

立法會
Legislative Council

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Paper for the House Committee meeting on 2 June 2006

**Report of the Bills Committee on
Securities and Futures (Amendment) Bill 2005**

Purpose

This paper reports on the deliberations of the Bills Committee on Securities and Futures (Amendment) Bill 2005 (the Bill).

Background

Existing arrangements

2. The Securities and Futures Commission (SFC) was established under the then Securities and Futures Commission Ordinance (SFCO) in 1989 as the statutory regulator of the securities and futures market. In 2002, ten ordinances including SFCO were consolidated and modernized into the Securities and Futures Ordinance (SFO) (Cap. 571) which came into operation on 1 April 2003. The regulatory objectives, functions and powers, and general duties of SFC are set out in Part II of SFO, while the constitution and proceedings of SFC are set out in Schedule 2 to the Ordinance. The salient features of the existing governance structure of SFC are as follows:

- (a) SFC shall consist of a chairman and such number of executive directors (EDs) and non-executive directors (NEDs) as determined by the Chief Executive (CE), all of whom shall be appointed by CE. The number of members of SFC shall not be less than eight; and majority of the members of SFC shall be NEDs of SFC.
- (b) The Chairman of SFC shall, by virtue of holding that office, be regarded as an ED of SFC.
- (c) CE may appoint an ED of SFC as the Deputy Chairman of SFC.

3. Currently, the Chairman heads both the governing body (hereinafter referred to as the SFC Board¹) as well as the executive arm of SFC.

Proposed changes

4. In an effort to continually enhance the regulatory structure for the securities and futures markets in Hong Kong and to ensure the effective functioning of SFC to meet challenges of the future, the Administration has proposed to separate the role of the SFC Chairman from that of the executive arm. According to the Administration, the proposed split model is in line with the best governance practice both locally and internationally. Under the proposed structure, the Commission will be led by a Chairman who will have no executive responsibility for the day-to-day running of SFC while the executive arm will be headed by a Chief Executive Officer (CEO). The Administration has also drawn up broad principles governing the proposed division of responsibilities between the non-executive Chairman and the CEO as follows:

- (a) The SFC Chairman will not be involved in the day-to-day regulatory work. He/she should not influence the decisions of the executive arm on individual cases being reviewed or investigated. The Chairman should focus on the following-
 - (i) establishing and developing an effective SFC Board;
 - (ii) setting agenda and establishing priorities;
 - (iii) facilitating effective contribution of NEDs; and
 - (iv) representing SFC publicly in liaison with local and international financial institutions and other stakeholders.

- (b) The CEO will take up the executive responsibility on the day-to-day running of SFC. He/she should implement the objectives, policies and strategies agreed by the SFC governing body. The CEO's key responsibilities include-
 - (i) reporting to the governing body regularly with appropriate, timely and quality information;
 - (ii) informing and consulting the Chairman on all matters of significance to SFC;
 - (iii) developing and delivering the strategic objectives agreed with the governing body; and
 - (iv) overseeing the day-to-day operation and regulatory work of the Commission and ensuring that the Commission is equipped with the necessary staffing and financial and risk management system for its mission.

¹ Pursuant to section 1 of Part 1 of Schedule 2 to SFO, the Commission shall consist of a Chairman, executive directors and non executive directors. To distinguish between the Commission and its employees or staff, the term "SFC Board" is also used in this paper to represent the Commission.

The division of functions and responsibilities between the SFC Chairman and the CEO will not be spelt out in the legislation.

The Bill

5. The Bill seeks to amend SFO to give effect to the proposed governance structure of SFC under the split model. In gist, the Bill provides for:

- (a) the removal of the ED status of the Chairman of SFC;
- (b) the power of CE to appoint a CEO for SFC;
- (c) an excess of NEDs over EDs on the SFC Board; and
- (d) related and incidental matters.

The Bills Committee

6. At the House Committee meeting on 8 April 2005, Members decided to form a Bills Committee to study the Bill. Hon SIN Chung-kai was elected Chairman of the Bills Committee and the membership list of the Committee is in **Appendix I**. The Bills Committee has held nine meetings with the Administration and met with SFC and other interested parties. Individuals and organizations that have presented views to the Bills Committee are listed in **Appendix II**.

Deliberations of the Bills Committee

7. In considering the split model proposed under the Bill, the Bills Committee has examined the proposed arrangements under the new governance structure, as well as its implications on the future operation of SFC. The views and concerns raised by members are summarized in the ensuing paragraphs.

Need for the proposed change

8. The Bills Committee notes that when the Panel on Financial Affairs (FA Panel) was consulted on the splitting proposal in late 2004 and early 2005, members' views were divided. Nevertheless, the FA Panel passed a motion at its meeting on 17 February 2005 in support of the splitting proposal. Given that the SFO has only come into operation on 1 April 2003, some members of the Bills Committee have queried the need for the proposed change and cautioned against implementing the splitting proposal in haste. Meanwhile, the Bills Committee also notes that apart from one submission which has expressed disagreement, most of the deputations have indicated support in principle for the splitting proposal.

