

For information
on 31 May 2004

**Bills Committee on
Clearing and Settlement Systems Bill**

**The Administration's Final Responses to
Recent Comments from Stakeholders**

Purpose

At the last meeting held on 21 May 2004, Members noted that the Administration had received further written submissions regarding the Bill from the Continuous Linked Settlement Bank International (CLS), Hong Kong Society of Accountants (HKSA) and Hong Kong and Shanghai Banking Corporation (HSBC). This paper sets out the Administration's final responses to their comments.

Continuous Linked Settlement Bank International

2. CLS, through its legal advisers in Hong Kong, raised the following comments with the Hong Kong Monetary Authority (HKMA) on 19 May 2004 –

- (a) references to analogous circumstances and analogous court orders in clause 22 of the Bill should be deleted to avoid unnecessary conflict of law issues; and
- (b) it should be clarified that the references to presentation of a petition for bankruptcy or winding up in clauses 26(1)(b)(i) and 27(1)(c)(i) refer to such occurrence in Hong Kong. This is to avoid a relevant insolvency office-holder appointed in a place outside Hong Kong seeking to take action under clauses 26 and 27, which is not a right of action intended by the Bill.

3. Following discussions with CLS and its legal advisers, the Administration has agreed to introduce Committee Stage Amendments (CSAs) to clause 22 to the effect of (a) above. For achieving (b), we have proposed a

CSA to amend the definition of “relevant insolvency office-holder” in clause 2 to clarify that the definition would only be confined to persons acting under the laws of Hong Kong. The legal advisers to CLS have confirmed with us that CLS has no further comment on the Bill.

Hong Kong Society of Accountants

4. The Administration received a letter from the HKSA on 20 May 2004, which was tabled at the Bills Committee at its meeting on 21 May 2004 in response to Members’ request. The HKSA suggested that the expression “[e]xcept to the extent that it expressly provides” at the beginning of clause 25 should be deleted; and sought clarification on the circumstances under which an exemption would be granted under clauses 26(4) and 27(4).

5. As we mentioned at the last meeting, the Administration had considered but did not agree to the HKSA’s comment on clause 25. Part 3 of the Bill as it now stands does not limit, restrict or otherwise affect the underlying transaction. However, we note that without the said expression it may be argued that rights etc. in respect of a transfer order are also protected under clause 25(1) to the extent that they may overlap with a right etc. mentioned in clause 25(1)(a). In other words, such expression helps to clarify that the protection of rights resulting from the underlying transaction as provided for under clause 25(1) is consistent with the savings in respect of the transfer order etc. provided for under clause 25(2). Regarding the exemptions under clauses 26(4) and 27(4), the policy intention is to grant these for the transactions entered into by a system operator or settlement institution (as the case may be) as first participant (as defined in the clauses) in its respective capacity as the system operator or settlement institution, but not as a participant or user of the designated system. We have conveyed these to the HKSA.

Hong Kong and Shanghai Banking Corporation

6. The HKMA received HSBC’s submission on 19 May 2004, at **Annex**, regarding clauses 27A, 40(1), 46 and 50 of the Bill. HSBC’s comments were, in essence –

- (a) that default arrangement was defined very broadly in clause 2(1) and there was a time limit for preparing and submitting a default proceedings report under clause 27A and contravention of the requirement was an offence where company officers could be held liable; and
- (b) that company officers could be held personally liable under clause 46 but the scope of immunity under clause 50 did not cover all the acts done by such officers.

7. The Administration appreciates HSBC's standpoint but the Bill has to carry reasonable requirements and appropriate sanctions to ensure that the oversight regime being established would function properly and achieve its purpose. We have explained to HSBC that the provisions and requirements under the Bill are reasonable.

