

立法會
Legislative Council

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Legislative Council
Panel on Financial Affairs

Minutes of Meeting held on
Monday, 14 February 2000, at 10:45 am
in the Chamber of the Legislative Council Building

Members present : Hon Ambrose LAU Hon-chuen, JP (Chairman)
Hon Albert HO Chun-yan
Dr Hon David LI Kwok-po, JP
Hon NG Leung-sing
Hon Ronald ARCULLI, JP
Hon CHEUNG Man-kwong
Hon HUI Cheung-ching
Hon Bernard CHAN
Hon SIN Chung-kai
Dr Hon Philip WONG Yu-hong
Hon Jasper TSANG Yok-sing, JP
Hon FUNG Chi-kin

Non-Panel members attending : Hon CHAN Kwok-keung
Hon CHAN Kam-lam

Members Absent : Hon Eric LI Ka-cheung, JP (Deputy Chairman)
Hon James TIEN Pei-chun, JP
Hon LEE Cheuk-yan
Hon Martin LEE Chu-ming, SC, JP
Hon James TO Kun-sun
Hon Emily LAU Wai-hing, JP
Hon Timothy FOK Tsun-ting, SBS, JP

- Public officers attending** : For Items IV and V
- Mr Bryan P K CHAN
Principal Assistant Secretary for Financial Services
- For Item VI
- Mr LEUNG Cham-tim
Director of Electrical and Mechanical Services
- Mr HO Kwong-wai
Deputy Director of Electrical and Mechanical Services/Trading Services
- Mr LAU kwok-choi
Principal Assistant Secretary for Works (Policy & Development)
- Miss Jenny YIP
Principal Assistant Secretary for the Treasury (Investments)
- Attendance by invitation** : For Items IV and V
- Mr Andrew L T SHENG
Chairman, Securities and Futures Commission
- Mr Mark DICKENS
Executive Director, Supervision of Market, Securities and Futures Commission
- Mr Alec TSUI
Chief Executive, The Stock Exchange of Hong Kong
- Mr Roger LEE
Director, Trading and Information Services, The Stock Exchange of Hong Kong
- Clerk in attendance** : Ms LEUNG Siu-kum
Chief Assistant Secretary (1)4

Staff in attendance : Ms Pauline NG
Assistant Secretary General 1

Ms Rosalind MA
Senior Assistant Secretary (1)6

I. Confirmation of minutes of previous meetings
(LC Paper Nos. CB(1) 899 and 936/99-00)

The minutes of meetings held on 1 November and 6 December 1999 were confirmed.

II. Information papers issued since last meeting

2. Members noted the following information papers issued since last meeting:

LC Paper No. CB(1)807/99-00 - Submission on sales tax

LC Paper No. CB(1)832/99-00 - Re-organization of the office of the Commissioner of Insurance

LC Paper No. CB(1)932/99-00 - "Members' Transaction Survey 1999" provided by the Stock Exchange of Hong Kong

LC Paper No. CB(1)946/99-00 - "Secondary Market Survey 1999" provided by the Stock Exchange of Hong Kong

III. Date of the next meeting and items for discussion

(LC Paper Nos. CB(1)944/99-00(01) and (02) - List of outstanding items for discussion and list of follow up actions)

3. Members noted that the next Panel meeting would be held on Monday, 6 March 2000 at 10:45 am in the Chamber of the Legislative Council Building. The Chairman invited members to propose items for discussion and pass them to the Panel Clerk before the next meeting.

(Post-meeting notes: The next Panel meeting was rescheduled for Monday, 13 March 2000 at 10:45 am.)

4. Members also agreed that the regular Panel meeting in May 2000 would be held on Tuesday, 2 May 2000 at 10:45 am. The Chief Executive of the Hong Kong Monetary Authority, Mr Joseph YAM, would be invited to brief members on the 1999 annual report of the Authority at that meeting.