9. The Administration has highlighted the increasing complexity of the securities and futures market and the ongoing need for Hong Kong's regulatory

structure to meet future challenges. It has also referred to the governance structure of other local regulators and public bodies (such as the Mandatory Provident Fund Schemes Authority, the Hong Kong Exchanges and Clearing Limited, the Airport Authority and the Mass Transit Railway Corporation Limited) underpinned by a non-executive chairman and a CEO. The Administration considers that as a principal market regulator of the financial services sector, SFC should set an exemplary standard.

10. Regarding overseas experience, members note that the split model of the Financial Services Authority (FSA) of the United Kingdom (UK) and the Swedish Financial Supervisory Authority referred to by the Administration have only been implemented since 2003. Owing to the relatively short implementation experience and the differences in regulatory jurisdiction², some members urge for careful consideration on whether a similar arrangement should be adopted in Hong Kong for SFC.

11. Members are keenly aware of the need to consider the views of the SFC because the Bill, if enacted, will bring about a major change to its future governance structure. According to SFC's earlier submission in October 2004, the SFC Board had agreed in principle to the proposed split but was concerned about accountability and how the actual functions could be split between the SFC Chairman and the CEO. As stated in the submission, the majority of Board members also had doubt on whether the chairmanship could be a part-time post, given the complexity and range of policy and regulatory issues that SFC was tasked to handle. The Bills Committee notes SFC's view that the introduction of the Bill should not be taken as a reflection of the existing governance of the Commission which is working well, transparent and well respected by the market.

Delineation of roles and responsibilities

Actual division of responsibilities

12. Some members point out that the Administration has merely set out a series of broad principles that the SFC Chairman will have no executive responsibility for the day-to-day running of SFC and that such responsibility is vested with the CEO. They are gravely concerned about the lack of details on the delineation of roles and responsibilities of the two posts. Without such information, they consider it highly difficult to ascertain the effectiveness of the proposed split model. Some members further urge that the respective roles and responsibilities of the SFC Chairman and the CEO should be stipulated in the legislation.

13. As the Chairman and the CEO are key members of the SFC, the Administration considers that the detailed division of their roles and responsibilities should best be decided by SFC upon passage of the Bill. Such details will be

² For example, the FSA in UK is the sole regulatory body of the financial services industry in UK, including the banking, the investment business and the insurance sectors. Its regulatory jurisdiction is therefore much larger than that of the SFC.

attached to the appointment letter of the Chairman and the employment contract of the CEO and made known to the public on SFC's website. The Administration has also decided against stipulating the division of roles and responsibilities in the legislation for the reason that duties and responsibilities may evolve over time. Moreover, the current SFO does not prescribe the respective duties of the SFC Chairman, EDs and NEDs. Referring to the examples of local and overseas statutory bodies such as the Mandatory Provident Fund Schemes Authority and the FSA of UK, the Administration has advised that it is not a common practice to stipulate the respective functions and responsibilities of the chairman and the CEO of the regulatory body in its governing legislation.

14. Some members maintain strong reservation on being asked to pass the Bill without knowing how various responsibilities will actually be shared between the SFC Chairman and the CEO in future. They have urged the Administration and SFC to engage in discussion and come up with more concrete information. The Administration and SFC agreed, and worked together on the proposed division of responsibilities in the subsequent months. The proposed division of responsibilities between the SFC Chairman and the CEO finally presented to the Bills Committee is at **Appendix III**. In addition, the Administration has highlighted that following the split of the chairman post, there are a number of responsibilities the delivery of which will require the Chairman and CEO to work closely together. The Bills Committee notes that the proposed division of responsibilities will still be subject to refinement and formal approval by the SFC Board and may be amended by the SFC Board from time to time. The Administration also maintains its stance against stipulating the division of duties in the Bill.

15. Members note that pursuant to new section 9D proposed to be added to Part 1 of Schedule 2 to SFO, the SFC Chairman, Deputy Chairman and CEO will have such functions as are assigned to them by the Commission. On whether the functions thus assigned may turn out to be incompatible with the proposed roles and responsibilities of the Chairman and CEO, the Administration has advised that the functions to be assigned will be subject to the provisions of SFO and will not conflict with the principles as set out in the proposed roles and responsibilities of the Chairman and CEO.

16. Some members have pointed out that the row between the Chairman and the senior management of the Kowloon-Canton Railway Corporation (KCRC) in March 2006 has demonstrated amply the dire consequences which may result from unclear delineation of responsibilities between the non-executive chairman and the chief executive officer of a public body. Members urge the Administration to take heed of the incident and to set out in unequivocal terms the division of responsibilities between the future SFC Chairman and its CEO to avoid disputes and ambiguities which may adversely affect the operation of SFC. Noting members' concern, the Administration reiterates that the splitting proposal will help strengthen the internal checks and balances of SFC.

