

Proposed amendments to the Securities (Margin Financing)(Amendment) Bill 1999

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| 1. | 2 | <ul style="list-style-type: none"> To delete the definition of “agent”. | <ul style="list-style-type: none"> Technical amendment. Also for consistency with existing provision in the Ordinance. | <ul style="list-style-type: none"> Reflected in the CSA (clause 2(a) refers). | 20, 26 |
| 2. | 2 | <ul style="list-style-type: none"> The Bills Committee requested the Administration to review the need for the definition of “audit”. | <ul style="list-style-type: none"> As SFC has clarified at the Bills Committee meeting, in actual practice the interpretation of “audit” for the purposes of the Securities Ordinance includes “examination”. For drafting clarity and certainty, it is considered appropriate to retain the definition. | <ul style="list-style-type: none"> No CSA is proposed. | 20 |
| 3. | 2 | <ul style="list-style-type: none"> In the definition of “financial accommodation”, to add “a” before “discounted” and “guarantee” respectively. | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA (clause 2(b) refers). | |
| 4. | 2 | <ul style="list-style-type: none"> To add the definition of “margin ratio” and “margin value”. | <ul style="list-style-type: none"> Technical amendments. | <ul style="list-style-type: none"> Reflected in the CSA (clause 2(c) refers). | |
| 5. | 2 | <ul style="list-style-type: none"> To consider whether amendment to the definition of “record” is necessary in order to ensure that records in electronic form will also | <ul style="list-style-type: none"> Our legal advice confirms that the present formulation of the definition of “record” together with | <ul style="list-style-type: none"> No CSA is proposed. | |

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| | | be covered in the light of advancement in technology. | that of “document” are broad enough to cover electronic record as well. Therefore no CSA is proposed. | | |

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| 6. | 2 | <ul style="list-style-type: none"> In the definition of “securities margin financier’s representative”, to delete “an employee or agent of” and substituting “a person in the employment of, or acting for or by arrangement with,”. | <ul style="list-style-type: none"> Technical amendments. Consequential to the deletion of definition of “agent” (please see also item 1 above). | <ul style="list-style-type: none"> Reflected in the CSA (clause 2(d) refers). | |
| 7. | 2 | <ul style="list-style-type: none"> To amend the definition of “securities collateral” to cover also securities deposited by clients with a securities dealer as security for purposes other than the provision of financial accommodation and thereby subject to the protection given under section 81A by adding a new subparagraph as follows – “(c) for the purpose of section 81A only, with the dealer as security for purposes other than for the provision of financial accommodation;” | <ul style="list-style-type: none"> It is the market practice for securities dealers to deposit collateral from clients when clients wish to engage in short selling or trading in Exchange-traded options. It is not clear whether this will amount to financial accommodation, as the securities dealers may not be extending a loan of money to clients in these circumstances. It is therefore appropriate that such securities collateral should be dealt with in accordance with the proposed section 81A. | <ul style="list-style-type: none"> Draft CSA under formulation. | |
| 8. | 2 | <ul style="list-style-type: none"> To consider if separate definitions for “registered financier” and “registered financier’s representative” are necessary | <ul style="list-style-type: none"> We are advised that the present approach of using “registered financier” and “registered financier’s representative” is in order from the drafting point of view and necessary in the structure | <ul style="list-style-type: none"> No CSA is proposed. | |

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| | | | of the Bill. | | |
| 9. | 121B | <ul style="list-style-type: none"> To provide the exemption list now listed in section 121B(2) under a new Schedule 4 of the Ordinance which may be amended by the Commission by way of subsidiary legislation. To delete subsection (3). A new subsection is added to clarify that Part XA applies to all business (including any of the kinds of business listed in the new Schedule 4) carried on by a registered financier. | <ul style="list-style-type: none"> The exemption list will be amenable by the Commission by way of subsidiary legislation, providing greater flexibility to the SFC to cope with market changes. Subsection (3) is no longer necessary given the reference to “group of companies” has been removed. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(a) and the new clause on p.9 refer). | 14 |
| 10. | 121B(2)(g) | <ul style="list-style-type: none"> To consider clarifying the meaning of the word “prospectus” as offer documents in other jurisdictions may not be covered by the term. | <ul style="list-style-type: none"> In the paragraph (f) of the new Schedule 4 proposed under the CSA, we have clarified that the exemption will cover “the provision of financial accommodation to facilitate an acquisition of securities in accordance with the terms of a prospectus, regardless of whether the offer of securities is made in Hong Kong or elsewhere”. We believe the policy intent is clear and there is no need to provide a | <ul style="list-style-type: none"> No CSA is proposed. | 27 |

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| | | | specific definition of “prospectus”. | | |
| 11. | 121C | <ul style="list-style-type: none"> To add “Subject to section 121B(2)” in subsection (1). Also to clarify that the registration requirement is only applicable to securities margin financing carried on in Hong Kong. To increase the pecuniary penalty under section 121C(2)(a) to \$1,000,000 on conviction on indictment and \$5,000 per day for continuing offence. Also to increase the penalty under section 121C(2)(b) to level 6 (\$100,000) on summary conviction. To add a new subsection (2A) to provide that if a person who provides financial accommodation and has a reasonable belief that it is not to be used to facilitate acquisition or the continued holding of securities listed on a stock exchange, that person does not contravene section 121C. | <ul style="list-style-type: none"> For clarity (please also see item 9 above). The purpose of the new subsection is to ensure that recklessness cannot be deployed as a defence for contravention of section 121C. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(b) refers). | 7, 55 |
| 12. | 121C(3) and D(3) | <ul style="list-style-type: none"> The Bills Committee wondered if there would be any conflicts between sections 121C(3) and 121D(3), and 121S and 121U, if persons under | <ul style="list-style-type: none"> As explained in our letter dated July 6, we believe there is no conflict between the sections. Section 121D(3) only applies | <ul style="list-style-type: none"> No CSA is proposed. | 30 |