5. The Chairman drew members' attention to the Administration's response to members' motion passed at the meeting on 6 December 1999 expressing objection to the Administration's ground rules for special consideration of private sector initiatives. In its response, which was circulated to members vide LC Paper No. CB(1)860/99-00, the Administration insisted that these ground rules provided the best justification for a departure from the norm in handling private sector initiatives. The Chairman invited members to consider whether the Panel should follow up on this matter.

IV. Trade disruption in the Stock Exchange of Hong Kong (LC Paper Nos. CB(1)969/99-00(01) and 944/99-00(03))

6. Mr Alec TSUI, the Chief Executive of the Stock Exchange of Hong Kong (SEHK), briefed members on the information paper tabled at the meeting. He expressed on behalf of the SEHK its sincere apology and regret to all those who suffered inconvenience as a result of the market disruption on 8 February 2000 and briefed members on the incident as follows:-

- (i) The temporary interruption to trading began at 15:08 and lasted for about 20 minutes. A power trip occurred on Hong Kong Island and affected the electricity supply to SEHK's computer room. As a result, SEHK's Uninterrupted Power Supply (UPS) as well as its alarm bell were triggered. While deactivating the alarm bell, the emergency stop button of the UPS system was accidentally triggered, resulting in the cut off of power supply to the entire Exchange Square data centre. Within five minutes of the interruption, members of the Contingency Management Team of SEHK assembled and initiated the normal emergency procedures. UPS power came back at around 15:13. The first terminals i.e. on-floor terminals in the trading hall began to resume operation automatically and to re-establish their Automated Order Matching and Execution System (AMS) connection. At 15:30, over 90% of the first terminals had completed their AMS connection. Hong Kong Telecom was requested to reset the network equipment to connect second and third terminals i.e. off-floor terminals which then recovered progressively.
- (ii) The trading system failed to shut down at normal close of trading which should be at exactly 16:00. Despite a temporary trade

disruption due to the accidental cut-off of UPS power supply to AMS, the Contingency Management Team had decided to maintain the normal trading hours. The message was disseminated to all relevant parties including the regulator and members through various channels immediately. However, when the UPS power supply was cut off, the system timer to close the market failed to activate when the clock hit 16:00. Such an effect on a system timer was unexpected and had never before been documented either by the AMS host system developer or by the manufacturer of the system. The trading system was shut down at 16:04 eventually. Following the close of the market, examination of the AMS database to assess the nature and extent of trading that had taken place after 16:00 was conducted. SEHK informed the regulator and announced to members and the media that trades executed after 16:00 would not be recognized.

7. Mr Alec TSUI also took this opportunity to brief members on the immediate and longer term follow up actions by SEHK after the incident. Immediate measures included tightening up control on the operation of and access to the UPS system as well as arranging briefing to all technical staff on the procedures for handling UPS. Moreover, arrangements had been made for the market close mechanism for AMS to be switched from automatic control mode into a manual control mode in the event of similar power interruption in the future. For longer term improvement, SEHK would appoint an independent consultant to review the system processes for handling the abnormal suspension of UPS and similar emergency situations in collaboration with the AMS host computer manufacturer.

8. Mr TSUI emphasized that the overriding objectives of SEHK under emergency situation were the maintenance of or rapid return to normal market operation and the minimization of market confusion. Both of these were keys to the decision to maintain continuous trading during scheduled trading hours. In addition, it was a central philosophy of SEHK that all market participants had to be made aware of events clearly and quickly so that they could make their own trading decisions. SEHK had established reliable channels for communication under emergency circumstances in line with this philosophy.

Discussion with members

9. While appreciating that there might be unforeseeable problems in any system, Mr Albert HO opined that the incident was not of a minor nature. The incident had attracted local and international attention and might have adverse impact on Hong Kong's image as an international financial centre. He commented that if appropriate precautionary measures had been in place before the incident, its occurrence could have been prevented. He pointed out that SEHK might be held liable for the losses caused by the trade cancellations and sought information

on whether there was any insurance coverage to provide for such claims for compensation.