Performance of statutory functions

17. Members are concerned about the implications of the splitting proposal, if enacted, on the performance of a wide range of statutory functions currently vested with SFC under the SFO. Regarding the non-delegable functions specified in Part 2 of Schedule 2 to SFO and other powers and functions which the Board has not delegated, the Administration has confirmed that they will continue to be vested with the SFC Board which will be held collectively accountable for the exercise of these powers and functions.

18. Currently, there are eight statutory functions under the SFO which are assigned to the Chairman of SFC. The Administration has advised that arising from the changes to the role of the SFC Chairman and the creation of a new CEO post under the split model, the Administration has agreed with SFC's suggestion that amendments should be made in respect of five of these statutory functions to transfer or extend such functions to the future CEO. A table summarizing the relevant existing provisions with the proposed changes marked-up is at **Appendix IV**. The Bills Committee notes that since certain statutory functions are proposed to be conferred on the CEO, the Administration will introduce consequential amendments to the Bill to expressly provide for the inclusion of the CEO in the composition of SFC.

Proposed amendment to section 11(1) of the Ordinance

19. While the Bills Committee has no objection to most of the proposed changes as indicated in **Appendix IV**, some members express strong reservation on the proposed amendment to section 11(1) of SFO³ that CE should consult the CEO, instead of the SFC Chairman as currently required, before giving written directions to SFC. Noting that the power under section 11(1) of SFO will not be invoked lightly and will only be resorted to under exceptional circumstances, these members consider that the future SFC Chairman, being responsible for the overall policies and directions of SFC, should not be left out in the consultation process. They query the propriety of relegating the consultation requirement to the level of CEO. There is a further view that consequential to the split of the chairman post, both the Chairman and the CEO should be consulted under section 11(1) of SFO. Members have also discussed whether CE should be required to consult the SFC Board, instead of just the Chairman or the CEO.

20. The Administration explains that the proposal for the CEO to act as the channel for consultation by CE has been put forward by SFC. Since the future CEO will be the one who will understand best the detailed daily operation of SFC, he will be in the best position to respond to or advise CE on what is achievable as to the subject of the written directions. As section 11(1) of SFO will only be invoked in the most pressing and extreme circumstances, a requirement on CE to

³ Existing section 11(1) of SFO provides that after consultation with the chairman of the Commission, the Chief Executive may, upon being satisfied that it is in the public interest to do so, give the Commission written directions as to the furtherance of any of its regulatory objectives or the performance of any of its functions.

consult both the Chairman and the CEO or the whole SFC Board before giving written directions is not conducive to enabling the Government to respond to a crisis or emergencies in a timely manner. To address members' concern, the Administration will include a requirement in the duty list of the CEO that he should consult the Chairman and other member(s) of the Commission as appropriate before tendering advice to CE. The Administration has advised that where necessary, CE may also require the CEO to advise him of the views of the SFC Board. Hence, it would be unlikely that the SFC Chairman or the Board will not be aware of any prospective written directions to be issued to SFC.

21. In the view of some members, a mere administrative requirement in the CEO's duty list to consult the SFC Chairman and any other member of the Commission as appropriate before tendering advice to CE is insufficient. They maintain their grave reservation that as the power under section 11(1) of SFO will only be exercised under exceptional circumstances, it is inconceivable as to why only the CEO is required by law to be consulted. Some other members however consider the Administration's proposal of consulting only the CEO an acceptable arrangement in unforeseen and extreme scenarios.

22. As the Administration has decided to maintain its current proposal, there has been considerable discussion by the Bills Committee on whether and how section 11(1) of SFO should be amended to strengthen the consultation requirement, such as requiring CE to consult the SFC Chairman instead of just the CEO; or to extend the consultation requirement to the SFC Chairman and the Board. On another suggestion that CE should be required to consult the SFC Chairman and/or the CEO, most members of the Bills Committee consider the use of "and/or" in the relevant section imprecise and lacks clarity. Some members recall that during the scrutiny of the former Securities and Futures Bill, grave concern was raised about whether the reserve power under section 11(1) would become a tool for the Government to interfere with the operation of SFC, thereby eroding its independence as the market regulator. Noting that a similar reserve power is not available to other securities regulators such as FSA of UK, members have also discussed whether such reserve power under SFO can be removed by deleting existing section 11 altogether in the context of the current Bill. In the absence of any collective view reached by the Bills Committee, it has been agreed that it would be for individual members to decide whether they would propose amendments to section 11 of SFO as appropriate. Subsequently, Hon Margaret NG has proposed to move a Committee Stage Amendment (CSA) to repeal section 11 of SFO. Hon Ronny TONG has proposed a CSA to amend section 11(1) of SFO to require CE to consult both the SFC Chairman and the CEO before giving written directions to SFC.

23. Some members have taken the opportunity to request the Administration to consider including an additional provision under section 11 of SFO to require the Administration to make a public announcement of the written directions issued and to stipulate the timing for making such an announcement. The Administration's response is that at present, there is no provision in the SFO which prohibits the disclosure of the written directions given by CE under section 11(1) of SFO. CE

will decide whether to make public such written directions, and if so, in what manner. As there are no similar requirements in other securities-related ordinances, the Administration considers the proposed additional provision neither necessary nor appropriate. The Administration also considers that the provision to impose a legal obligation on the CE is a substantially different issue from those which form the purposes of the Bill and is therefore outside the scope of the Bill. Some members, however, do not subscribe to the Administration's view that the proposed provision is outside the scope of the current Bill.