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| | | suspensions would be deemed as unregistered. | where there has been a suspension ordered under another section so, for example, it would operate if a suspension was ordered under section 121U(3)(b). the result under section 121D(3) would be that the person would commit an offence if during the suspension, he acted as a securities margin financier's representative or held himself out as such a representative. Similar explanation in the case of section 121C(3). No CSA is proposed. | | |
| 13. | 121D(1) | <ul style="list-style-type: none"> • In section 121D(1)(b), repeal "is prepared to act". • At the end of section 121D(1), add "in Hong Kong". | <ul style="list-style-type: none"> • Technical amendments | <ul style="list-style-type: none"> • First bull point reflected in the CSA (clause 3(c) refers). • Second one to be included. | 31 |
| 14. | 121E(1) | <ul style="list-style-type: none"> • To replace "company" in section 121E(1)(b) and substitute "person". • To amend section 121E(1)(b) to enable a registered financier to conduct business that is incidental to his carrying on business of | <ul style="list-style-type: none"> • Technical amendment • To allow a financier to engage in other businesses incidental to their conduct of business, e.g. trading in futures and options for hedging | <ul style="list-style-type: none"> • Reflected in the CSA (clause 3(d) refers). | 23 |

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| | | securities margin financing. | purposes | | |
| 15. | 121F(3) | <ul style="list-style-type: none"> To amend section 121F(3) to make it consistent with section 24 of the SFC Ordinance. | <ul style="list-style-type: none"> The proposed section 121F(3) is supposed to be analogous to section 24 of the SFC Ordinance but there are some apparent differences in the drafting of the two provisions. CSA is proposed to ensure consistency. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(e) refers). | 32 |
| 16. | 121F(4) | <ul style="list-style-type: none"> The Bills Committee questioned why there was no pecuniary penalty for contravention of that section, i.e. making false statements upon an application for registration. | <ul style="list-style-type: none"> As explained in our letter of 6 July 1999, the apparent gap is filled by the Magistrate's Ordinance. | <ul style="list-style-type: none"> No CSA is proposed. | 34 |
| 17. | 121F(6) | <ul style="list-style-type: none"> We are asked to consider if it is necessary to amend the provision to put it beyond doubt that any proceedings for offence under that section cannot be brought more than 6 months after the discovery of the offence. | <ul style="list-style-type: none"> Our legal advice confirms that the present drafting already clearly implies that proceedings cannot be brought after 6 months of the discovery of the offence and similar drafting has been used in other legislation. We therefore do not propose any amendment. | <ul style="list-style-type: none"> No CSA is proposed. | 33 |
| 18. | 121G(2) | <ul style="list-style-type: none"> To delete section 121G(2)(a) as the concept of ineligibility to make application does not exist in the Bill. | <ul style="list-style-type: none"> Technical amendment. We do not propose any amendment to sections 121G(3) and (4) as the | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(f) refers). | 35 |

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| | | <ul style="list-style-type: none"> It has separately been suggested that sections 121G(3) and (4) be grouped together, under which the Commission must refuse the application. | Law Draftsman confirms that the present drafting is in order. | | |
| 19. | 121H(2) | <ul style="list-style-type: none"> To delete section 121H(2)(a) as the concept of ineligibility to make application does not exist in the Bill. | <ul style="list-style-type: none"> Technical amendment It was separately suggested that sections 121H(3) and (4) be grouped together. For the same reason as item 18 above, we do not propose any amendment in this respect. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(g)(i) refers). | |
| 20. | 121H(5) | <ul style="list-style-type: none"> To specify that the Commission may take into account any relevant information in its possession whether provided by the applicant or by some other person. | <ul style="list-style-type: none"> Section 121H(5) is supposed to be analogous to section 121G(6). For the sake of consistency, it is proposed to amend the subsection to read the same as section 121G(6). | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(g)(ii) refers). | 36 |
| 21. | 121J(3) | <ul style="list-style-type: none"> To specify that if the Commission imposes any condition and restriction in granting application for registration, it should provide reasons for its decision to the relevant person if so requested. | <ul style="list-style-type: none"> The subsection vests in the Commission the power to impose conditions and restrictions in granting application for registration but does not oblige the SFC to provide reasons for such imposition of conditions or restrictions. It is | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(h) refers). | 37 |

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| | | | therefore proposed to amend the provision to require SFC to do so in order to ensure procedural fairness to the registrants. | | |
| 22. | 121R(2) | <ul style="list-style-type: none"> In section 121R(2)(h), to repeal “(whether convicted of the contravention or not)”. | <ul style="list-style-type: none"> Technical amendment. The clause in parentheses is redundant. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(i) refers). | |
| 23. | 121R(5) and 121T(5) | <ul style="list-style-type: none"> It has been suggested that sections 121R(5) and 121T(5) should be amended to provide that the Commission cannot suspend the registration of a registered financier or representative without first giving the financier or representative an opportunity of being heard. | <ul style="list-style-type: none"> Given that the same language has been used in the existing Ordinance (section 55), for the sake of consistency, it is proposed not to amend the two sections. It may be worth noting that section 121W of the Bill provides that the Commission must give to the financier or the representative a written notice of the decision and an explanation of the grounds that lead to the decision. We believe the procedural fairness is ensured. | <ul style="list-style-type: none"> No amendment is proposed. | 24 |

