business since the present requirement of only one "approved director" could give rise to practical problems particularly when the sole "approved director" was not able to supervise the business for some reasons.

Clause 3 - Division 2

(Registration of securities margin financier)

3. The Chairman expressed concern about the provisions under sections 121C(3) and 121D(3) which stipulated that a SMF or a SMF's representative would be regarded as unregistered when their registration was suspended. Noting the low penalties prescribed in sections 121C(2) and 121D(2) for contravening sections 121C(1) and 121D(1), he opined that there was an apparent lack of control over unregistered financiers and their representatives in the Bill whose activities might seriously jeopardise the interests of the investing public.

4. The Director of Licensing, Securities and Futures Commission advised that SFC could take prosecution actions against the suspended SMF or SMF's representative for continuing to act without registration. If the SMF or SMF's representative continued to defy the suspension order, SFC could revoke their registration as provided in sections 121S(3) and 121U(3). A SMF could be prosecuted for aiding and enabling unregistered representatives in carrying out securities margin financing activities. SFC could also initiate inquiry into the fitness and properness of such SMF for continued registration. Other powers available to SFC in respect of regulation of registrants' business included the issuance of restriction notice limiting the scope of business of a SMF as provided under section 39 of the Securities and Future Commission Ordinance (SFCO) (Cap. 24), and the application of a court order as provided under section 144 of SO restraining the business of a SMF if this was warranted in the public interest. ED/IIP(SFC) supplemented that there were provisions in section 121X of the Bill

stipulating that a SMF or its representatives could not re-apply for registration within 12 months after revocation of their registration. In respect of regulation of SMF's representatives, besides revoking the registration, thus barring them from being employed in the capacity of SMF's representatives, SFC could issue restriction notice to a SMF with the condition that the financier could not engage the suspended representatives in conducting its business.

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SFC 5. The Chairman pointed out the anomalies between sections 121C(3) and 121S(3), as well as between sections 121D(3) and 121U(3). He wondered whether SFC could "revoke the registration" of a SMF or a SMF's representative when they were regarded as "unregistered". He urged the Administration to review these provisions.

Admin. 6. On section 121D(1)(b), ED/IIP(SFC) undertook to consider the Chairman's suggestion to review the drafting in relation to the need of the phrase "is prepared to act".

7. As to section 121E(2), members noted that the age requirement of 18 years was prescribed for registration as a SMF's representative. They noted the Administration's explanation that it would be in conflict with anti-discrimination legislation to set an age requirement above 18 for an "approved director". However, the fit and proper criteria for assessing applications for approved directorship would include a combination of tertiary education and working experience which could hardly be attained by persons at the age of 18. Hence, it was almost certain that an "approved director" would always be above the age of 18. Members also noted that, theoretically speaking, it would be possible for an incorporated entity to apply for registration as a SMF's representative. But this was considered inappropriate in practice since SFC would have difficulties in assessing such an application. Hence, the phrase "a natural person" was adopted in section 121E(2).

Admin. 8. On section 121F(3), members noted the Assistant Legal Adviser's view that the provisions were inconsistent with section 24 of SFCO and that the Administration had undertaken to propose Committee Stage amendments (CSA) in this respect to specify the types of additional information that SFC might require from an applicant in relation to the application for registration as a SMF or a SMF's representative.

SFC 9. Responding to the Chairman's enquiry about the reasons for not including any financial penalty in section 121F(4) for the offence of making false information in the application for registration, ED/IIP(SFC) advised that a similar provision was in section 62(1) of the existing SO concerning false representation for the purpose of obtaining a certificate of registration of a securities dealer or its representatives. In view of members' concern, he undertook to examine SFC's past enforcement records to review the need of

providing a financial penalty in this section and revert to the Bills Committee.

Admin. 10. At members' request, the Administration agreed to consider recasting section 121F(6) as "...under subsection (4) may not be brought more than 6 months after the discovery of the offence."

11. On section 121G, members questioned the need for splitting the situations under which SFC could refuse applications for registration as a SMF into subsections (2), (3) and (4). They also remarked that the condition provided under subsection (2)(a) that "the applicant is not eligible to make the application" should result in rejection of the application for certain.

Admin. 12. ED/IIP(SFC) explained that while sections 121G(3) and (4) stipulated those situations under which SFC "must" refuse the application, section 121G(2) listed out factors which SFC "may" consider in making a judgement when assessing the application. This would provide SFC with flexibility since if the situations prescribed under subsection (2) were improved or rectified, SFC could reconsider the application. The Administration undertook to consider members' suggestion of recasting sections 121G(3) and (4) to include the condition stated under 121G(2)(a).