Accountability

24. The Bills Committee has followed up the concern as to whether the future Chairman or the CEO should be held ultimately accountable for the affairs of SFC under the splitting proposal. The Administration's view is that the SFC Board is ultimately accountable for the performance of the SFC under the SFO and this will continue to apply in future. On the question of who will be the public accountable face of SFC, the Administration has advised that as a general principle, the Chairman should be accountable for the overall directions, policies, agendas, strategies and priorities of SFC while the CEO should be accountable for all operational matters.

25. On SFC's accountability to the legislature, members note that existing section 9 of the Urban Renewal Authority Ordinance (Cap. 563) and section 6A of the Kowloon-Canton Railway Corporation Ordinance (Cap. 372) provide explicitly that the committees and subcommittees of the Legislative Council (LegCo) may request the Chairman and the CEO of the two statutory organizations to attend its meetings and they shall comply. The Chairman and the CEO shall also answer questions raised by Members at the meeting. To enhance accountability, some members consider that a similar requirement should be included in the Bill. In this regard, the Bills Committee has noted its legal adviser's advice that the aforesaid sections are declaratory in nature and that non-compliance will not incur any sanction. If a similar provision is included in the present Bill, an inference may be drawn that where no similar provisions are explicitly stipulated in other pieces of legislation, the statutory bodies concerned will not be under an obligation or requirement to attend meetings of LegCo and its committees.

26. In the view of the Administration and SFC, concerns about the accountability of the SFC Chairman and the CEO to the legislature can be addressed by relevant provisions⁴ in the Legislative Council (Powers and Privileges) Ordinance (Cap. 382) which empower LegCo and its committees to order the attendance of any person to give evidence or to produce documents. As an independent regulator, SFC has always been and will continue to be cooperative with LegCo and its committees in respect of attending meetings on request and

⁴ Section 9(1) of the Legislative Council (Powers and Privileges) Ordinance (Cap. 382) empowers LegCo or its standing committee to order any person to attend before the Council or before such committee and to give evidence or to produce any paper, book, record or document in the possession or under the control of such person. Section 9(2) further allows any other committee specially authorized by a resolution of the Council to exercise the powers conferred by section 9(1).

providing information, subject to the confidentiality requirement of SFO. The Administration has also advised that existing legislation such as the Banking Ordinance (Cap.155) and the Mandatory Provident Fund Schemes Ordinance (Cap.485) do not contain provisions similar to section 9 of Cap. 563 and section 6A of Cap. 372. Nevertheless, the Administration will include the requirement of attending meetings of LegCo's committees, where requested and appropriate, in the duty lists of the SFC Chairman and the CEO.

27. Some members maintain their preference for a statutory obligation, instead of merely an administrative requirement in the duty lists. They are concerned that if not obliged by law, the SFC Chairman and the CEO will have too much discretion in deciding whether or not to attend meetings of LegCo's committees, as well as the level of representation. These members are keen to ensure that although on this occasion, the Administration has declined to include such an attendance requirement in the Bill, this should not be taken to imply that similar obligation should not or need not be stipulated in other legislation in future. Some members however agree that to allow for a certain degree of flexibility, it may not be necessary or appropriate to specify the attendance requirement in law having regard to the cooperation displayed by SFC so far and its status as an independent market regulator. As no general agreement has been reached on the issue, members agree that the Bills Committee will not move an amendment to the Bill in its name but individual members are at liberty to consider doing so.

Appointment of the future SFC Chairman

Selection of candidates

28. Given the crucial role of the SFC, the Bills Committee and deputations concur on the need to appoint a person with the necessary expertise and experience to take up the chairman post to provide the necessary steer to SFC. Some members urge for an independent and objective mechanism such as a selection panel, instead of arbitrary appointment by CE based on political considerations. Where necessary, the Administration should conduct a global search for the most suitable candidate instead of limiting its search to a small pool of candidates as in the case of making appointments to advisory and statutory bodies.

29. The Administration has stressed that it is keenly aware of the need to select the right candidate based on merit and having regard to the requirements of the post. The appointment will be made in accordance with the existing appointment system for advisory and statutory bodies. Through various sources, the Financial Services and the Treasury Bureau will draw up and finalize a list of qualified and suitable candidates for the consideration of CE who will appoint the SFC Chairman pursuant to section 1, Part 1 of Schedule 2 to SFO. On whether there is any preference for local or overseas candidates, the Administration highlights that the essential qualities required for the post include good understanding of the local and international financial markets, integrity, commitment, vision and ability to interact with various stakeholders.