10. Mr Alec TSUI explained that remedial actions had been taken in an expeditious, efficient and professional manner after the incident. Nevertheless, there was room for improvement and SEHK was trying its best to put in place precautionary measures for maintenance of normal market operation and proper procedures under emergency circumstances. He reiterated that the message of adhering to the normal trading hours, that is, no extension in the trading time, had been disseminated through various channels after the decision had been made by the Contingency Management Team. A press announcement was made immediately after the decision to cancel all trades executed after 16:00. As for the provision of compensation for claims of financial losses, he informed members that in accordance with the rules of SEHK, there would not be any compensation provided in this regard. It was also a general principle for stock exchanges all over the world that compensation would not be provided under such emergency circumstances. Nevertheless, he undertook to check the details of the insurance policy for any compensation provision in this connection.

11. Mr SIN Chung-kai sought clarification on whether consideration had been given to activate the market close mechanism for AMS manually when it was detected that transactions were executed beyond 16:00. Mr Philip WONG shared his concern and sought information on the means to monitor the exact amount of time being consumed during a manual termination. Mr Alec TSUI replied that the problem was detected immediately and the Contingency Management Team had considered manual termination of AMS as a remedy. However, there was a set of procedures required to activate the manual termination. In this particular incident, as the market closure was only delayed for four minutes, there was not enough time for the Team to make a decision and to execute the required procedures for the manual termination of AMS. He informed members that SEHK had drawn up a proposed measure of switching the market close mechanism for AMS from automatic control mode into a manual control mode in the event of similar power interruption in the future. As to the timing of the operation of a manual termination, he advised that exact timing for market closure would be ensured by taking the reference of the clock in SEHK, which was checked at a weekly interval.

12. In response to Mr Philip WONG's enquiry on the precautionary measures against the triggering of the emergency stop button of the UPS system, Mr Alec TSUI explained that the UPS controls and the alarm bell controls were all housed in the same control room of SEHK. Access to this room was confined to authorized persons. To prevent future reoccurrence of the incident, SEHK had set new requirements of having at least two qualified and experienced persons for the operation of the UPS system.

13. Mr FUNG Chi-kin pointed out that market participants had been confused during the incident. Some of them had got the message that normal trading hours would be extended to allow time for clearing the transaction backlog during the trade interruption. There were problems in the dissemination of information and not all market participants were kept informed of the up-to-date situation concerning market operation during the emergency. As a result, there had been a number of complaints from the clients and some of the brokers had to compensate their clients' loss in order to settle the matter. He complained that there was inadequate channel for the market participants to communicate with SEHK.

14. Mr Alec TSUI reiterated that the maintenance or resumption of normal market operation as well as the minimization of market disruption or confusion were of vital importance to the work of SEHK. These considerations were behind most of its actions in dealing with the incident. It was also SEHK's central philosophy that all market participants must be kept informed of events clearly and quickly so that they could make their own trading decisions. Reliable channels for communication under emergency circumstances had been established for this purpose and they were used accordingly during the incident.

15. Sharing Mr FUNG Chi-kin's views on the unsatisfactory dissemination of information to market participants, Mr CHAN Kam-lam urged SEHK to review the procedures for emergency operation and the operation of the AMS. Commenting on the difference in timing for the re-connection of on-floor and off-floor terminals to the AMS, he suggested that SEHK should consider the resumption of trading only when all the terminals were re-connected so that it would be fair to all market participants. Mr FUNG Chi-kin and Mr Philip WONG concurred and requested SEHK to study the feasibility of this suggestion. As regards the need for extension of trading time beyond 16:00, members had divergent views. Mr FUNG Chi-kin supported the extension of trading time and considered that such decision should be announced at the same time when trading was resumed after the interruption. Mr Philip WONG however opined that it would be preferable to stick to the normal trading hours since any changes to this well-established trading schedule might cause unnecessary market confusion.

