Bills Committee on Securities and Futures Bill and Banking (Amendment) Bill 2000

Summary of Public Comments and Administration's Response on Part XVI of the Securities and Futures Bill

Clause no.	Respondent	Respondent's comments	Administration's response
Part XVI – Miscellaneous			
366	Law Society	The SFC commonly states that clause 366 and its existing equivalent impose secrecy obligations on third parties during an SFC investigation or inquiry. The clause does not support this extension and the imposition of secrecy obligations on third parties can cause problems (e.g. if the SFC asks a bank for a client's account details, the bank cannot tell its client of the SFC request). Clause 366 should make third parties' secrecy obligations clearer.	Using the example described in the comment of the Law Society as an illustration, a bank required by the SFC to disclose customer banking records should not be allowed to inform its customer of the SFC request as this may warn its customers of the SFC investigation and increase the risk of evidence being destroyed, the targets of the investigation fleeing Hong Kong and proceeds of crime or misconduct being transferred overseas and out of reach. Clause 366(11)(a) makes clear that for the purpose of interpreting the meaning of "assisting any other person in the performance of any function under or in carrying into effect any of the relevant provisions" (which is defined under clause 366(15) as within the meaning of "specified person" who will be subject to the secrecy obligation under clause 366(1)), a person subject to an inquiry or investigation under clauses 172 to 174 and 176 as well as persons acting for him in this connection would be covered. We therefore do not agree that clause 366 does not support the imposition of secrecy obligations on these people.
369	HKSA	The Administration should consider extending this immunity to company secretaries, independent directors, employees and the like as auditors are frequently not the first people to detect fraud. The HKSA will be drawing up a practice note for auditors on the practical application of this section in consultation with the SFC. Auditors who are providing audit working papers and explanations to the SFC under clause 172 should not be exposed to additional liability as a result of rendering such	The issue of responsibilities of company directors and other officers and their accountability to shareholders will form part of the on-going review of corporate governance spearheaded by the Standing Committee on Company Law Reform. This will be a separate exercise independent of the immunity proposal under the SF Bill, which deals with a unique relationship with the company, i.e. an auditor of a listed company as an outside service provider carrying out an independent check on the company's accounts. We welcome the proposed positive step of the HKSA. The SFC is happy to co-operate with the HKSA in finalizing the practice note. Clause 368(3) provides immunity to a person who complies with a requirement made under any provision of the SF Bill, which covers an auditor providing audit working papers and explanations to the SFC

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		assistance. The explanations given by the auditors to the SFC could, if taken out of context, be subsequently used against the auditor in civil litigation by third parties.	under clause 172. In addition, audit working papers and explanations from auditors are protected from disclosure under clause 366.
370	KGI	A person should only be regarded as committing an offence under clause 370 if he without reasonable cause obstructs any other person in the performance of a function under or in carrying into effect any provision of the SF Bill.	It is in the interest of the public that the SFC should be able to perform its functions without being hampered by obstructive individuals. By way of information, the offence is comparable to the like offence provided in many other Ordinances, for example the Companies Ordinance, the Gambling Ordinance, the Building Management Ordinance, the Crimes Ordinance and the Prevention of Bribery Ordinance.
373	KGI	Clarification is sought as to whether the power of the SFC to intervene in third party proceedings under clause 373 represents "class actions" on behalf of the investing public or is designed for enabling it to provide expert opinion from regulatory perspective. If it is the former case, the proposal is welcomed. If it is the latter case, considerations should be given to the following observations: (a) There is inherent risk in allowing the SFC to intrude into court proceedings against the wishes of the litigating parties , as such might upset market certainty and cast substantial unjust to the litigants. (b) The more appropriate approach would be to understand the court ruling, and then issue guidelines to address the weaknesses and set the practice straight.	The objective of the proposal to allow the SFC to intervene in third party proceedings is to enable it to provide expert opinion from the regulatory perspective. The issue of "derivative action" is being considered separately in the above-mentioned Review of Corporate Governance. We have explained in paragraph 9 of Paper 14/01 the need for this proposal as well as the corresponding safeguards. In particular, having regard to the views of the Legislative Council Sub-committee on the SF Bill in 1999/2000 and the Bar Association, the SFC must consult the Financial Secretary before invoking the power and must be satisfied that its intervention would be in the interest of the investing public. Parties to the litigation will have the right to challenge the intervention and if the Court grants the SFC leave to intervene, the intervention will be subject to such terms as the Court considers just. Moreover, if the SFC is granted leave to intervene in proceedings, it may be subject to adverse orders for costs where the Court considers it appropriate. The procedures would be comparable to the current procedures for the joinder of third parties in civil litigation. We take the view the proposal strikes an appropriate balance between the wider interest of investors at large and the interests of individual litigants. The proposal provides the Court with expert opinion from the regulatory perspective only in justified cases such that its determination would be a more informed one. Amending and updating rules, codes and guidelines to take account of changes in market practices and conditions is a separate matter and on its own, would in some cases leave a regulatory gap in the interim.
378	Charles Schwab	The criteria adopted in clause 378 to attribute criminal liability to officers with respect to offence committed by the	We do not agree. As mentioned in paragraph 13 of Paper 14/01, the standard of "with the consent and connivance of" is adopted in section 101E of the Criminal