8. First, on clause 27A, six working days are considered sufficient to prepare a report on a default case. Also, in response to HSBC's request, the HKMA has undertaken to provide guidance to designated systems on how default arrangements should be reported. Second, on clause 46, it should be noted that an officer of a corporation would not be liable unless either clause 46(a) or (b) is met. The term "officer" has also been appropriately defined in clause 2 of the Bill based on similar provisions in existing laws. As for immunity, we have explained to HSBC previously that clause 50 of the Bill provides civil immunity to system operators and settlement institutions as well as their employees and company officers if they are acting in good faith in carrying out the Monetary Authority's directions. Our policy intent is not to expand the immunity to cover all the other activities of the system operators and settlement institutions because doing so would prejudice the rights of other participants entering into contracts with these operators and institutions. HSBC noted our response and has not raised further comment.

Way forward

9. Apart from those mentioned in the preceding paragraphs, we have not received any further comment on the Bill since we issued the "Updated Summary of Comments Received and the Administration's Response" (LC

Paper No. CB(1)1870/03-04(02)) to Members for the last meeting on 21 May 2004. We have also checked with two other relevant parties, namely the Hong Kong Association of Banks and the Hong Kong Interbank Clearing Limited. They have indicated that they have no further comment to make.

10. The Administration has carefully considered the comments raised by relevant parties and in response proposed CSAs to the Bill as appropriate. We believe that the comments have been adequately addressed. All the CSAs have been incorporated in the latest marked-up version of the Bill circulated to Members on 27 May 2004.

Hong Kong Monetary Authority
Financial Services and the Treasury Bureau
27 May 2004

Annex
附件

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Subject: Clearing and Settlement Systems Bill - Latest Draft

Stanley

We refer to the latest draft Bill that is posted on the LECO's website under LC Paper No. CB(1) 1795/03-04(04), and advise our further comments as follow:-

Clause 27A - Duty to report on completion of default proceedings

This new clause imposes duty on SI and SO to report on completion of "any action taken under default arrangements" within 6 (working) days.

For the "Default arrangements", we find that it is defined very broadly in Clause 2(1), and the wording of 27A will oblige a report even if one of the less serious "default" actions is taken, which may not involve any netting at all (as is contemplated in Clause 27A(a)).

With reference to the corresponding section of the SFO (47), "default proceedings" is defined more restrictively to effectively refer to the taking of proceedings or similar action (section 40(2)(a)) and closing out actions (Part 5 of Schedule 3).

We would be grateful if MA could consider to narrow down the wording of 27A to refer specifically only to the taking of netting or closing out actions under the default arrangements and not "any action".

For the time limit of 6 (working) days, it appears to be rather short for preparing the report. In comparison to S47 of the SFO, there is no time limit imposed.

We would be grateful if MA could consider to lengthen the time limit (if not removed altogether).

Clause 40 (1) - Contravention of provision of Part 3

This new section makes the failure to comply with 27A an offence and, under 46, company officers may be held personally liable for the offence.

While it is understandable to impose a penalty for contravention of 27A, it does not seem reasonable to impose personal liability on officers on a matter that does not appear to have that much significance.

Please consider that 40(1) should only apply if a person contravenes 27A "without reasonable excuse".

Clause 46 - Liability of company officers

We note that the new definition of "officer" covers exactly the same range of persons in the original wording of 46. Also, the "senior" officers that is stated in the existing draft version in Chinese appears only in the heading of the Clause and not the text, and in any event, does not in any way thereby restrict the definition of "officer".

Despite that both USD SI and HKICL have reiterated our points several times, we are disappointed to find that the latest version of this clause still has not addressed our concern.

We also refer to the "Comments from HKICL of 28 April 2004 and the Administration's Responses" on 7 May with regard to the following:

Clause 50 - Immunity

Our view will largely be the same as for Clause 46.

Summary of Conclusion

We would like to confirm our understanding from the discussion among the HKMA, HKICL and USD SI at the meetings as follows:

- the current arrangements are considered to be adequate,
- should any changes be required in the future, HKMA will consult with HKICL and HSBC before requiring those changes to be implemented,

- a reasonable time-frame will be allowed for implementing the changes.

Please would you advise if otherwise.

Thanks and regards,
Susan

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