

**立法會**  
*Legislative Council*

LC Paper No. LS89/09-10

**Paper for the House Committee Meeting  
on 8 October 2010**

**Legal Service Division Report on  
Securities and Futures and Companies Legislation  
(Structured Products Amendment) Bill 2010**

**I. SUMMARY**

- 1. Objects of the Bill**      To transfer the regulation of public offers of structured products from the prospectus regime of the Companies Ordinance (Cap. 32) (CO) to the offers of investments regime of the Securities and Futures Ordinance (Cap. 571) (SFO) and to make consequential and related amendments.
- 2. Comments**

  - (a) Public offer of all structured products except convertible and exchangeable bonds and subscription warrants would be regulated under SFO.
  - (b) The regulatory requirements applicable to securities under SFO would only apply to structured products the offering documents of which require the authorization by SFC.
  - (c) SFC would be empowered to authorize structured products under the new section 104A of SFO.
- 3. Public Consultation**      The Securities and Futures Commission (SFC) conducted a two-month consultation on Possible Reforms to the Prospectus Regime in CO and SFO from 30 October 2009 and published its consultation conclusions on 22 April 2010.
- 4. Consultation with LegCo Panel**      The proposals were discussed by the Panel on Financial Affairs on 3 May 2010. No objection was raised.
- 5. Conclusion**      The rationalization of the regulatory regime of structured products involves not merely technical amendments but a policy change. Members may wish to form a Bills Committee to study the details of the Bill.

## II. REPORT

### Objects of the Bill

To transfer the regulation of public offers of structured products from the prospectus regime of the Companies Ordinance (Cap. 32) (CO) to the offers of investments regime of the Securities and Futures Ordinance (Cap. 571) (SFO) and to make consequential and related amendments.

### LegCo Brief Reference

2. File Ref.: LP SUB/12/2/2/1 issued by the Financial Services Branch of the Financial Services and the Treasury Bureau and dated 30 June 2010.

### Date of First Reading

3. 14 July 2010.

### Comments

#### *Existing regimes for authorizing offering documentation*

4. Under existing legislation, when investment products are offered to the public in Hong Kong, the offering documentation must be authorized by SFC unless an exemption applies. The requirements for authorizing offering documentation are set out in CO and SFO. They are two separate regimes. Under CO, it is the prospectus regime for shares and debentures. Under SFO, it is the offers of investments regime under Part IV of SFO for securities and regulated investment agreements.

5. There are a number of exemptions from the authorization requirements under the CO prospectus regime. They are set out in the Seventeenth Schedule of CO which includes an offer:

- (a) to not more than 50 persons;
- (b) with a minimum denomination of HK\$500,000;
- (c) with a maximum size of HK\$ 5 million; and
- (d) to professional investors.

These exemptions have been used to facilitate the sale of credit-linked notes by private placement.

6. Under the existing legislative framework, the public offer of structured products may, according to their legal form, be subject to different regimes, even though

such structured products may have similar economic risks and return profiles. Structured products, such as Minibonds, that have been structured to conform to the definition of “debenture” under CO, are regulated under the CO prospectus regime as debentures. Offer documents of equity-linked instruments are regulated under the SFO offers of investments regime as their legal form is that of securities or regulated investment agreements or a hybrid of securities and regulated investment agreements. The Administration is of the view that the legislative framework should be rationalized by transferring the regulation of public offers of structured products from the CO prospectus regime to the offers of investments regime in Part IV of SFO so that all structured products irrespective of their legal form will be regulated under the latter regime. However, convertible and exchangeable bonds as well as subscription warrants issued for capital raising purposes are excepted.

7. Members may wish to note that SFC in its Report to the Financial Secretary on Issues raised by the Lehmans Minibonds crisis (paragraphs 25.1 and 25.2) submitted at the end of December 2008 stated that the all-embracing definition of “debenture” in CO enabled issuers of an investment arrangement or instrument to structure it as a debenture in order to bring it within the CO prospectus regime. It also recognized that such arrangements or instruments could not have been in contemplation of the provisions when the law was enacted.

#### *The legislative proposals*

8. “Structured product” is defined in the new section 1A of Schedule 1 to SFO (clause 15). The exceptions of convertible and exchangeable bond and subscription warrant are set out in section 1A(2)(a) and (b) respectively. The Financial Secretary is empowered under a new section 392 in SFO (clause 13) to prescribe by notice published in the Gazette that any interests, rights or property are to be or not to be regarded as structured products.

9. The definition of “securities” in section 1 of Schedule 1 to SFO is amended by adding a new paragraph (g) (clause 15(5)) to include structured products in respect of which the offering documents require the authorization of SFC.

10. Section 103(1) in SFO is amended in clause 4(1) of the Bill to expressly cover structured products. The amendment will extend the regulation by SFC of offering documents to those in respect of structured products. The exemptions under the CO prospectus regime mentioned as items (a), (b) and (c) in paragraph 5 above have not been replicated.

11. The Stock Exchange of Hong Kong is, and will remain, the frontline regulator responsible for reviewing and approving listed documents for listed structured products. The issue by SFC licensees of offering documents and marketing materials of listed structured products will be exempted from SFC’s authorization. The exemption is provided in a new subsection (2)(a) in section 103 of SFO (clause 4 (2)).

12. Any offering documents made in respect of the issue of currency-linked instruments, interest rate-linked instruments or currency and interest rate-linked instruments by an authorized financial institution will also be exempted under a new subsection (3)(ea) in section 103 of SFO (clause 4(5)).

13. The empowering of SFC to authorize structured products will be effected by the new section 104A in SFO (clause 5). It replicates section 104 in SFO. According to the LegCo Brief, the authorization process will depend on compliance with codes and guidelines issued by SFC. SFC has issued a new Code on Unlisted Structured Investment Products on 25 June 2010.

14. The dis-application of the provisions of the CO prospectus regime to structured products as defined in SFO will be effected by new sections 38AA (for a company incorporated in Hong Kong) (clause 19) and 342AA (for a company incorporated outside Hong Kong) (clause 20) in CO. The reference to “securities” in the definition of ‘debenture’ in section 2(1) of CO is replaced by “debt securities” (clause 18(1)). However, the latter expression does not appear to have been defined in the Bill or CO.

15. Transitional provisions are provided in clause 17 as amendments to Schedule 10 to SFO. Structured products issued under the CO prospectus regime before the commencement of sections 19 and 20 of the enacted Bill will not be affected by the new law at least until the end of the offer period stated in the relevant prospectus. A 6 month grace period will be granted to a business dealing in structured products existed immediately prior to the commencement of section 15(5) of the enacted Bill before the licensing regime under Part V of SFO will apply.

16. The Legal Service Division is seeking clarification on a few drafting points from the Administration and will submit a further report if necessary.

## **Public Consultation**

17. The Securities and Futures Commission (SFC) conducted a two-month consultation on Possible Reforms to the Prospectus Regime in CO and SFO from 30 October 2009 and published its consultation conclusions on 22 April 2010. According to the LegCo Brief, SFC received 13 written submissions and held more than 16 meetings to discuss aspects of the consultation paper with industry representatives. It is stated by the Administration that the major concerns have been addressed.

## **Consultation with LegCo Panel**

18. The Panel on Financial Affairs was briefed of the legislative proposals at its meeting on 3 May 2010. Members discussed the proposals and no objection was raised.

## **Conclusion**

19. The rationalization of the regulatory regime of structured products involves not merely technical amendments but a policy change. Members may wish to form a Bills Committee to study the details of the Bill.

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