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BY HAND & BY FAX (No. 2869 6794)

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Dear Sirs

Mandatory Provident Fund Schemes (General) Regulation (the "General Regulation")

Further to the meeting of the Subcommittee held last Wednesday 26 April 2000 the group of custodians/trustees (named at the end of our 11 April 2000 letter) (the "**Group**") met yesterday with the MPF Authority to discuss further the Group's main points.

Following, and as a result of, that meeting with the MPF Authority we attach the Group's "drafting notes" which reflect the Group's requirements (which are not yet reflected in the Mandatory Provident Fund Schemes (General) (Amendment) Regulation 2000). These "drafting notes" remain subject to the MPF Authority's approval (and the FSB's consideration and approval).

In terms of the application of Schedule 3 to sub-custodian agreements (embodied in Section 72 of the General Regulation), the preferred route would be to repeal Section 72 altogether (for reasons previously explained). In the FSB's letter dated 20 April 2000, the FSB (admittedly in the context of permitted encumbrances) acknowledged that it is desirable that custodians should not have "... to renegotiate a new sub-custodial agreement with each of [their sub-custodians], which might be difficult, time-consuming and costly". The best way to achieve this would be to repeal Section 72. However, we understand that this may not be acceptable for a number of reasons. Accordingly, we have provided in the "drafting notes" an alternative to repealing Section 72, which the Group feel they can persuade their sub-custodians to accept. If neither alternative is approved, there must be a real risk that MPF compliant sub-custody agreements cannot be renegotiated with the result that schemes will not be able to invest in the markets operated by those sub-custodians. The Group feel that this is a real risk.

Representatives from the Group will be happy to attend the Subcommittee meeting on 16 May 2000. A list of these representatives will be submitted to you shortly.

Yours faithfully

Clifford Chance

Hkg-1/212309/01

cc Ms Susie Ho

Financial Services Bureau

Mr Greg Willis/Mr Raymond Tam
Mandatory Provident Fund Schemes Authority

MPF - Drafting Notes

1. Section 65

- Amend the first part of Section 65(2)(a)(iii) and (b)(iii):

"at the time the borrowing was made, it was unlikely that the period of the borrowing would exceed....."

- Add new Section 65(4):

(4) "For the avoidance of doubt, any encumbrance created over scheme assets of a registered scheme that is, at the time of creation, consistent with subsection (2) shall remain valid throughout the period for which the borrowing remains outstanding."

2. Section 72

- Repeal Section 72; **OR**
- Amend Section 72:

"Any agreement entered into between a custodian of scheme assets and any delegate of the custodian shall be on terms that are not inconsistent in substance with the requirements specified in Schedule 3".

Schedule 3

3. Paragraph 1(b):

- Amend Paragraph 1(b):

(b) "to be entrusted to the custodian for safe keeping;"

- Add new paragraph 1(c):

(c) "entrusted to the custodian:

(i) which are in registered form, to be registered in the name of the custodian or its delegate; or

(ii) which are in bearer form, to be held in the physical possession of the custodian, or its delegate;"

- Add new paragraph 1(d):

(d) "be segregated from the custodian's and its delegates' own assets."

- Add new Paragraph 1A:

"The agreement must require the custodian to hold any document of title and document evidencing title in its or its delegate's physical possession."

- Add new Paragraph 1B:

"The agreement must require the custodian to be responsible for the collection of any income due to be paid for the account of the scheme."

- Add new Paragraph 1C:

"For the avoidance of doubt, scheme assets:

- (a) comprising cash held by a custodian which is an authorised institution or an approved overseas bank may be held by such custodian in its capacity as a bank;
- (b) may be deposited by the custodian and its delegates with, and held in, any central securities depository on such terms as such central securities depository's customarily operate".

4. Paragraph 3

- Reflect in paragraph 3 the same changes as sections 652(a)(iii) and (b)(iii), described under 1. above.
- Add new Paragraph 4A:

"Any encumbrance created over scheme assets of a registered scheme that is, at the time of creation, consistent with paragraph 3 above shall remain valid throughout the period for which the borrowing remains outstanding."

5. Paragraph 5(a)

- Amend the first part of paragraph 5(a):

"for any direct losses incurred by scheme members that are....."

- Add proviso to the end of paragraph 5(a):

"...provided that the agreement need not require the custodian to indemnify scheme members for any indirect losses"