

香港特別行政區政府財經事務局的信頭  
Letterhead of FINANCIAL SERVICES BUREAU, GOVERNMENT OF THE  
HONG KONG SPECIAL ADMINISTRATIVE REGION

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本函檔號 OUR REF.: C9/29C(2000)@Paper No. CB(2)1447/99-00(01)  
來函檔號 YOUR REF.:

20 March 2000

Ms. Pauline Ashall  
Partner  
Linklaters & Alliance  
10<sup>th</sup> Floor  
Alexandra House  
Chater Road  
Hong Kong

Dear Ms. Ashall,

**Securities (Amendment) Bill 2000**

I am writing in response to your letter of 3 March 2000, which was copied to the Chairman of the Bill Committee, and following our meeting this morning.

In view of the deliberation of the Bills Committee and the previous discussions between the Group and the Administration, we have proposed some amendments to the Bill, which we believe should help address the concerns raised. A mark-up copy of the Bill is attached for easy reference.

**Definition of “short selling order”**

As suggested by the Group, we have modified the drafting language of the proposed definition of “short selling order” by confining the proposed revised paragraph (i) to the borrowing side of a securities borrowing and lending agreement and by including the concept of a “hold” notice. It will also put beyond doubt that where the seller has issued irrevocable instructions to obtain the securities, the subsequent sale of such

securities will not fall within the definition of “short selling order” (the new paragraph (b) refers).

The Group has suggested that a sale of securities, which has been loaned out or obtained through a repurchase transaction or a swap, should not be regarded as a “reportable” short sale. In view of the prevailing practices both in Hong Kong and overseas, and on balance of the practical concerns of the industry vis-a-vis the potential systemic risks that may arise from the sales of securities loaned out or obtained through repurchases and swaps, we agree to exclude such sales from the proposed reporting regime. We have therefore proposed to delete paragraph (ii) of the definition of “short selling order”.

I also note that you have no strong view on whether the term “short selling order” should be replaced by, for instance, “reportable sale order” as long as its scope is clarified. I believe with the above proposed amendments, it will not be necessary to amend the term and on the advice of the drafting officer, we will keep the term.

Separately, in your letter of 3 March 2000, you have proposed to remove the rule-making power by the Securities and Futures Commission (“the SFC”) to prescribe the types of agreement or arrangement that may fall within the definition of “short selling order”. The Administration believes that the SFC as the market regulator should be vested with sufficient flexibilities to cope with market changes and developments and to improve its regulatory functions within the remits of the primary legislation. It may also be useful to note that such rules are subsidiary legislation and subject to negative vetting by the Legislative Council. We therefore maintain that that paragraph should not be deleted.

### **Obligations under section 80B**

The Administration remains of the view that the proposed reporting requirements are necessary and appropriate in maintaining the discipline and transparency of short selling activities. Indeed, as we have previously pointed out, the proposed provisions stipulated in the Bill generally mirror the existing reporting and disclosure requirements under the relevant Rules of the SEHK and Code of Conduct issued by the SFC, except that the Bill will also seek to extend the reporting requirements to

other market participants in addition to SEHK Members (now “exchange participants”). In addition, to ensure an effective and meaningful regulation of reported short selling, documentary assurance that the seller has a presently exercisable and unconditional right over the securities to which the short selling order relates must be available at the time when the short selling order is placed. We note that the Group has considerable concerns about the requirement for obtaining documentary assurance and the potential administrative burden on the industry. However, as I have pointed out in my letter of 25 February 2000, such documentary evidence is not only essential to support prosecution but also important for the protection of interests of both the intermediaries and their clients. At present there is a similar requirement by the Hong Kong Futures Exchange upon its members and we are not aware from the futures industry that there is an insurmountable problem, both in terms of technology or actual implementation. We therefore do not consider the redraft proposed by the Group dated 3 March 2000 acceptable.

On the basis of the views previously raised by the Group and the comments of other members of the industry, we have proposed to modify the proposed section 80B by clarifying that the short seller is only required to confirm with the counterparty to the agreement or arrangement concerned that such counterparty will provide the securities to him and a new subsection (7) is added to provide for a defence if the defendant did not know or had no reasonable ground to believe that the order was a short selling order. A new subsection (2A) is also added to address the concern in respect of the position of a fund manager or a trustee selling under any discretionary authority.

### **Obligation to disclose short selling order**

We agree to the suggestion made by the Group that an offence is committed under section 80C(3) if the person “knowingly or recklessly” contravenes subsection (1). We will also introduce amendments to replace “stockbroker” with “exchange participant” in the light of the enactment of the Exchanges and Clearing Houses (Merger) Ordinance.

**Rules made under section 146**

In addition to the proposed rule-making power of SFC in respect of the record-keeping requirements on stock lenders, we propose to extend the rule-making power of SFC to demand copies of such records as necessary. This is necessary as stock lenders usually are not registrants of the SFC which has no power to demand information from such persons.

**Other drafting matters**

In your letter of 3 March 2000, you have also raised some suggestions in respect of the drafting of the Bill which are essentially technical in nature. We will request the drafting officer to give further considerations to them and incorporate them into the amendments as appropriate.

We hope the above help address the concerns of the Group of 14, the PASLA and the Hong Kong Securities Industry Group. We will explain the same to the Bills Committee at its meeting tomorrow.

Yours sincerely,

(Bryan P. K. Chan)  
for Secretary for Financial Services

Att.

c.c. The Hon. Ronald Arculli, Chairman of the Bills Committee  
Mrs. Constance Li, Clerk to Bills Committee  
Ms. Stella Chan, Department of Justice  
Mr. Mark Dickens, SFC