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| 24. | 121S(1) | <ul style="list-style-type: none"> It has been suggested that section 121S(1) be amended to ensure that the Commission has the power to inquire into any of the matters listed in 121R(2)(a)-(h). | <ul style="list-style-type: none"> Our legal advice confirms that given section 121S(1)(a)(iv) enables the SFC to conduct inquiries to ascertain whether a financier remains fit and proper to be registered and in that connection, SFC can have regard to the financier's financial integrity and reliability, the scenarios listed in section 121R(2) should have been covered. Therefore no amendment is necessary. | <ul style="list-style-type: none"> No CSA is proposed. | 39 |
| 25. | 121S(4) | <ul style="list-style-type: none"> To repeal "impose a penalty under this section" and substitute "take any action under subsection (3)". | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(j) refers). | 40 |
| 26. | 121U(4) | <ul style="list-style-type: none"> To repeal "impose a penalty under this section" and substitute "take any action under subsection (3)". | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(j) refers). | 44 |
| 27. | 121V(3) and (4) | <ul style="list-style-type: none"> To delete "cancel" and substitute "revoke". | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(k) refers). | 43 |
| 28. | 121W(1) and (2) | <ul style="list-style-type: none"> To delete "impose any other penalty on" and substitute "take any other action against". | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(l) refers). | 44 |

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| 29. | Suspension New section 121WA(?) | <ul style="list-style-type: none"> To introduce a new section to enable the Commission to suspend the whole or any part of the registration of a financier (or a financier's representative as the case may be) and make an order specifying the manner in which an existing business is to be carried on and attach to it such reasonable conditions as the SFC consider necessary. Non-compliance with the suspension order will constitute an offence. | <ul style="list-style-type: none"> The proposed amendment is in response to the concerns that a suspended financier should not be prevented from engaging in activities/business which are necessary for the continuous survival of its business and for serving the interests of its exiting clients. It is therefore proposed to enable SFC to suspend the registration in respect of the whole or the part of the securities margin financing business and specify the manner in which the business can continue to be carried on. | <ul style="list-style-type: none"> Draft CSA under formulation. | |

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| 30. | 121Y(1) | <ul style="list-style-type: none"> To repeal (d) and (e) and substitute “(d) an adjustment of the amount of financial accommodation provided to the client by the financier (except as a result of interest charged by the financier) (e) an adjustment of the terms on which financial accommodation is provided to the client, whether by extension, reduction, credit or debit (except as a result of change in market value of securities collateral provided by the client)” | <ul style="list-style-type: none"> Technical amendments to streamline the statement of account requirement, specifically to clarify that a financier should not be required to provide a statement of account solely for the purpose of indicating interest charges. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(m)(i) refers). | 24, 42 |
| 31. | 121Y(3) | <ul style="list-style-type: none"> In section 121Y(3)(d), to add “together with the interest rate and basis of interest calculation” after “financial accommodation” To add “initiated “ after “all disposals” in section 121Y(3)(h). To delete section 121Y(3)(i). | <ul style="list-style-type: none"> Technical amendments. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(m)(ii) refers). | 24 |
| 32. | 121Y(4) | <ul style="list-style-type: none"> In subsection (4)(b), to repeal the word “give” and substitute “provide”. At the end of subsection (4), add “except in the | <ul style="list-style-type: none"> In response to the comments made by the Bills Committee, we have reconsidered if it is necessary to require a financier to provide to its | <ul style="list-style-type: none"> First bull point reflected in the CSA (clause 3(m)(iii) refers). | 10 |

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| | | case where there is no movement in the account over the relevant period, or the account does not have any outstanding balance or securities holding at the end of the relevant period.” | client a monthly statement even if there is no movement in the client’s account over the month or there is no outstanding balance or securities holding in the account at the end of the relevant period. On balance, we agree that the financier should not be required to do so in order to relieve the potential administrative burden on the part of the financier and a CSA is proposed accordingly. | <ul style="list-style-type: none"> The other one to be included. | |
| 33. | 121Y(5) | <ul style="list-style-type: none"> In section 121Y(5)(h), to add “initiated” after “disposal”. | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(m)(iv) refers). | |

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| 34. | 121Y(6) | <ul style="list-style-type: none"> To add “without reasonable excuse” after “who”. | <ul style="list-style-type: none"> For clarity. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(m)(v) refers). | 41 |
| 35. | 121Z(3) | <ul style="list-style-type: none"> In section 121Z(3)(a), to delete “2 years” and substitute “3 months”. | <ul style="list-style-type: none"> The information contained in the statement of accounts referred to in section 121Y(2) should have been reflected in that referred to in section 121Y(4). It is therefore proposed that financier should keep record of the former for 3 months only. The Bills Committee also questioned the reasonableness to require keeping of statement of accounts referred to in section 121Y(4) for 6 years respectively. The requirement is in fact consistent with section 83(5) of the existing Ordinance, which is comparable to the 7-year record keeping requirement under the Inland Revenue Ordinance. This anomaly will be redressed under the composite Securities and Futures Bill when all licensed persons will be required to maintain records for a minimum of 7 years. No CSA is proposed in this | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(n) refers). | 42 |