Full-time or part-time nature of the post

30. Noting that the incumbent SFC Chairman is an executive and full-time post, some members share the concern raised by some deputations on whether the future Chairman not working on a full-time basis can effectively discharge his responsibilities. The Administration however does not consider it meaningful to distinguish whether the future chairman post is full-time or part-time as the post is not to be regarded as an employment with SFC but a service to the community. Its view is that when a candidate agrees to take up the chairmanship, he/she also accepts the heavy responsibilities and high public expectation associated with the post and should have the commitment and willingness to spend as much time and effort as necessary to fulfil the Chairman's role and responsibilities.

Remuneration

31. Some deputations have submitted to the Bills Committee that the remuneration for the future SFC Chairman should be set at a competitive level commensurate with the level of responsibility of the post. The Hong Kong Society of Financial Analysts in particular has highlighted the industry's view that the SFC requires a full-time, competitively remunerated and technically competent chairman. Their concerns are echoed by some members who have enquired about the underlying principles and objective criteria for determining the remuneration of the chairman post.

32. In this connection, the Administration reiterates that the appointment in question is a community service and not an employment with SFC. In proposing a remuneration at \$702,000 per annum, which is three times that of NEDs of SFC, the Administration has taken into consideration the role and responsibilities of the future SFC Chairman, the remuneration of non-executive chairmen of other statutory bodies in Hong Kong which ranges from nil to not more than \$1 million per annum. The Administration considers that for individuals with a commitment to serve Hong Kong, remuneration is not their key consideration. It has also indicated that the actual level of remuneration can be further negotiated with the identified candidate.

33. Some members and deputations do not subscribe to the Administration's viewpoint. They consider the proposed \$702,000 per annum a token remuneration which is not commensurate with the demanding responsibilities of the SFC Chairman. It is also noted that for the FSA in UK where a split model is in place, its chairman's remuneration is much higher at about £ 300,000 per annum. Some members remain gravely concerned that the Administration may only be able to make its selection from a limited pool of individuals willing to undertake public duty at a modest honorarium, instead of being able to appoint a person possessing the necessary competence and commitment to take up the SFC chairman post.

Arrangement for acting appointment

34. At present, it is the usual practice that in the temporary absence of the SFC Chairman, the Chief Operating Officer of SFC is designated to act as Chairman pursuant to section 6, Part 1 of Schedule 2 to SFO. Members have enquired about the acting arrangements to be put in place during the temporary absence of the future Chairman or the CEO under the split model. The Bills Committee has also made reference to the FSA of UK and notes that there is no express provision in the relevant Act to provide for acting arrangements.

35. The Administration has advised that since the duties of the current SFC Chairman is executive in nature, there is a practical need to arrange for acting appointment in the absence of the Chairman in order that the day-to-day management and operation of SFC will not be affected. Under the split model, however, the responsibilities of the Chairman are non-executive, strategic and long-term in nature. Hence, it may not be necessary to arrange an acting appointment on each occasion of the future Chairman's temporary absence. Its current thinking is that if necessary, the future CEO may act as the SFC Chairman during the latter's temporary absence. If the Chairman is absent for a relatively long period, consideration will be made for a NED to act as Chairman. For prolonged absence and where circumstance so warrant, consideration will be made for CE to appoint a new Chairman. Although it is provided in the Bill that CE may appoint an ED or NED to be the Deputy Chairman of the Commission and that the Deputy Chairman shall act as Chairman, the Administration has stated that it has no policy intention to appoint a Deputy Chairman should a CEO be appointed.

36. Regarding the acting arrangement when the future CEO post is vacant or when the CEO is unable to act, the Administration's previous thinking was that administrative arrangements would be made for other EDs to take up or share the CEO's duties during the latter's temporary absence. Nevertheless, in response to members' concern for a clearer delineation of roles and responsibilities, the Administration has proposed to confer certain statutory functions on the future CEO, including a new section 9B in Part 1 of Schedule 2 to SFO to provide for CE's designation of an ED to act as CEO when the CEO is unable to act due to illness, absence from Hong Kong or any other cause, and that the designation may be revoked at any time.

Safeguards against conflict of interests

37. The Bills Committee agrees that as the head of SFC, the independence of the Chairman is of vital importance for inspiring public confidence in the securities and futures markets in Hong Kong. Concern has been expressed as to whether adequate safeguards are in place to avoid any real or perceived conflict of interests between the roles of the future SFC Chairman and his/her past or current employment/connections with listed or private companies. The Administration has assured members that it attaches great importance to the independence of the Chairman from any perceived or real conflict of interests. On statutory safeguards, members take note of sections 378 and 379 of SFO

which govern the preservation of secrecy and avoidance of conflict of interests respectively. The relevant provisions in the Prevention of Bribery Ordinance (Cap. 201) are also applicable to all members (including Chairman, EDs and NEDs) and staff of SFC. Moreover, SFC's internal code of conduct which sets out the requirements on confidentiality, conflict of interests, personal investments and prevention of bribery, will continue to apply to the future Chairman, EDs and NEDs and staff of SFC under the split model.

38. The Bills Committee's attention has been drawn to the additional requirements on the future SFC Chairman that he/she should not be a director in any listed company in Hong Kong; and should not have any material interest in any principal business activity or be involved in any material business dealing with any persons or institution regulated by SFC. Some members have sought clarification on what constitutes "material interest" and "material business dealing".