SEHK 16. Mr Alec TSUI said that the suggestion of resuming trading for all terminals at the same time would be considered in the review of SEHK. Mr Andrew SHENG, Chairman of the Securities and Futures Commission (SFC), supplemented that problems had been revealed during this incident and lessons could be drawn from the experience. He explained that systemic risk was not involved in this incident. Nevertheless, the development of electronic transactions had increased the operational risk in the market. SFC and SEHK would work in cooperation for measures to minimize such risk. He said that improvements could be made in the following aspects:

- (i) On dissemination of information, messages and decisions should be disseminated to all market participants through different channels quickly and efficiently. SEHK had been trying to achieve this as far as possible during this incident and means for further improvement would be explored.
- (ii) On minimizing the operational risk, SFC and SEHK would work together to review the operational procedures.

17. As to the issue on the extension of trading hours, Mr Andrew SHENG explained that there was a set of procedures required for the extension. In this particular incident, SEHK did not have adequate time to complete the set procedures for an extension. The Principal Assistant Secretary for Financial Services (PAS/FS) added that SFC and the Financial Services Bureau (FSB) supported SEHK's decision of maintaining the normal trading hours given the circumstances surrounding the incident. He informed members that FSB would urge the SEHK and SFC to conclude the review of operational procedures as soon as possible. In addition to the above two aspects of improvement mentioned by Mr SHENG, it was suggested that consideration should be given to strengthening training of SEHK staff in information technology. The need for simplifying the standard procedures for extending the trading hours would be studied separately in due course.

V. Recent performances of the information technology-related stocks
(LC Paper Nos. CB(1)969/99-00(02) and 944/99-00(04))

18. Mr Andrew SHENG briefed members on the information paper regarding the performances of the information technology-related stocks (IT stocks). Members noted that in recent months, a number of IT stocks in Hong Kong had seen substantial rise in their share prices and trading volumes and that several IT stocks had outperformed the Hang Seng Index. Speculation in IT stocks had also been experienced in other major markets, such as NASDAQ in the United States, Neurer Market in Germany and the Techmart in London. Some analysts thought that the boom in IT stocks involved a much larger process of global resource allocation which reflected the increasing importance of information technology in the economy. The rise of the Internet-related industry and the possibility of substantial business potential of electronic commerce had fuelled worldwide investor interest. Since such Internet businesses were still in their infancy, there was little experience on how to value them. Price/earning ratios could not apply when earnings of many Internet companies were still negative. He drew members' attention to three aspects of work by SFC as a regulator under these circumstances, as follows:-

- (i) On information disclosure, SFC was working with the industries to provide investors with accurate, fair and timely information to make their decisions. As the regulator, SFC's responsibilities were to point out the risks and to ensure that everyone played by the rules of transparent, orderly and fair markets. The SFC felt that Internet companies should have independent verification of their disclosed "hit rate" and Internet membership, so that the market would have more reliable information to assess their operation. SFC was continually working with the exchanges and the accounting profession on areas such as the SEHK Rules to keep Hong Kong on par with best international standards, befitting its status as an international financial centre.
- (ii) On market surveillance, SFC would continue to monitor the trading on SEHK on a daily basis using a sophisticated computerized system that could identify any untoward movements in the prices and/or volumes of shares. It also analyzed media and corporate announcements daily. Since late 1999, relevant web pages and chat rooms on the Internet were included as part of its Internet surveillance program. If the untoward movement of a company's share price appeared to be based on rumors or speculative comment, SFC would take appropriate follow up actions. The company concerned would have to make an explanation of the movement or request suspension of trading, depending on the nature of the case. Both courses of action were aimed at keeping the market fully and fairly informed of matters that were relevant to the share price of a company. SFC would investigate further if certain untoward movements were indicative of market manipulation and /or insider dealing.
- (iii) On investor education, SFC would launch various education initiatives through the print, radio, television and Internet media as well as outreach activities in 2000. An Electronic Investor Resource Centre would be established, providing a 24-hour one-stop reference centre for investors. The education programmes would further reinforce SFC's key messages that it was important for investors to make informed decisions, to understand the nature of their investments and to know the level of risk they were undertaking.