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| | | | regard. | | |
| 36. | 121AA(1) | <ul style="list-style-type: none"> • In section 121AA(1), to add “(aa) registered in the name of the financier or a nominee controlled by the financier; or”. • In section 121AA(1)(b), delete the word “financial”. • To repeal section 121AA(1)(c). | <ul style="list-style-type: none"> • To allow financiers to register client’s securities collateral in their names or their nominees’ names for purpose of providing better protection of their collateral interest. • Amendment to section 121AA(1)(b) is consequential to the amendment to the definition of “authorized financial institution”. • Section 121AA(1)(c) is redundant as the policy intent should have been adequately covered by section 121AA(1)(b), and therefore should be deleted. | <ul style="list-style-type: none"> • Reflected in the CSA (clause 3(o) refers). | 9, 52 |
| 37. | 121AA(4) | <ul style="list-style-type: none"> • To amend section 121AA(4)(a) to impose a condition that credit facilities obtained by pledging margin clients’ securities collateral by a securities margin financier should not exceed an amount as prescribed by Commission Rules. • To amend section 121AA(4)(b) and (c) so that | <ul style="list-style-type: none"> • The amendment to section 121AA(4)(a) is for the purpose of better investor protection by limiting the extent to which the financiers can borrow from authorized institutions and/or registered dealers by pledging clients’ securities collateral, i.e. the | <ul style="list-style-type: none"> • Draft CSA under formulation. | 9, 53 |

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| | | financiers may dispose of the securities collateral in case of client default if client's authority is obtained and such authority will not be subject to the annual renewal. | pooling arrangement. Please refer to our letter dated 24 September 1999 for more details. <ul style="list-style-type: none"> Sections 121AA(4)(b) and (c) now require the financier to obtain client's authority before it can dispose of the securities collateral to meet the client's obligation to the financier. Such authority is however subject to renewal annually. To better protect the security right of the financier over securities collateral, we propose to amend the section 121AA so that the financier is only required to obtain an one-off authority from the client for such purposes. | | |
| 38. | 121AA(7) | <ul style="list-style-type: none"> To add an imprisonment penalty under section 121AA(7) and to increase the pecuniary penalty on summary conviction to level 6 (\$100,000). | <ul style="list-style-type: none"> The penalty levels are increased to increase deterrence. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(o) refers). | 49 |
| 39. | 121AB(4) | <ul style="list-style-type: none"> To clarify that the obligation imposed under section 121AB(4)(b) should only be triggered whenever the Commission has a reasonable belief that there is a breach of the financial | <ul style="list-style-type: none"> For proper checks and balances, the Commission should only exercise the powers under section 121AB(4) when it has a reasonable belief that | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(p) refers). | 49 |

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| | | resources rules, as envisaged under section 121AB(3) | there is a breach of the financial resources rules. | | |
| 40. | 121AB(6) | <ul style="list-style-type: none"> To increase the penalty on summary conviction to level 6 (\$100,000) and \$1,000 per day for continuing offence. | <ul style="list-style-type: none"> To increase deterrence. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(p) refers). | 46, 55 |
| 41. | Division 4 121AC to 121AH | <ul style="list-style-type: none"> To amend the Division 4 of the Bill by adopting UK approach as embodied in the Financial Services and Market Bill now under consideration by the UK Parliament. The UK model focuses on enforceability of the contract between the client and the unregistered person and compensation to the client. | <ul style="list-style-type: none"> As explained in our letter dated 27 July 1999, the policy intent of the Division 4 is to render better protection to the investors by providing a client of an unregistered securities margin financier with the right to rescind the contract entered into between them. The concept of rescission is not unusual in existing laws and indeed, it is already in place in sections 72(4), 73(4), 143(5) and 144(c) of the existing Securities Ordinance, though structured differently as compared with the proposed Division 4. In view of the concerns of the Bills Committee, we have reviewed further the concept of rescission embraced in Division 4. The | <ul style="list-style-type: none"> Draft CSA under formulation. | 24, 48, 56 |

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| | | | provisions were mainly derived from the Australian Corporations Law and might be complicated to interpret. Upon further consultation with the SFC, we propose to adopt the UK model which is embodied in the Financial Services and Market Bill now under consideration by the UK Parliament. | | |
| 42. | 121AK(4) | <ul style="list-style-type: none"> To increase the penalty on summary conviction to level 3 (\$10,000). | <ul style="list-style-type: none"> To increase deterrence. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(q) refers). | 49 |
| 43. | 121AS(1) | <ul style="list-style-type: none"> To repeal “(and without intent to defraud)” | <ul style="list-style-type: none"> Section 121AS(1) is analogous to section 84 of the existing SO. The proposed amendment seeks to remove the apparent inconsistency between the two provisions. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(r) refers). | |
| 44. | 121AT(3) | <ul style="list-style-type: none"> In section 121AT(3)(a), to amend “employee of such employee”. To add a new section to provide that a registered financier may appoint its general auditor appointed for the purposes of the Companies Ordinance (Cap. 32) to act as an | <ul style="list-style-type: none"> There has been doubt as to what the exact meaning of “employee of such employee” is. The proposed amendments seek to clarify the types of persons who are not qualified for appointment as an auditor. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(s) refers). | 54 |