39. According to the Administration, an example of "having a material interest" would be shareholder status or directorship of the SFC Chairman in a listed company/licensed intermediary. For a listed company, the holding of about 5% shares may be regarded as material. As regards being "involved in any material business dealing with a listed company/licensed intermediary", an example is where the SFC Chairman or a company in which he holds shares or is a director has business dealings with the listed company or licensed intermediary. Where the proposed SFC Chairman is a partner of a law firm whose clients are listed companies regulated by SFC, the Administration takes the view that there is a risk that a potential or real conflict of interest may arise if the proposed candidate is appointed as Chairman of SFC. Hence, as a condition for appointment, the candidate will be required to resign from the law firm. During the term of appointment, he/she should not have any direct or indirect interest in the law firm.

40. Concern has been raised about the efficacy or otherwise of the additional safeguards as they are only administrative, not statutory, requirements and carry no sanction against non-compliance. The Administration's intention is to include them in the terms of appointment of the prospective Chairman. In accepting the appointment, the candidate will be required to agree to comply with these requirements. The Administration does not consider it necessary to include the additional safeguards in the law as sections 378 and 379 of SFO already provide criminal sanctions against any person who breaches the secrecy and avoidance of conflicts requirements under these two sections.

SFC's participation in the International Organization for Securities Commissions (IOSCO)⁵

41. Noting that Mr Andrew SHENG the former Chairman of SFC, has chaired the Technical Committee of IOSCO, some members are concerned whether the

⁵ IOSCO was created in 1983 and is today recognized as one of the world's key international standard setting bodies with a wide international membership.

appointment of a non-executive Chairman may have adverse implications on SFC's international status and its participation in IOSCO. They also note from SFC's written submission that the securities regulators which are members of the Technical Committee are all headed by executive chairmen and that there may be a risk for Hong Kong if SFC is denied the opportunity in the future to take up important chairmanship positions in the international community because some executive chairmen may not consider a non-executive chairman as an equal. In this regard, the Administration has provided for the Bills Committee's reference the written advice by the Secretary General of the IOSCO that the appointment of the Chairman of the IOSCO Technical Committee is a personal appointment based on the recognized experience and authority of the appointee, rather than on the executive nature or otherwise of the post held by the person.

42. To assess further the impact of the splitting proposal on Hong Kong's standing in the IOSCO Technical Committee, the Bills Committee has consulted the Chairman of the Executive Committee of IOSCO and the Deputy Chairman of the Technical Committee of IOSCO on their views. In the opinion of the former, the IOSCO principles are sufficiently broad to be adapted to domestic contexts and to provide some flexibility with respect to the governance structures of securities regulators. As such, there will be no bar to participation in IOSCO by a non-executive chairman. Nevertheless, in the selection of the Chairman of the Technical Committee, other executive chairmen may well not be confident in appointing a person who is not having detailed technical knowledge and experience normally gained from the day to day work as a securities regulator. The Deputy Chairman of the Technical Committee has advised that each regulatory body is responsible for appointing its representative to IOSCO. Active participation in discussions and chairmanship of various committees may hinge on the level of authority the representative can command. However, to the best of his knowledge, every member of the Executive Committee of IOSCO or of the Technical Committee is an executive chairman.

43. Notwithstanding that there has not been any explicit comment on the desirability of a non-executive chairman of a securities regulator to chair committees of IOSCO, members note that relevant professional knowledge and experience possessed by the person in question are key factors for consideration. The Administration has also advised that in actual practice, participation and chairmanship at the committees of IOSCO are not restricted to executive chairmen of securities regulators. Currently, securities regulators from different jurisdictions are represented at various committees/sub-committees of IOSCO by their chairmen, vice-chairmen, secretary-generals, executive directors, or chief executive officers etc.

Committee Stage Amendments

44. The full set of CSAs to be moved by the Administration is at **Appendix V**. The Bills Committee will not move any CSAs in its name. The CSAs proposed to be moved by Hon Margaret NG and Hon Ronny TONG are at **Appendices VI** and

VII respectively.

Recommendation

45. The Bills Committee supports the resumption of the Second Reading debate on the Bill on 14 June 2006.

Advice sought

46. Members are invited to note the recommendation of the Bills Committee in the preceding paragraph.

Council Business Division 1
Legislative Council Secretariat
1 June 2006

**Bills Committee on
Securities and Futures (Amendment) Bill 2005**

Membership List

Chairman Hon SIN Chung-kai, JP

Deputy Chairman Hon Ronny TONG Ka-wah, SC

Members Hon Margaret NG
Hon Bernard CHAN, JP
Hon CHAN Kam-lam, SBS, JP
Hon Howard YOUNG, SBS, JP
Hon Emily LAU Wai-hing, JP
Hon Abraham SHEK Lai-him, JP
Hon Audrey EU Yuet-mee, SC, JP
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon Andrew LEUNG Kwan-yuen, SBS, JP
Hon WONG Ting-kwong, BBS
Hon CHIM Pui-chung
Hon KWONG Chi-kin
Hon TAM Heung-man

