

立法會
Legislative Council

LC Paper No. CB(1) 2049/99-00
(These minutes have been seen
by the Administration and
cleared by the Chairman)

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**Bills Committee on
Exchanges and Clearing Houses (Merger) Bill**

**Minutes of meeting
held on Tuesday, 30 November 1999, at 8:30 am
in Conference Room B of the Legislative Council Building**

- Members present** : Hon Ronald ARCULLI, JP (Chairman)
Hon LEE Kai-ming, SBS, JP
Hon NG Leung-sing
Hon CHAN Kam-lam
Hon Jasper TSANG Yok-sing, JP
Dr Hon Philip WONG Yu-hong
Hon FUNG Chi-kin
- Member absent** : Hon SIN Chung-kai
- Public officers attending** : Mr Bryan P K CHAN
Principal Assistant Secretary for Financial Services
- Ms Gloria LO
Assistant Secretary for Financial Services
- Ms Mabel CHEUNG
Government Counsel
Department of Justice
- Attendance by invitation** : Mr David STANNARD
Executive Director, Corporate Finance
Securities and Futures Commission

Mr Gerald D GREINER
Senior Director of Supervision of Markets
Securities and Futures Commission

Clerk in attendance : Ms LEUNG Siu-kum
Chief Assistant Secretary (1)4

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

Ms Connie SEZTO
Senior Assistant Secretary (1)1

I Meeting with the Administration

(LC Paper Nos. CB(1) 480/99-00(01), 487/99-00 (01) and (02))

Members noted the papers tabled at the meeting. On the Coordinating Committee on Market Structure Reform (CCMSR) which was formed in May 1999, members noted that its objective was to provide a forum for the relevant parties to exchange views on key issues relating to the merger reform and to clarify issues raised by the industry. The membership of CCMSR comprised the Secretary for Financial Services (Chairman), former and incumbent chairmen of the two Exchanges, chairman of the Hong Kong Securities and Clearing Company, market leaders and participants, representatives of the Hong Kong Association of Banks as well as the Securities and Futures Commission (SFC). Apart from soliciting views from CCMSR and receiving feedbacks from the market on the reform from time to time, the Administration had not specifically conducted public consultation on the Bill.

Cooperative arrangements with overseas regulators

2. Members noted the list on cooperative arrangements that SFC had entered into with overseas regulators. Responding to members' enquiries, the Senior Director of Supervision of Markets, SFC (SDSM/SFC) said that SFC had entered into Memorandum of Understanding (MOU) with all major overseas regulators. He added that SFC was negotiating with regulators of India and Portugal for the establishment of MOU. Moreover, SFC had also managed to exchange information with some overseas regulators, for instance the regulator of Philippines, without the signing of MOU. As whether SFC would need to revise the existing MOU or to establish new MOU with overseas regulators as a result of the merger, SDSM/SFC confirmed that the merger

reform would not affect the status of existing MOU and that SFC would continue to exchange cross market information with its counterparts under the MOU. On the contents of MOU, SDSM/SFC explained that each MOU was unique while some MOU, like those entered into with the regulators of United States (US), were more elaborate covering the sharing of a wide range of regulatory information, others had a narrower scope covering less information.

3. As regards effectiveness of MOU in addressing problems arising from the Asian financial turmoil in 1997, SDSM/SFC responded that besides the arrangements under MOU, consolidated efforts of all regulators in the banking, securities and futures, commodities and other financial services sectors were necessary in meeting the challenges of the turmoil. He added that a task force had been formed to provide a forum for regulators and all relevant parties to exchange views on key issues relating to the financial stability of Hong Kong. The work of the task force had proved to be promising. Mr FUNG Chi-kin however commented that apart from the signing of MOU, other measures should be in place to enhance the financial stability of Hong Kong. SDSM/SFC stressed that SFC was committed to maintaining the fairness and competitiveness of the securities and futures market in Hong Kong through enhancing transparency of the market and establishment of MOU with overseas regulators. He considered that in order to tackle the problem of regulating international market players, the establishment of alliances amongst regulators would be necessary.

4. On the question about whether MOU would have the force of law, SDSM/SFC replied that MOU was essentially cooperative arrangements between regulators for sharing of market information. Prosecution would not be taken under MOU. However, experience had shown that when the overseas regulator had close relationship with its government, the cooperation between the two jurisdictions would be more productive. The Chairman remarked that prosecution would only be taken when there was sufficient evidence. He expressed confidence that the measures introduced by the Administration after the 1997 financial turmoil were effective in protecting the financial system of Hong Kong. However, he was not optimistic about the development of international regulatory framework. The Principal Assistant Secretary for Financial Services (PAS/FS) reiterated that the establishment of an effective international regime governing the securities markets and the exchange industry required consolidated efforts of considerable number of regulators and concerned parties all over the world. There was increasing awareness on the issue due to the globalization of financial markets driven by the advancement of technology as well as the growing population of sophisticated investors.

Regulatory functions between SFC and the Hong Kong Exchanges and Clearing Limited (HKEC)

5. On Mr FUNG Chi-kin's concern about the division of regulatory functions between SFC and HKEC, SDSM/SFC replied that the division of functions would remain essentially the same as present. In respect of surveillance functions, HKEC as a commercial organisation would be more business-oriented and would focus on trading operations and risk management. SFC as the overall market regulator, would be primarily responsible for detecting market malpractices or statutory breaches. As regards intermediaries supervision, the functions currently performed by the Exchanges for prudential regulation of their members would be taken up by SFC. The transference of functions would reduce the areas of duplication and enable SFC to make comprehensive response to regulatory issues. However, HKEC would continue to monitor particular aspects of the business of intermediaries so that it might assess and manage the risks inherent in the operations of its subsidiary business units. In relation to market development, the function would be performed by HKEC. The Executive Director, Corporate Finance, SFC added that SFC would provide the necessary flexibility and incentives for HKEC to pursue its commercial interests.