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| | | auditor under this section. | <ul style="list-style-type: none"> Under the Companies Ordinance, a company is required to appoint an auditor. A financier, being a company, is required under section 121AT to appoint an auditor as well. It is therefore proposed to clarify that it is unnecessary for a registered financier to appoint an auditor in addition to the one appointed under the Companies Ordinance. | | |
| 45. | 121AY(2) | <ul style="list-style-type: none"> To repeal the word “section” and substitute “Division”. | <ul style="list-style-type: none"> It is unclear from the present drafting of section 121AY(2) as to whether the expenses of an auditor appointed under section 121AZ would be borne by the registered financier. The proposed amendment seeks to put this beyond doubt. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(t) refers). | 51 |
| 46. | 121BD(3), (4) and (6) | <ul style="list-style-type: none"> To amend section 121BD along the lines of existing section 95(2) and (3) of the SO. | <ul style="list-style-type: none"> Existing section 95 deals with the powers of an auditor appointed by the SFC, which is presently under review in the context of the composite Bill. In order not to preempt the composite Bill, we propose to redraft section 121BD to | <ul style="list-style-type: none"> Draft CSA under formulation. | 50 |

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| | | | read along the lines of the existing section 95. | | |
| 47. | 121BE | <ul style="list-style-type: none"> To increase the penalty on summary conviction to level 6 (\$100,000). | <ul style="list-style-type: none"> To increase deterrence. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(u) refers). | 49 |
| 48. | 121BF | <ul style="list-style-type: none"> To increase the penalty on summary conviction to level 6 (\$100,000). | <ul style="list-style-type: none"> To increase deterrence. | <ul style="list-style-type: none"> Reflected in the CSA (caluse 3(v) referes). | 49 |
| 49. | 121BG | <ul style="list-style-type: none"> To refine the drafting language for the thresholds under which SFC may refuse the application of waiver and modification of the requirements specified under the section. To oblige SFC to state the reasons on refusal of an application made under section 121BG for waiver or modification of the requirements or granting an application with conditions. To include section 121D as specified provisions eligible for application for waiver and modification. | <ul style="list-style-type: none"> In response to the concerns expressed by the Bills Committee, the Administration in consultation with SFC has reviewed the present drafting of section 121BG(3)(a) and (b) and agreed to modify it so as to convey our policy intent more clearly. Separately, the Bill is presently silent on whether SFC has to provide reasons on refusal of an application for waiver or modification of any of the specified requirements or granting an application with conditions. While it has been a practice of SFC to do so to ensure procedural fairness, we have no objection to | <ul style="list-style-type: none"> Draft CSA under formulation. | 59, 60 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
|-----|-------------------|---|---|--|---|
| | | | stating it clearly in the law that SFC should provide reasons. A CSA is proposed accordingly. | | |
| 50. | 121BH | <ul style="list-style-type: none"> To increase the penalty levels to a fine of \$1,000,000 and imprisonment for 5 years on conviction on indictment; and to a fine at level 6 (\$100,000) and imprisonment for 6 months on summary conviction. | <ul style="list-style-type: none"> To increase deterrence. | <ul style="list-style-type: none"> Reflected in the CSA (clause 3(w) refers). | 49 |
| 51. | New section 121BI | <ul style="list-style-type: none"> To provide that a person whose only securities margin financing business is to recover outstanding margin loans prior to the commencement of the Amendment Ordinance and collect interests accrued therefrom is not required to be registered under section 121C. | <ul style="list-style-type: none"> It is envisaged that there may be finance companies transferring the well-secured margin loans to the dealing firms and leaving themselves with the under-secured ones with a view to recovering the loans in due course. The proposed amendment seeks to waive such companies from the registration requirement as a securities margin financing, provided that they do not engage in any other securities margin financing except recovery of old loans and collection of interest accrued. | <ul style="list-style-type: none"> Draft CSA under formulation. | |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| 52. | New clause 3A | <ul style="list-style-type: none"> To add a new Schedule 4 as referred to in the proposed revised section 121B(2). | <ul style="list-style-type: none"> Please also see item 8 above. On the rationale of the proposed additional exemptions, please refer to the Administration's responses to the Bills Committee dated 25 June and 16 July 1999. | <ul style="list-style-type: none"> Reflected in the CSA. | 8, 14, 25 |
| 53. | Schedule 1 Item 1 Section 2 | <ul style="list-style-type: none"> To consider if the proposed subparagraph (d) in the definition of "dealer" should be expanded to cover activities conducted by registered financiers that may be regarded as "dealing in securities". | <ul style="list-style-type: none"> It was raised in the Bills Committee meeting that the originally proposed amendments to the definition of "dealer" was too narrowly drafted and might inadvertently capture securities margin financiers in their ordinary business. To address the problem, it is proposed to extend the definition as set out in the left column. | <ul style="list-style-type: none"> Reflected in the CSA. | 64 |
| 54. | Schedule 1 Item 1 Section 2 | <ul style="list-style-type: none"> To redefine "authorised financial institutions" as "authorised institutions". | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA. | 65 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
|-----|--|--|--|---|---|
| 55. | Schedule 1 Items 5 and 6 Section 55 and 56 | <ul style="list-style-type: none"> In section 55(c) and 56(c), to repeal ““registered person” (註冊人)” and substitute ““registered” (註冊) person” | <ul style="list-style-type: none"> For clarity. | <ul style="list-style-type: none"> To be included in the CSA by the sinophone draftsman. | |
