

## **LEGISLATIVE COUNCIL BRIEF**

Securities and Futures Commission Ordinance (Chapter 24)

### **SECURITIES AND FUTURES COMMISSION (LEVY) (SECURITIES) (AMENDMENT) (No. 2) ORDER 2000**

#### **INTRODUCTION**

At the meeting of Executive Council on 30 May 2000, the Council ADVISED and the Chief Executive ORDERED that the Securities and Futures Commission (Levy) (Securities) (Amendment) (No. 2) Order 2000 (“Amendment Order”), at the Annex, should be made under section 52(1) of the Securities and Futures Commission Ordinance.

#### **BACKGROUND AND ARGUMENT**

##### **General Background**

2. Under section 52(1)(a) of the Securities and Futures Commission Ordinance (“the Ordinance”), a person who engages in the purchase or sale of securities recorded on the Stock Exchange of Hong Kong (“SEHK”) or notified to it under its rules is liable to pay to the Hong Kong Securities and Futures Commission (“SFC”) a levy at a rate specified by order of the Chief Executive in Council. The current rate of the levy is 0.011% of the relevant consideration as specified in paragraph 2 of the Securities and Futures Commission (Levy) (Securities) Order (“the Order”). Pursuant to the Securities and Futures Commission (Levy) (Securities) (Amendment) Order 2000, which is subject to negative vetting by the Legislative Council, the rate will be amended to 0.01% with effect from 12 June 2000.

3. As a means to further enhance its position as a major regional and international stock market, the SEHK launched a Pilot Programme on 31 May for the trading of selected overseas securities on the SEHK. As a start, the SEHK will allow in its securities market the quotation of a few large and well established corporations with track records listed on the National Association of Securities Dealers Automatic Quotations (“Nasdaq”) and the American

Stock Exchange (“Amex”). Those invited to participate in the Pilot Programme are foreign entities with several years of audited records of profits attributable to shareholders and a primary listing on the Nasdaq-Amex Market Group. The securities admitted to the Pilot Programme will have to be registered with the US Securities and Exchange Commission.

4. The Pilot Programme is expected to last for a period of three years during which the programme may be formalised into a permanent structure, extended, modified, or terminated, depending on its result and market needs.

5. The Pilot Programme Securities are not listed on the SEHK. Hong Kong laws and regulations which apply to “listed” securities and “listed corporation”, such as the Securities (Disclosure of Interests) Ordinance and the Securities (Insider Dealing) Ordinance, do not apply to the Pilot Programme Securities and issuers. Instead, they are primarily governed by the laws and regulations in their home market (in this instance the state and federal laws of the US and the listing requirements set by Nasdaq – Amex Group). In admitting these securities for trading on the SEHK, the SFC will ensure that the laws and regulations in their home exchange or market are adequate. In addition, the trading of Pilot Programme Securities in Hong Kong will also be governed by Hong Kong laws and regulations, including the market manipulation provisions under the Securities Ordinance. The market surveillance and supervision for Pilot Programme Securities will also be the same as for the existing securities market. The SFC has confirmed that this arrangement is legally in order.

6. As Pilot Programme Securities are not listed on the SEHK and are not required to maintain a share register in Hong Kong, their securities will not constitute Hong Kong stock and stamp duty will not be payable on the transfer of these securities.

7. In view of the special characteristics of the Pilot Programme, the SEHK will emphasize the special nature of the investments and the “buyers beware” philosophy similar to the SEHK Growth Enterprise Market. The Pilot Programme Securities will be assigned a separate series of stock codes. The SEHK has arranged educational seminars for brokers and prepared an education booklet for investors’ education.

8. Similar to Hong Kong securities, the Pilot Programme Securities are traded through the Exchange’s Automatic Order Matching and Execution System (“AMS”) under an order-driven and auto-matching mechanism. To promote liquidity, a limited number of designated market makers have been

invited for each security to provide two-way prices on the AMS order book. Market makers must be Exchange Participants of the SEHK and are required to obtain separate Pilot Programme Market Maker permits from the SEHK. Under the SEHK Rules, market makers are obliged upon occurrence of a wide spread in the bid-ask price of Pilot Programme Securities to enter two-sided market making orders to the AMS in no less than the minimum quantity, as specified by SEHK, and within the maximum spread of 10 times the smallest allowable change in share price as specified in the Rules of the SEHK. The SEHK Rules also govern the response time and the holding time of a market making order.

### **The Proposal**

9. In providing the services, market makers will have to take on additional financial and market risks in the process of making a market for particular securities. As a measure to encourage the SEHK Exchange Participants to provide market making services and provide the necessary trading liquidity of the securities concerned, it is proposed to exempt the Pilot Programme Market Makers from payment of the levy under section 52(1) of the Ordinance for their market-making trades. Investors trading Pilot Programme Securities are still required to pay the levy in the same way as for other securities traded on the SEHK.

### **THE AMENDMENT ORDER**

10. The Amendment Order seeks to amend paragraph 2 of the Order. Where a Pilot Programme Market Maker purchases or sells in such a capacity Pilot Programme Securities, the Amendment Order specifies the rate of levy for the purpose of section 52(1) of the Ordinance at 0% of the relevant consideration.

### **PUBLIC CONSULTATION**

11. The SEHK has consulted Exchange Participants who had shown interests in the Pilot Programme and the proposal was welcomed. Since the Amendment Order seeks to provide an exemption to Pilot Programme Market Makers, we do not think the public or the investing public are likely to be concerned. We therefore do not think that any further public consultation is necessary.

## **BASIC LAW IMPLICATIONS**

12. The Department of Justice advises that the Amendment Order does not conflict with those provisions of the Basic Law carrying no human rights implications.

## **HUMAN RIGHTS IMPLICATIONS**

13. The Department of Justice advises that the Amendment Order is consistent with the human rights provisions of the Basic Law.

## **BINDING EFFECT**

14. The amendment will not affect the current binding effect of the Order.

## **FINANCIAL AND STAFFING IMPLICATIONS**

15. There are no financial or staffing implications for the Administration. While theoretically it is possible that locally-listed companies in the SEHK may seek to transfer their listing to Nasdaq or Amex, with a view to participating in the Pilot Programme, such that transaction of their stocks will not be liable to payment of stamp duties, in practical terms such possibility is rather remote, bearing in mind that stamp duty is only payable by parties to the transaction and not the listed companies themselves and that a company is more concerned about the capital-raising capability of a market, the brand name effect of the listing status and above all the listing requirements and the regulatory regime. The Administration will keep in view the impact of the Pilot Programme on the market and would assess its overall effect when the Pilot Programme is reviewed in three years' time.

## **ECONOMIC IMPLICATIONS**

16. The proposal will help enhance the liquidity of the securities under the Pilot Programme and thus, by promoting trading in such securities,

will be conducive to enhancing the competitiveness of the Hong Kong securities market.

### **LEGISLATIVE TIMETABLE**

17. The legislative timetable as approved by the Executive Council is as follows –

Publication in the Gazette	2 June 2000
Tabling at Legislative Council	7 June 2000

### **COMMENCEMENT**

18. The Amendment Order will commence on 3 July 2000.

### **PUBLICITY**

19. The Amendment Order will be published in the Gazette on 2 June 2000 and a press release will be issued on the same day. A spokesman will be available for answering media enquiries.

### **ENQUIRIES**

20. For any enquiries on this brief, please contact Mr Bryan Chan, Principal Assistant Secretary for Financial Services at 2528 9161.

Financial Services Bureau  
2 June 2000