List of bodies for consultation

6. Members noted the proposed list of organizations as provided by the Administration for consultation on the Bill. They also noted that the Law Society of Hong Kong had already made a submission on the Bill and copy of the submission had been circulated to members vide LC Paper No. CB(1) 424/99-00(03). In addition to the Administration's list, members agreed to invite the following bodies to give views on the Bill:

- The Securities and Futures Market Reform Members' Concerns Coordinating Group;
- The Hong Kong Society of Accountants;
- The Hong Kong Association of Banks;
- The Bar Association of Hong Kong; and
- The Hong Kong Securities Industry Group Limited.

7. Members also decided to place advertisements in the South China Morning Post and Hong Kong Economic Times to invite public views on the Bill. The closing date for submission would be 20 December 1999. The date for receiving oral representation of the deputations would be 6 January 2000.

Clause-by-clause examination on the Bill

Clause 1 - Short title and commencement

8. Members had no comment on this clause.

Clause 2 - Interpretation

“Associate”

9. The Chairman expressed concern over the definition of "associate". He pointed out that shareholders could authorize trustees to vote at a general meeting of HKEC and consequently these trustees might be classified as “minority controller” under the Bill if they were to exercise, or control the exercise of 5% or more of the voting power in HKEC. These trustees could be charged with an offence since it would be unlawful to become “minority controller” of HKEC without prior approval of SFC as stipulated under the Bill.

10. SDSM/SFC replied that these trustees could apply to SFC for exemption under Clause 6 of the Bill. He added that the 5% shareholding limit could be waived by SFC in consultation with the Financial Secretary (FS) where it could be demonstrated that an exemption was in the interest of the public and the market. The application for exemption would be considered on a case-by-case basis.

11. PAS/FS added that where a person was charged with the offence of becoming "minority controller", it could be a defence under Clause 6 for the person to prove that he did not know that the acts or circumstances by virtue of which he became a "minority controller" of HKEC. However, SFC would still take the necessary steps to order a person to dispose of any excess shares of HKEC for the purpose of discontinuing the contravention of the provision.

12. Dr Philip WONG pointed out that as all listed companies in Hong Kong had the possibility of being taken over in the securities market, HKEC would be the exception under the proposed shareholding arrangement. He was concerned that this might be against the listing rules and that such exception might have adverse effect on the confidence of shareholders of HKEC. He also raised concern about the market value of HKEC shares after listing. The Chairman concurred that shareholders of HKEC might not be able to protect their own interests as they would be able to in other listed companies.

13. PAS/FC replied that the shareholding arrangement of HKEC would not be against the listing rules. It was the Administration's intention to impose the shareholding limit of 5% in the law to prevent the control of HKEC by any

individual parties or parties acting in concert. The practice of 5% shareholding limit was also adopted by the Australian Stock Exchange when it demutualised and listed in 1998. Market response had proved to be positive. He stressed that the performance of HKEC would be the key factor in determining the market value of its shares. The Administration was optimistic in this respect.

14. He added that the definition of "associate" was in fact borrowed from the Banking Ordinance (Cap.155) and no adverse comments over the definition had been received so far.

15. Members asked whether the Administration had considered the issuance of differential shares (i.e. Share A and Share B) or "golden share" and the holding of over 50% shares of HKEC by the Government to ensure its control on HKEC.

16. PAS/FS explained that the issuance of differential shares and "golden share" was outdated measure. He re-iterated that the Administration had no intention to control HKEC.

17. Mr FUNG Chi-kin commented that unlike HKEC, the Government would remain as the majority shareholder after the privatization of the Mass Transit Railway Corporation, so as to protect the public interests. The Government seemed to be adopting conflicting policies in these two cases.

Admin 18. In view of members' grave concern over the interpretation of "associate", PAS/FS undertook to reflect members' views to the Law Draftsman for further consideration and to inform members of the outcome in due course.

19. Members also expressed concern about whether under Clause 2(2), the Chief Executive in Council could, by notice in the Gazette, declare that a person would no longer be an associate for the purpose of the Ordinance, and whether there was appeal channel in respect of the approval to be an associate.

Admin 20. PAS/FS remarked that the Chief Executive in Council did have the authority to declare a person no longer an associate for the purpose of the Ordinance. He, however, undertook to seek clarification with the Law Draftsman and revert to the Bills Committee at the next meeting.

21. The Chairman said that the person who aggrieved by the decision of the Chief Executive could appeal to the court.

"Constitution"

Admin 22. In reply to the enquiry about the meaning of "other instrument providing the constitution of the company" in the definition of "constitution", PAS/FS said that the definition of "constitution" was borrowed from the Securities Ordinance (Cap.333) and the Commodities Trading Ordinance (Cap.250). He undertook to seek clarification from the Law Draftsman in due course.

"Indirect controller"

Admin 23. Upon members' request, PAS/FS undertook to seek clarification on the definition of "indirect controller" from the Law Draftsman.

"Shares"

24. Members noted the comments from the Law Society of Hong Kong in relation to the definition of "shares".

25. In order to ensure that the securities which also carried voting power would not be inadvertently excluded from the Bill, members agreed to the view of the Administration that the proposed definition was necessary and appropriate.

"Working day"

Admin 26. Members pointed out that a "working day" might not be a "trading day". In order to avoid confusion between "working day" and "trading day", PAS/FS agreed to forward members' concern to the Law Draftsman for further consideration.

II Any other business

27. There being no other business, the meeting ended at 10:30 am.