| 56. | Schedule 1 Item 10 | <ul style="list-style-type: none"> The Bills Committee queried if it is appropriate to elaborate on the meaning of “prescribed”. | <ul style="list-style-type: none"> The Law Draftsman responded at the Bills Committee meeting that the intention might be to avoid any confusion with any possibility of matters prescribed under 146A by Chief Executive. | <ul style="list-style-type: none"> No CSA is proposed. | |
| 57. | Schedule 1 New item 19A Section 75 | <ul style="list-style-type: none"> In section 75(3), to add “without reasonable excuse” after “who”. | <ul style="list-style-type: none"> Technical amendment | <ul style="list-style-type: none"> Reflected in the CSA. | |
| 58. | Schedule 1 Item 20 Section 75A(1) | <ul style="list-style-type: none"> In section 75A(1), to repeal (d) and (e) and substitute “(d) an adjustment of the amount of financial accommodation provided to the client by the dealer (except as a result of interest charged by the dealer); or | <ul style="list-style-type: none"> Technical amendments to streamline the statement of account requirement (specifically to clarify that a financier should not be required to provide a statement of account solely for the purpose of indicating interest charges). | <ul style="list-style-type: none"> Reflected in the CSA. | 24, 66 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | | (e) an adjustment of the terms on which financial accommodation is provided to the client, whether by extension, reduction, credit or debit (except as a result of change in market value of securities collateral provided by the client)" | <ul style="list-style-type: none"> It was separately suggested by the Bills Committee that section 75A could simply refer to the requirements set out in section 121Y as the requirements under these two sections are basically identical. However, by so doing, it will in effect require a dealer to turn to a Part of the Ordinance that he would not normally consult in order to find out his responsibilities. For the sake of clarity and certainty, no amendment to section 75 is proposed. | | |
| 59. | Schedule 1 Item 20 Section 75A(3) | <ul style="list-style-type: none"> In section 75A(3)(d), to add “together with the interest rate and basis of interest calculation thereon” after “financial accommodation” To add “initiated “ after “all disposals” in section 75A(3)(h). To delete section 75A(3)(i). | <ul style="list-style-type: none"> Technical amendments. | <ul style="list-style-type: none"> Reflected in the CSA. | 24, 42 |
| 60. | Schedule 1 Item 20 Section | <ul style="list-style-type: none"> In subsection (4)(b), to repeal the word “give” and substitute “provide”. At the end of subsection (4), add “except in the | <ul style="list-style-type: none"> In response to the comments made by the Bills Committee, we have reconsidered if it is necessary to require a dealer to provide to its | <ul style="list-style-type: none"> First bull point reflected in the CSA. The other one to be | 10 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
|-----|--|---|---|---|---|
| | 75A(4) | case where there is no movement in the account over the relevant period, or the account does not have any outstanding balance or securities holding at the end of the relevant period.” | client a monthly statement even if there is no movement in the client’s account over the month or there is no outstanding balance or securities holding in the account at the end of the relevant period. On balance, we agree that the dealer should not be required to do so in order to relieve the potential administrative burden on the part of the dealer and a CSA is proposed accordingly. | included. | |
| 61. | Schedule 1 Item 20 Section 75A(5) | <ul style="list-style-type: none"> In section 75A(5)(h), to add “initiated” after “disposal”. | <ul style="list-style-type: none"> Technical amendment. | <ul style="list-style-type: none"> Reflected in the CSA. | |
| 62. | Schedule 1 Item 22 Section 77(4) | <ul style="list-style-type: none"> In section 77(4)(a), to delete “2 years” and substitute “3 months”. | <ul style="list-style-type: none"> The information contained in the statement of accounts referred to in section 75A(2) should have been reflected in that referred to in section 75A(4). It is therefore proposed that dealers should keep record of the former for 3 months only. The Bills Committee also | <ul style="list-style-type: none"> Reflected in the CSA. | 42, 67 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | | | questioned the reasonableness to require keeping of statement of accounts referred to in section 75A(4) for 6 years respectively. The requirement is in fact consistent with section 83(5) of the existing Ordinance, which is comparable to the 7-year record keeping requirement under the Inland Revenue Ordinance. This anomaly will redressed under the composite Securities and Futures Bill when all licenced persons will be required to maintain records for a minimum of 7 years. No CSA is proposed in this regard. | | |
| 63. | Schedule 1 Item 23 Section 79 | <ul style="list-style-type: none"> The Bills Committee has requested the Administration to consider if it is tidier to group the rule making power of SFC under section 146 rather than under section 79(9). | <ul style="list-style-type: none"> Under the existing Securities Ordinance, for the sake of clarity, context-specific rule making power of SFC are provided in the relevant provisions, such as sections 76(1), 79(9) and 80(4)(d). The more general rule making powers are on the other hand grouped under section 146. The approach has been worked well in years and we see no strong reason to make a | <ul style="list-style-type: none"> No CSA is proposed. | 68 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
|-----|---|--|---|--|---|
| | | | change. This will also be the approach adopted in the composite Bill. | | |
| 64. | Schedule 1 Item 25 Section 81 | <ul style="list-style-type: none"> To delete the word “financial” in section 81(2)(b). To recast the last few words of section 81(3) to read “satisfactory facilities for such safe custody”. To increase the penalty under section 81(6) on summary conviction to level 6 (\$100,000) in section 81(6). | <ul style="list-style-type: none"> Technical amendment | <ul style="list-style-type: none"> Reflected in the CSA (except 2nd bull point). | 72, 73 |