(Total : 15 Members)

Clerk Miss Polly YEUNG

Legal Adviser Mr KAU Kin-wah

Date July 2005

**Bills Committee on
Securities and Futures (Amendment) Bill 2005**

**List of individuals and organizations that have
presented views to the Bills Committee**

1. Securities and Futures Commission
2. Hong Kong Stockbrokers Association Limited
3. The Institute of Securities Dealers Limited
4. Hong Kong Securities and Futures Industry Staff Union
5. Hong Kong Society of Financial Analysts Limited
6. The Law Society of Hong Kong (Securities Law Committee)
7. Mr David M WEBB
8. Mr Ermanno PASCUTTO

**Proposed Division of responsibilities
between Chairman and CEO of SFC¹**

(A) Role and responsibilities of the chairman of the SFC

1. The Chairman has no executive responsibility for the day-to-day running of the SFC.
2. His/her key responsibilities are to –
 - (a) establish and develop an effective Board;
 - (b) lead the Board as a team;
 - (c) plan and manage the Board's business;
 - (d) lead the Board in its setting of the overall directions, policies, strategies, agendas and priorities of the Commission;
 - (e) facilitate effective contributions by the non-executive directors;
 - (f) maintain and develop a productive relationship with the CEO;
 - (g) with the CEO, ensure that key issues are discussed by the Board in a timely manner, that the Board has adequate support and is provided with all the necessary information on which to base decisions
 - (h) with the CEO, lead the communication of SFC policies to its stakeholders;
 - (i) as Chairman of the Commission, represent the SFC officially at the local and international level, as appropriate, including attending meetings of the committees and subcommittees of the Legislative Council when requested;
 - (j) provide a source of counsel and challenge to the CEO on how the SFC is run, including giving feedback to the CEO on senior management performance, development and succession, and on organizational structure; and

¹ The proposed duty lists of Chairman and CEO set out in this document are subject to refinement and formal approval by the SFC Board and may be amended by the SFC Board from time to time.

- (k) Evaluate the effective functioning of the Board, SFC committees and individual directors.

(B) Role and responsibilities of the CEO of SFC

1. The CEO has the overall executive responsibility for the day-to-day running of the SFC and specific functions or duties delegated by the Board from time to time.
2. His/her key responsibilities include -
 - (a) implementing the strategy agreed by the SFC Board, in whose formulation s/he will have played a major part, and facilitating the effective functioning of the Board;
 - (b) reporting to the Board regularly with appropriate, timely and quality information so that the Board can discharge its responsibilities effectively;
 - (c) informing and consulting the chairman and the Board on all matters of significance to the SFC including helping ensure that key issues are discussed by the Board in a timely manner, that the Board has adequate support and is provided with all the necessary information on which to base decisions;
 - (d) developing and delivering the strategic objectives agreed with the Board including helping to set the agenda and establish priorities for the SFC;
 - (e) recommending to the Board significant operational changes and major capital expenditures where these are beyond the delegated authority;
 - (f) assigning responsibilities clearly to senior management and supervising the work of other Executive Directors;
 - (g) overseeing the day-to-day regulatory work of the Commission and ensuring that the Commission is equipped with the necessary staffing, financial and risk management systems for its mission;

- (h) tendering advice to the Chief Executive of the Hong Kong Special Administrative Region under section 11(1) of the Securities and Futures Ordinance (Cap. 571) after consulting Chairman and any other member of the Commission as appropriate;
- (i) signing the annual accounts of the SFC and the Investor Compensation Fund;
- (j) sharing with the chairman the task of convening meetings of the Board and the Advisory Committee;
- (k) recruiting, developing and retaining talented people to work at the SFC and in particular establishing a strong management team which is fair and fully evaluated;
- (l) communicating throughout the SFC the strategic objectives agreed with the Board, including those in the corporate plan, and ensuring that these are achieved in practice;
- (m) sharing with the chairman and other members of the SFC senior management the responsibility of communicating the SFC's messages externally; and
- (n) as CEO of the Commission, represent the SFC officially at the local and international level, as appropriate, including attending meetings of the committees and subcommittees of the Legislative Council when requested.

Financial Services Branch
Financial Services and the Treasury Bureau
April 2006

Proposed changes in relation to the exercise of statutory functions of the Chairman under the Securities and Futures Ordinance (Cap.571)

Description	Section(s)
(i) Chief Executive to give written directions to the Commission after consultation with <u>the chief executive officer</u> . Chairman.	s.11(1)
(ii) Chairman and <u>the chief executive officer</u> one non-executive director (NED) to sign the financial statements of the Commission.	s.15(2)b
(iii) Chairman and <u>the chief executive officer</u> at least one NED to sign the financial statements of the Investor Compensation Fund.	s.240(4)
(iv) Chairman to designate an executive director ^{Note} to act as chairman.	s.6, Part 1, Schedule 2
(v) Chairman, deputy chairman, <u>chief executive officer</u> or any 2 other members may convene meetings of the Commission.	s.14 and 15, Part 1, Schedule 2
(vi) The chairman of the meeting has a casting vote in case of equal votes.	s.19, Part 1, Schedule 2
(vii) Chairman or deputy chairman or other members as authorized shall authenticate the affixing of the seal.	s.25, Part 1, Schedule 2
(viii) Chairman and <u>the chief executive officer</u> shall be members of the Advisory Committee and may convene meetings.	s.27-29, Part 1, Schedule 2

^{Note} : Clause 3 of the Bill amends section 6 of Part 1 of Schedule 2 to the effect that an executive director or a non-executive director may be designated to act as chairman.