Discussion with members

19. Mr Bernard CHAN expressed concern over the substantial rise in the share prices of a number of IT stocks in the recent months, in particular, the increasing trend of backdoor listing through acquiring a shell company. He sought information on measures to be taken by SFC for protection of investors' interest

during this IT stock fever. Mr Andrew SHENG responded that as US Federal Reserve Chairman Alan GREENSPAN commented earlier on that innovations in information technology was bringing about business opportunities and re-allocation of global resources, these opportunities came together with the risk involved in the investment of IT stocks. SFC's role was to ensure that all listed companies would disclose their business information accurately and in a timely manner so that investors could assess their own risks and make investment decisions accordingly. He advised investors to uphold the three “need-to-know” principles, as follows:-

- (i) To understand the nature of the stocks they intended to invest in;
- (ii) To understand the level of risk involved in the investment; and
- (iii) To understand the basic factors affecting the price of stocks and to assess the risk they were prepared to bear in the investment.

20. On the issue of backdoor listing, Mr SHENG said that companies seeking to be listed through this channel would have to satisfy the requirements under the SEHK Listing Rules, which were the same for all companies applying for new listing. Mr Alec TSUI supplemented that backdoor listing was one type of commercial activities. According to the SEHK Listing Rules, applications for listing through acquisition of a shell listed company would have to be vetted as if it was a new company if it intended to engage in business of a different nature.

21. Mr NG Leung-sing opined that in view of investors' increasing interest in IT stocks, it would be beneficial to investors if more choices could be provided in the stock market. In this connection, he urged SEHK to expedite the vetting and processing of applications from companies for listing on the Growth Enterprise Market (GEM). Mr Alec TSUI replied that there was a statutory requirement for the vetting and processing of applications for listing on GEM to be completed within 25 days of the applications. Nevertheless, in the event that the applicant failed to provide necessary information for the vetting, the processing of the case would be delayed. He cited the example of companies which had business partners in the Mainland. The processing of listing applications of these companies would have to be deferred if necessary legal documents had to be obtained from the Mainland authorities.

Admin 22. In view of members' concern over the vetting and processing of applications from companies for listing on GEM, the Chairman invited the Administration to provide additional information in this respect for members' reference after the meeting.

(Post - meeting note: The Administration had provided an information paper on "Vetting and processing of listing applications for the GEM" and this was circulated to members vide LC Paper No. CB(1)1136/99-00)

23. In response to Mr CHAN Kam-lam's concern over the measures SFC would employ in educating the public, in particular, on the risk that might be involved in their investment, Mr Alec TSUI said that there had been on-going programmes for investor education. Such programmes included seminars on the characteristics and investment risks of GEM stocks and pamphlets with emphasis on the investment risks involved in these stocks. In addition, investors were requested to sign an agreement to declare that they understood fully the risk related with their investments in these stocks. Continuing efforts would be made to increase public awareness of factors to be considered before investing in the stock market.

24. Mr HUI Cheung-ching sought information on the operation of the Internet surveillance program of the SFC, such as the number of internet-related stocks being monitored, the criteria for selecting these stocks and the penalty in case of misconduct. Mr Andrew SHENG said that all stocks would be included in the surveillance program of SFC. In the event that untoward movement in the price and/or volume of a stock was detected, SFC would take a series of follow up actions. It would inform SEHK which would then contact the company concerned to seek their explanation of the untoward movement. The company would have to make appropriate announcement on its corporate plans or to seek a suspension of trading in its stock pending a detailed announcement as to the status of those plans. SFC would also look out for any irregularities through its monitoring of relevant web pages and chat rooms on the Internet. SFC had close contacts with regulators in overseas jurisdictions for exchange of information and experience for surveillance on Internet.