| 65. | Schedule 1 Item 25 Section 81 | <ul style="list-style-type: none"> To amend section 81 to ensure that securities deposited by a securities margin financier with a securities dealer for safe custody purpose are also subject to the protection given under that section. To amend section 81 so that dealers may dispose of the securities deposited by a client for the purpose of settling any liability owed by the client but only with the written authority of the client or as permitted by Commission rules. | <ul style="list-style-type: none"> On the first point, since most securities margin financiers will not in their own right maintain an account at CCASS, it is quite common in practice for these financiers to deposit the securities collateral on CCASS via a dealer being CCASS participants. These financiers normally do not effect securities transactions through the dealers and therefore will not be regarded as the “client” of the dealer. It is therefore necessary to | <ul style="list-style-type: none"> Draft CSA under formulation. | |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | | | <p>ensure that such securities will be subject to the same level of protection given under section 81.</p> <ul style="list-style-type: none"> The other amendment is to enable dealers to set off different accounts maintained by the same client, provided that client's written authority is obtained. | | |
| 66. | Schedule 1 Item 25 Section 81 | <ul style="list-style-type: none"> The Bills Committee at the meeting on 17 September 1999 requested the Administration to reflect further on the following points – <ul style="list-style-type: none"> It is unclear whether the exceptions provided for in the Commission Rules can override the requirements set under section 81(2). It may be helpful to require that client agreements should be counter-signed by the dealer or designated officer to ensure that the terms and risks are clearly explained and disclosed to the clients. | <ul style="list-style-type: none"> On the first point, our legal advice confirms that given the exceptions to the prohibition (to be provided in the subsidiary legislation) is expressly permitted under section 81(4), there does not appear to be a problem. No CSA in this regard is therefore required. On the latter point, as indicated in paragraph 85 of our Consultation Paper published in May 1998, the staff responsible for explaining the authorization under section 81 (and sections 81A and 121AA) letter will be required to sign off to ensure that proper information and risk disclosure is made and to | <ul style="list-style-type: none"> No CSA is proposed. | 69, 70, 71 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | | | improve accountability. Requirements in this respect will be embodied in the proposed revised Code of Conducts in due course. | | |
| 67. | Schedule 1 Item 25 Section 81A | <ul style="list-style-type: none"> To delete the word “financial” in section 81A(5)(a). To increase the penalty on summary conviction to level 6 (\$100,000) to increase deterrence. To amend section 81A so that dealers may dispose of the securities deposited by a client for the purpose of settling any liability owed by the client but only with the written authority of the client or as permitted by Commission rules. To amend section 81A to impose a condition that credit facilities obtained by pledging margin clients’ securities collateral by a securities dealer should not exceed an amount as prescribed by Commission rules. | <ul style="list-style-type: none"> Sections 81A(5)(b) and (c) now require the dealer to obtain client’s authority before it can dispose of the securities collateral to meet the client’s obligation to the dealer. Such authority is however subject to annual renewal. To better protect the security right of the dealer over securities collateral, we propose to amend the section 81A so that the dealer is only required to obtain an one-off authority from the client for such purposes. The amendment will also seek to enable dealers to set off different accounts maintained by the same client within the dealer entity. The last one is for the purpose of better investor protection by limiting the extent to which the dealers can borrow from authorized institutions by pledging clients’ | <ul style="list-style-type: none"> Draft CSA under formulation. | 9, 53 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | | | securities collateral, i.e. the pooling arrangement. | | |
| 68. | Schedule 1 Item 25 Section 81A(2) | <ul style="list-style-type: none"> In section 81A(2), delete the word “either” and separately add “(aa) registered in the name of the dealer or a nominee controlled by the dealer; or”. | <ul style="list-style-type: none"> To allow financiers and dealers to register client’s securities collateral in their names or their nominees’ names for purpose of providing better protection of their collateral interest. | <ul style="list-style-type: none"> Reflected in the CSA. | 9, 52 |
| 69. | Schedule 1 Item 27 Section 83 | <ul style="list-style-type: none"> To consider retaining “or any related corporation” in section 83(3)(a)(vi) to include keeping of records of those securities which had been deposited with a third party as collateral for loans or advances made to the dealer or to any related corporation of the dealer. To consider not replicating “financial accommodation” in section 83(3)(a)(viii) as the full definition was provided under the amended section 2(1). To re-examine the need for dealers to keep records for 6 years. | <ul style="list-style-type: none"> On the first bull point, we are of the view that it could be misleading if the reference to “or any related corporation” is retained in section 83(3)(a)(vi). It is because under the proposed sections 81 and 81A, dealers can no longer deposit clients’ securities with a third party as security for loans or advances made to related corporations. Should there be any dealers who deposit clients’ securities in this manner, they would have to record the same details since this would be captured by “or for any other purposes” at the end of the subparagraph. No CSA is | <ul style="list-style-type: none"> No CSA is proposed. | 74, 75, 76 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | | | <p>therefore proposed.</p> <ul style="list-style-type: none"> ● “Financial accommodation” is defined as loans or other arrangement under which a person is or is to be provided with credit, which may or may not be for the purposes of facilitating acquisition or the continued holding of securities. Section 83 relates to the records of credit facilities that are related to the facilitation of acquisition or the continued holding of securities only. Thus there does not appear to be any repetition problem and no CSA is proposed. ● On the requirement to keep records for 6 years, as explained in item 35 above, the requirement is broadly in line with that under the Inland Revenue Ordinance and we do not see grounds to change it. | | |