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		corporation they are acting or purporting to act for should be based on "intention" and "recklessness" only, instead of including "with the consent and connivance of" the person. Furthermore, the reference to 'purporting to act in such capacity' should be amended to include 'as authorized by the corporation' for ensuring that an unrelated third party outside of activities authorized by the corporation should not create liability for the corporation.	Procedures Ordinance. By way of information, section 400 of the Financial Services and Market Act also adopts such standard. We fail to see the unfairness in this standard given any corporation has to act through the mind and will of its officers; and the standard helps achieve a minimum standard of management responsibility. There is a mixed up in the market comment in that clause 378 deals only with the liability of an officer for an offence committed by a corporation where the offence is attributable to the officer, or to a person purporting to act in the capacity of an officer of the corporation; instead of the liability of a corporation for acts of its officers. Therefore, we are unable to construe clause 378 as having the effect expressed in the respondent's comment. As explained in paragraph 27 of Paper 14/01, the SF Bill would rely on the common law to deal with the liability of a corporation for acts of its officers, etc.
384 & 385	Charles Schwab	The general power for the SFC to promulgate codes and guidelines is essential to the flexibility and timely responsiveness of the SFC to developments in the market. The breadth of the rule making power provided both in clauses 384(1) and 384(2) is supported.	Noted.
384	Charles Schwab	The distinction between 'other matters for the better carrying out of the objects and purposes of this Ordinance' in clause 384(1) and 'necessary for the furtherance of its regulatory objectives and the performance of its functions' in clause 384(2) is unclear. As the two types of rules are to be subject to different procedural steps, further clarification about the distinction is required. In any case, all rules made by the SFC should be subject to public notice that allows for a reasonable period for comments.	Clause 384(1)(p) is a typical sweep-up clause designed to provide for the making of rules on subjects ancillary to those stated in the preceding paragraphs (in this case, clause 384(1)(a) to (o)). In other words, the coverage of clause 384(1)(p) is to be construed by reference to clause 384(1)(a) to (o). As for the rule making power provided in clause 384(2), it is intended to have a much wider scope and is to be construed with reference to the regulatory objectives and functions of the SFC. This is to ensure that, should the need arise, the SFC may make appropriate rules for the proper regulation of the market and to safeguard the interests of investors. By way of information, the UK Financial Services Authority is provided under section 138 of the Financial Services and Markets Act with a general rule-making power to make any rules that it considers necessary or expedient for the purpose of protecting the interests of consumers, for application to authorized persons. The SFC consults widely on any emerging rules and codes/ guidelines as a matter of practice. The express reference to the consultation requirement with respect to the

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			new reserve rule-making power proposed is intended to allay concerns of the market which is unfamiliar with this new arrangement; and in no way implies that consultation would not be conducted for other rules made. However, having regard to the concern of some Members and market participants, we are considering a Committee Stage Amendment to statutorily require the SFC to consult before making and publishing rules and codes/guidelines that affect market participants. The requirement should however be flexible enough to allow the SFC to respond to for example, emergency and exceptional circumstances in a timely and flexible manner.
388	Law Society	The compulsory use of forms specified by the SFC under clause 388 would not be desirable given the need to retain flexibility.	The use of prescribed forms is both convenient and appropriate, not least because it obviates arguments about whether sufficient or effective notification has been made. Furthermore, clause 388(5) allows the SFC to exercise discretion to modify the requirements in cases where there are genuine compliance difficulties.

Details of Submissions Referred to in the Comment / Response Table

Date received	Respondent
23 January 2001	Law Society of Hong Kong ("Law Society")
18 January 2001, 31 January 2001	Hong Kong Society of Accountants ("HKSA")
23 January 2001	KGI Asia Limited ("KGI")
29 January 2001	Charles Schwab

Securities and Futures Commission
Financial Services Bureau
18 May 2001