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**Paper for the House Committee Meeting
of the Legislative Council
on 12 November 1999**

**Legal Service Division Report on
Exchanges and Clearing Houses (Merger) Bill**

Object(s) of the Bill

The objects of the Bill are to facilitate the regulation of the Stock Exchange Companies within the meaning of section 2(1) of the Stock Exchanges Unification Ordinance (Cap. 361), Exchange Companies within the meaning of section 2(1) of the Commodities Trading Ordinance (Cap. 250) and the recognized clearing houses within the meaning of section 2(1) of the Securities and Futures (Clearing Houses) Ordinance (Cap. 420) by :-

- (a) prohibiting a person from becoming or continue to be the controller of an Exchange Company or clearing house unless the person is a company recognized by the Securities and Futures Commission as an exchange controller;
- (b) regulating a recognized exchange controller in relation to the Exchange Companies and clearing houses of which it is the controller;
- (c) providing for the conversion of the Hong Kong Securities Clearing Company Limited from a company limited by guarantee to a company limited by shares; and
- (d) providing for other consequential matters.

LegCo Brief Reference

2. SUB 56/7 (99) issued by the Financial Services Bureau and dated 4 November 1999.

Date of First Reading

3. 10 November 1999.

Comments

4. Although the title of the Bill contains the word "merger", the provisions of the Bill do not directly deal with the merger process of the existing Exchange Companies and clearing houses. The merger is rather presumed as an accomplished fact.

5. The Bill envisages a scenario in which the Exchange Companies and clearing houses would be controlled by certain controller or controllers. A controller of a company is a person who either alone or with any associate or associates is entitled to exercise, or control the exercise of, over 35% of the voting rights at any general meeting of the company or another company of which the company is a subsidiary. The Securities and Futures Commission ("SFC") shall exercise regulatory jurisdiction over such controller(s).

6. The regulation of the controller(s) is exercised by SFC through the following means :-

- (a) the grant or revocation of recognition of the controller(s), as exchange controllers without the recognition of, or upon the revocation of recognition by, SFC as recognized exchange controller cannot continue to hold the shares which constitute it a controller;
- (b) the approval by SFC of persons having 5% or over interest in a recognized exchange controller, as no person may be entitled to exercise, or control the exercise of, 5% or more of the voting rights at any general meeting of a controller or another company of which the controller is a subsidiary without the approval in writing of SFC;
- (c) the approval by SFC in writing of the amendment of the constitution or rules, the appointment of the Chairman and Chief Executive or Chief Operating Officer of a recognized exchange controller; and
- (d) the approval by SFC in writing of the listing of a recognized exchange controller.

7. SFC further has power to give directions to a recognized exchange controller where it is satisfied that a conflict of interest exists between the recognized exchange controller or the company controlled by it and the proper performance of functions conferred by the Ordinance on the recognized exchange controller or the company controlled by it.

Public Consultation

8. There has not been any public consultation on the Bill. However, the proposals of reforming the domestic securities and futures market were first announced by the Financial Secretary in his Budget Speech on 3 March 1999. Two papers, "A Policy Paper on Securities and Futures Market Reform" and "Hong Kong Exchanges and Clearing Limited: Reinforcing Hong Kong's Position as a Global Financial Centre", were published respectively in March and July 1999. According to the LegCo Brief, the public and market feedback has been widely reported in the mass media and there has been continuous dialogue with the industry on the merger proposal.

Consultation with LegCo Panel

9. The Financial Affairs Panel has been briefed on the securities and futures market reform on 8 June 1999. The reform and the legislative proposal were also mentioned during the Briefing by Bureau Secretaries on the Chief Executive's Policy Address 1999 at the Panel meeting on 11 October 1999.

Recommendation

10. The Legal Service Division is still studying the Bill and will seek clarification from the Administration on certain legal and drafting aspects of the Bill. Since the Bill represents the first legislative installment of the anticipated major restructuring of the securities and futures market in Hong Kong and will affect the development of Hong Kong as an international financial centre, Members may wish to set up a Bills Committee to study the Bill in detail.

Prepared by

KAU Kin-wah
Assistant Legal Adviser
Legislative Council Secretariat
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