| 70. | Schedule 1 Item 36 | <ul style="list-style-type: none"> ● To amend section 94 of the SO to clarify its relation with section 59 of the SFCO. | <ul style="list-style-type: none"> ● The Bills Committee questioned whether the communication of information between of an | <ul style="list-style-type: none"> ● Draft CSA under formulation. | 77 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | Section 94 | | employee of an auditor with another employee would be in breach of section 94(d) and what the relation of this section with section 59 of the SFCO is. The intent of this provision is to deter the divulgence of information any unrelated parties. We will propose a CSA to put this beyond doubt. | | |
| 71. | Schedule 1 Item 37 Section 95 | <ul style="list-style-type: none"> Delete paragraph (c) of this item. | <ul style="list-style-type: none"> The proposed amendment to section 95 was consequential to the proposed section 121BD. As explained in item 46 above, the matter is now under review in the context of the composite Bill. In order not to preempt the composite Bill, we propose to withdraw this clause from the present Bill. | <ul style="list-style-type: none"> Draft CSA under preparation. | 78 |
| 72. | Schedule 1 Item 43 Section 146 | <ul style="list-style-type: none"> The Bills Committee invited the Administration to consider amending the rule-making power of SFC under section 146 to subject it to the positive vetting of the LegCo. | <ul style="list-style-type: none"> The current regime for making rules by negative vetting has been working well and we see no strong reason to change the approach. | <ul style="list-style-type: none"> No CSA is proposed. | 79 |
| 73. | Schedule 2 | <ul style="list-style-type: none"> To refine the drafting language the proposed | <ul style="list-style-type: none"> In response to the concerns | <ul style="list-style-type: none"> Draft CSA under | 80 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
|-----|--|---|---|---|---|
| | Item 7 Section 29AA of SFCO | section 29AA(4)(a) and (b) in respect of the thresholds under which SFC may grant the application of waiver and modification of the requirements. | expressed by the Bills Committee, the Administration in consultation with SFC has reviewed the drafting of the proposed section 29AA(4)(a) and (b) and agreed to modify it so as to convey our policy intent more clearly, i.e. the grant of waiver of any FRR requirement shall not be contrary to the interest of the investing public. | formulation. | |
| 74. | Schedule 3 Item 3 Section 15(b) of SEUO | <ul style="list-style-type: none"> The ALA suggested that section 15(b) of the Stock Exchange Unification Ordinance should be amended by repealing “section 65B and any”. | <ul style="list-style-type: none"> Upon consultation with the Department of Justice, we take the view that the expression of “any financial resources rules” still makes sense in the context and therefore no further amendment is considered necessary. | <ul style="list-style-type: none"> No CSA is proposed. | |
| 75. | Schedule 3 New item Section 3 of Banking Ordinance | <ul style="list-style-type: none"> In section 3(1) of the Banking Ordinance (Cap. 155), to add “(ja) a person who is a registered securities margin financier within the meaning of the Securities Ordinance (Cap. 333), where section 121AM of that Ordinance applies to such a deposit”. | <ul style="list-style-type: none"> To exempt securities margin financiers under section 3 of the Ordinance in respect of deposit of client’s money into trust accounts. | <ul style="list-style-type: none"> Reflected in the CSA. | |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| 76. | Schedule 4 Item 1 | <ul style="list-style-type: none"> Delete section 1 of Schedule 4 of the Bill. | <ul style="list-style-type: none"> The Bills Committee questioned the need for providing the CE-in-Council with the power to make regulations of a savings or transitional nature consequent to the enactment of the Amendment Ordinance. Upon further consultation with SFC, we agree that the provisions embodied in the Bill should have provided SFC with sufficient flexibilities to deal with events of transitional nature and the additional saving powers of the CE-in-Council is not necessary. We propose to delete the provision. | <ul style="list-style-type: none"> Draft CSA under preparation | 81 |
| 77. | Schedule 4 Item 3 | <ul style="list-style-type: none"> Securities dealers will have 3 months transitional period to make arrangements to obtain authorizations from their existing client for the purpose of complying with the new section 81A. During this period, client authorization made under the existing section 81 will remain in force, provided that the authorization has not expired. | <ul style="list-style-type: none"> Technical amendments. | <ul style="list-style-type: none"> Reflected in the CSA. [may need revision] | |
| 78. | Unregistered dealing and margin | <ul style="list-style-type: none"> The Bills Committee has expressed concerns as to whether the Commission has adequate means to deal with unregistered dealing (and | <ul style="list-style-type: none"> As explained in our response of 6 July 1999, the SFC is enabled to investigate and seek injunctions in | <ul style="list-style-type: none"> No CSA is proposed. | 38 |

| | Section | Details | Purpose and justifications | Present Position | Reference in the checklist prepared by the Clerk |
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| | financing activities | margin financing) cases. <ul style="list-style-type: none"> To consider giving better protection to bona fide dealers dealing with the unregistered financier. | respect of unregistered dealing (and margin financing) under the various sections under the Securities Ordinance and the SFC Ordinance. The regime has been worked well so far and we believe no further amendment is necessary. | | |

Financial Services Bureau
10 December 1999
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