25. On improvement to the disclosure of information by listed companies, Mr SIN Chung-kai enquired whether SFC would consider requiring listed companies for the publication of quarterly reports, electronic filing to SFC and establishment of companies' web pages which would be linked to the web page of SFC. Mr Alec TSUI replied that quarterly reports were already provided by companies listed on GEM. For other listed companies, consultation was underway on the feasibility of providing reports on a quarterly basis. In the meantime, these companies were requested to increase the frequency of their reports to a half-yearly basis. On the issue of electronic filing, SEHK had started the development of the related system in 1999 and it was anticipated that the system would be ready for implementation within 2000. As to the possibility of requesting all listed companies to set up their own web pages, SEHK and SFC were having discussion on the need for this requirement, the type of information required on the web pages, and whether a revision of SEHK Listing Rules would be justified. Consultations with market participants would be conducted on the

suggestion of statutory requirement of setting up companies' web pages. At present, the web page of SEHK was linked to that of the listed companies which had set up their own web pages. It was expected that the review and consultation in this regard would be completed by the end of 2000.

VI. Performance of the Electrical and Mechanical Services Trading Fund
(LC Paper No. CB(1)944/99-00(05))

26. The Chairman informed members that this item was referred by the Finance Committee after its discussion on a funding proposal raised by the Marine Department for replacement of the vessel traffic services system at the meeting on 11 June 1999. At the meeting, some members expressed concern about the viability and competitiveness of the Electrical and Mechanical Services Trading Fund (EMSTF) and suggested the issue be examined by relevant Panels. He then invited members to give their views on the information paper.

27. Mr SIN Chung-kai commented that the EMSTF had shown remarkable performance in the past years by achieving a cumulative productivity gain of 15% through various measures. The performance had demonstrated the importance of introducing competition. He sought information on whether there was any staff reward scheme for recognition of good performance. Moreover, he expressed concern over the reason behind the 6% reduction in staff number in the past three and a half years of trading fund operation and whether this reduction would become a continuous trend in future.

28. The Director of Electrical and Mechanical Services (DEMS) responded that there was a staff reward scheme in the form of cash coupons which benefited over 4,000 staff with a total expenditure of \$2 millions in 1999. As to the 6% reduction in staff number, he informed members that this was a result of natural wastage. The EMSTF had developed plans to maintain a stable customer portfolio and to achieve business growth. These included, sharing the productivity gain with its customers, providing staff training for producing good quality of service, maintaining close communication with customers and exploring and developing new business opportunities.

29. In response to Mr NG Leung-sing's enquiry on the number of user departments which chose alternative service providers under the first phase of EMSTF's untying programme, DEMS said that only two departments among the nine had done so. These two departments were hiring services other than that provided by the EMSTF only for a small part of their work and the effect on EMSTF's business was therefore very minimal.

30. Referring to paragraph 14 of the information paper, Mr HUI Cheung-ching sought clarification on the short-term fluctuations in business anticipated by

EMSTF. He also expressed concern over the business growth and the risk of having a deficit in EMSTF in the coming years when the untying programme was to be implemented by phases. DEMS responded that a short-term fluctuation in business had been anticipated. However, the experience in the first five months after the commencement of the first phase of the untying programme had shown that the business reduction in this regard was not that worrying. EMSTF had developed plans to promote its service quality and to explore more business opportunities. It was confident that with its continued effort to provide high quality and efficient services to its customers, business growth could be achieved in the coming three to five years and it would be able to meet the standard set by the Government without having any deficit.

VII. Any other business

31. There being no other business, the meeting was adjourned at 12:45 pm.

Legislative Council Secretariat

27 April 2000