SECURITIES AND FUTURES (AMENDMENT) BILL 2005

COMMITTEE STAGE

Amendments to be moved by the Secretary for Financial Services
and the Treasury

Clause

Amendment Proposed

New

By adding -

1A. Directions to Commission

Section 11(1) of the Securities and Futures Ordinance (Cap. 571) is amended by repealing "chairman" and substituting "chief executive officer".

1B. Accounts and annual report

Section 15(2)(b) is amended by repealing ", and one non-executive director," and substituting "and the chief executive officer".

1C. Accounts of compensation fund

Section 240(4) is amended by repealing "at least one non-executive director" and substituting "the chief executive officer".

2

By deleting the clause and substituting -

"2. Interpretation and general provisions

Section 1 of Part 1 of Schedule 1 is

amended -

(a) in the definition of "executive director", by repealing everything after "means" and substituting "the chief executive officer of the Commission or any other person who is appointed as an executive director of the Commission under section 1 of Part 1 of Schedule 2 to this Ordinance (whether or not acting in any other capacity under that Part);";

(b) in the definition of "member", by repealing everything after "means" and substituting -

"-

(a) the chairman of the Commission; or

(b) the chief executive officer or any other executive director or non-executive director

of the Commission
(whether or not
acting in any other
capacity under Part
1 of Schedule 2 to
this Ordinance);";

(c) in the definition of "non-
executive director", by adding
"(whether or not acting in any
other capacity under that Part)"
before the semicolon."

3

(a) By adding before paragraph (a) -

"(aa) in the heading immediately before section 1,
by adding ", **chief executive officer**" after
"**Chairman**";

(ab) in section 1, by repealing "and such number
of" and substituting ", a chief executive
officer and such number of other";".

(b) By deleting paragraphs (c), (e) and (f).

(c) In paragraph (i) -

(i) in the Chinese text, in the proposed
section 9 of Part 1 of Schedule 2, by
deleting "須就所有目的而言" and
substituting "就所有目的而言，須" ;

(ii) by adding -

"9A. Notwithstanding section 9 -

(a) an executive director of the Commission shall not cease to be regarded as such only because of his acting as chairman of the Commission; and

(b) a non-executive director of the Commission shall not cease to be regarded as such only because of his acting as chairman of the Commission.

Vacancy in office of chief executive officer

9B. The Chief Executive may designate an executive director of the Commission to act as chief executive officer of the Commission for any period during which the chief executive officer of the Commission is unable to act as chief executive officer due to illness, absence from Hong Kong or any other cause, and may at any time revoke any such designation.

9C. An executive director of the Commission who acts as chief executive officer of the Commission shall be deemed for all purposes to be the chief executive officer of the Commission."

(d) In paragraph (k), by deleting "9A." and substituting "9D."

(e) By adding -

"(oa) in section 14, by repealing "or the deputy chairman" and substituting ", deputy chairman, chief executive officer";

(ob) by adding -

"16A. For the purpose of forming a quorum under section 16 -

(a) subject to paragraph (b), the chairman of the Commission shall be counted as a non-executive director of the Commission; and

(b) notwithstanding sections 9 and 9A -

(i) an executive director of the Commission who acts as chairman

of the
Commission shall
only be counted
as an executive
director of the
Commission; and

(ii) a non-executive
director of the
Commission who
acts as chairman
of the
Commission shall
only be counted
as a non-
executive
director of the
Commission." ;".

(f) By deleting paragraph (p) and substituting -

"(p) in section 27, by adding -

"(aa) the chief executive officer of the
Commission;" ;".

(g) By adding -

"(q) in section 28(a), by repealing "or";

(r) in section 28, by adding -

"(aa) the chief executive officer of
the Commission; or".

Securities and Futures (Amendment) Bill 2005

Committee Stage

Amendment to be moved by Hon. Margaret Ng

Clause

Amendment proposed

New Clause

By adding —

“1A Direction to the Commission

Section 11 of the Securities and
Futures Ordinance (Cap.571) is repealed.”

Appendix VII

SECURITIES AND FUTURES (AMENDMENT) BILL 2005

COMMITTEE STAGE

Amendment to be moved by Hon. Ronny Tong Ka-wah

Clause

Amendment Proposed

New

By adding -

"1A. Direction to the Commission

Section 11(1) of the Securities and Futures Ordinance (Cap. 571) is amended by adding "and chief executive officer" after "chairman"."