13. Referring to the concern about the need of section 121G(2)(d) which was concerned with the mental conditions of directors of a SMF, ED/IIP(SFC) remarked that although SFC might invoke subsections (5) (c) and (d) to refuse a financier's application if any of its director was or being suspected of suffering from mental disorder, it might not be easy to establish a relationship between "mental disorder" of a director and his ability to perform "efficiently, honestly and fairly" as well as his "reputation and reliability". Hence, it was necessary to have section 121G(2)(d) to put beyond doubt that "mental condition" of financier's officers was a factor of consideration in the application for registration. Concerning ways by which SFC could learn about changes in mental conditions of directors of registered financier, ED/IIP(SFC) said that in compliance with the Code of Conduct, registrants would have an obligation to report to SFC on any material change relating to their registration. SFC would learn about such changes through registrants' routine returns and would be able to detect irregularities during inspection visits to finance companies.

Admin. 14. On section 121G(6), ED/IIP(SFC) advised that the provision was analogous to that under sections 23(4) and (5) of SFCO. The proposed provision was to put beyond doubt that SFC could take into consideration all relevant information, including documentary information and interviews with applicants or other persons etc., in assessing the application. To address members' concern about inconsistency in the drafting of sections 121G(6) and 121H(5), the Administration undertook to consider recasting the two sections as "For the purposes of this section, the Commission may have regard to any information in

its possession."

15. Upon the Administration's advice that the "opportunity of being heard" before a refusal of the application for registration as a SMF was made as provided in section 121G(8) would be in the form of inviting written representation from the applicant concerned, the Chairman opined that it might be more appropriate to adopt the phrase "opportunity to make representation" in the drafting. In response, ED/IIP(SFC) said that similar provisions were found in existing law and had not given rise to problem so far. He also advised that all licensing decisions made by SFC were subject to review by the Securities and Futures Appeals Panel which was constituted of lay members.

16. Pointing out that the provisions requiring SFC to give reasons for refusal of application for registration as a SMF, a SMF's representative or an "approved director" were provided under sections 121G(9), 121H(7) and 121I(8), Mr Albert HO opined that a similar provision should be added in section 121J requiring SFC to give reasons for the imposition of special conditions or restrictions on granting the registration under section 121J(1)(b). ED/IIP(SFC) advised that notwithstanding such requirement was not expressly provided in section 121J, as a matter of fair administrative practice, registrants would be provided with reasons for the imposition of conditions or restrictions to facilitate them in preparing for the representation under section 121J(3). SFC considered that sufficient protection ensuring procedural fairness had been built into section 121J(3). Mr HO was not convinced of SFC's explanation. After deliberation, the Admin. Chairman suggested and the Administration agreed to consider adding a provision under section 121J to the effect that SFC would be required to furnish reasons for its decisions of imposing special conditions or restrictions on the registration to the relevant person if so requested.

17. When examining section 121K, members noted that failure of a registered SMF to provide the specified security required by SFC could result in SFC issuing a restriction notice, such as imposing trading caps to limit the operation of its business, or taking other disciplinary actions including suspension or revocation of registration. ED/IIP(SFC) advised that the power to issue restriction notice was a non-delegated authority to be exercised by the full board of SFC. Restriction notice would be served upon the concerned registrant and related third parties. The notice would prohibit a SMF from engaging in new business but not restrict him from undertaking activities to protect the interests of clients such as closing out their positions, or returning their scrips.

18. From sections 121L and 121M, members noted that the certificate of registration issued to a SMF's representative would specify the name of the SMF for whom the representative was authorised to act. The certificate would be valid as long as it was in force. Registered representatives would be required to pay annual fees and file annual returns with SFC for renewal of the certificate. A

registered representative would be required to apply for a new certificate whenever he switched to work for another SMF. In some cases, the representative who was in the process of applying for a new certificate would be permitted to work for the new employer in a restricted capacity. ED/IIP(SFC) assured that in case where there was little or no change in the representative's duties, SFC would be able to issue the new certificate fairly quickly.

19. When examining section 121N, members expressed grave concern that while subjecting registered financiers and their business to stringent regulation, the Bill did not seem to provide sufficient sanction against unregistered operators carrying out margin financing activities. They were surprised learning from SFC that offences in relation to the conduct of margin financing activities by unregistered operators would be dealt with by the Police rather than SFC, who was the market regulator.

20. In response, ED/IIP(SFC) remarked that if the unregistered financier was operating in relation with a registered securities dealer, SFC could invoke supervisory and investigative power vested under sections 30 and 33 of SFCO respectively to obtain information from the "registered person". Section 36 of SFCO provided that SFC could apply for a magistrate's warrant, in conjunction with the powers provided under sections 30 and 33, to enter the premises of a SMF and search for, seize or remove any relevant records or documents. SFC could also apply for court orders under section 144 of SO to restrain business operation of suspected unregistered financiers and to appoint administrator for the protection of clients' assets. Moreover, SFC could petition to the court, under sections 45 and 46 of SFCO, for expeditious winding up or bankruptcy of a company, if it was in the public interest to do so. In view of members' concern, SFC he undertook to provide more details regarding SFC's power over unregistered dealing cases after the meeting.

II Any other business

21. Members noted that the next meeting would be held on 7 July 1999, at 8:30 am.

22. The meeting ended at 6:45 pm.