

**立法會**  
*Legislative Council*

LC Paper No. CB(1)2660/10-11  
(These minutes have been seen  
by the Administration)

Ref : CB1/SS/9/10/2

**Subcommittee on Securities and Futures Ordinance  
(Amendment of Schedule 5) Notice 2011 and Securities and Futures  
(Financial Resources) (Amendment) Rules 2011**

**Third meeting on  
Wednesday, 23 March 2011, at 4:30 pm  
in Conference Room B of the Legislative Council Building**

**Members present** : Hon James TO Kun-sun (Chairman)  
Hon CHAN Kam-lam, SBS, JP  
Hon Audrey EU Yuet-mee, SC, JP  
Hon WONG Ting-kwong, BBS, JP  
Hon CHIM Pui-chung

**Public officers attending** : Financial Services and the Treasury Bureau  
  
Ms Mandy WONG  
Principal Assistant Secretary (Financial Services)  
  
Mr Bernard LO  
Assistant Secretary (Financial Services)  
  
Department of Justice  
  
Ms Carmen CHU  
Senior Government Counsel

**Attendance by invitation** : Securities and Futures Commission  
  
Mr Stephen TISDALL  
Senior Director of  
Intermediaries Licensing and Conduct  
  
Mr Wilson LO  
Director of Licensing

**Clerk in attendance** : Ms Anita SIT  
Chief Council Secretary (1)5

**Staff in attendance** : Mr YICK Wing-kin  
Assistant Legal Adviser 8

Mr Hugo CHIU  
Council Secretary (1)5

Ms Clara LO  
Legislative Assistant (1)10

**I Meeting with the Administration**

(LC Paper No. CB(1)1676/10-11(01) — The Administration's response to issues raised at the Subcommittee meeting held on 17 March 2011

LC Paper No. CB(1)1613/10-11(01) — The Administration's response to issues raised at the Subcommittee meeting held on 8 March 2011

L.N. 28 of 2011 — Securities and Futures Ordinance (Amendment of Schedule 5) Notice 2011

L.N. 29 of 2011 — Securities and Futures (Financial Resources) (Amendment) Rules 2011

- SUB/14/1/5 (2010) — Legislative Council Brief on Securities and Futures Ordinance (Amendment of Schedule 5) Notice 2011 and Securities and Futures (Financial Resources) (Amendment) Rules 2011 issued by the Financial Services and the Treasury Bureau
- LC Paper No. LS29/10-11 — Legal Service Division report on subsidiary legislation gazetted on 18 February 2011
- LC Paper No. CB(1)1499/10-11(01) — Marked-up copy of the Securities and Futures Ordinance (Amendment of Schedule 5) Notice 2011 (L.N. 28 of 2011) prepared by the Legal Service Division
- LC Paper No. CB(1)1499/10-11(02) — Marked-up copy of the Securities and Futures (Financial Resources) (Amendment) Rules 2011 (L.N. 29 of 2011) prepared by the Legal Service Division)

Discussion

The Subcommittee deliberated (Index of proceedings attached at **Appendix**).

Admin

Follow-up actions to be taken by the Administration

2. The Administration was requested to take the following follow-up actions:
- (a) Regarding the term "reasonable expectation" in the proposed definition of "providing credit rating services", to review whether there is any judicial authority on the interpretation of this term in Hong Kong or other common law jurisdictions, and whether the word "anticipation" ("預期") would be more appropriate than and thus can replace the word "expectation" in the context of the proposed definition.

- (b) Regarding the proposed definition of "credit ratings" (信貸評級), to consider whether a catch-all clause should be added to the definition to cater for future novel financial products, whose credit rating may be disseminated to the public.
- (c) Regarding the proposed definition of "debt securities" (債務證券), to confirm whether the present construction of the definition is sufficiently wide to cover financial products that may not involve "indebtedness" (whether in pecuniary form or not) but the credit rating of which may be disseminated to the public.

*(Post-meeting note: The Administration's response was circulated to members vide LC Paper No. CB(1)1724/10-11(01) on 28 March 2011.)*

## **II Any other business**

- 3. There being no other business, the meeting ended at 6:28 pm.

Council Business Division 1  
Legislative Council Secretariat  
5 July 2011

**Subcommittee on Securities and Futures Ordinance  
(Amendment of Schedule 5) Notice 2011 and Securities and Futures  
(Financial Resources) (Amendment) Rules 2011**

**Proceedings of the meeting on Wednesday, 23 March 2011, at 4:30 pm  
in Conference Room B of the Legislative Council Building**

Time Marker	Speaker	Subject(s)	Action Required
000353 – 000421	Chairman	Opening remark	
000422 – 001956	Administration Chairman	<p>The Administration briefed members on paragraphs 2 to 11 of the paper "The Administration's response to issues raised at the Subcommittee meeting held on 17 March 2011" (LC Paper No. CB(1) 1676/10-11(01)) ("the paper") regarding the definitions of "misconduct" and "fit and proper", the manner in which SFC exercised its disciplinary powers, the scope of misconduct that might be subject to SFC's disciplinary actions, and precedents of disciplinary cases.</p> <p>The Chairman said that he accepted the explanations set out in the paper.</p>	
001957 – 002111	Administration Chairman	<p>The Administration briefed members on paragraphs 12-13 of the paper regarding the regulatory arrangements in overseas jurisdictions to sanction credit rating agencies ("CRAs") for violating requirements governing their credit rating activities.</p> <p>Members did not raise any question.</p>	
002112 – 010153	Administration Mr CHAN Kam-lam Chairman SFC Mr WONG Ting-kwong ALA8	<p>The Administration briefed members on paragraph 14 of the paper regarding the issue of private rating and an amendment to paragraph 19 of the draft Code of Conduct for Persons Providing Credit Rating Services ("Code of Conduct").</p> <p>Mr CHAN enquired, with the provision prohibiting the dissemination of "private ratings" to the public, whether obligations in the Code of Conduct could be effectively monitored in practice. The Chairman also enquired whether such provision would affect the submission of relevant rating information to the court if the client initiated a legal case against the performance of the CRA.</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>SFC explained that private rating would not be subject to the licensing requirement as the rating information was not supposed to be disseminated to and thus affect the public. A client not satisfied with the conduct of a CRA in relation to a private rating could potentially take legal action against the latter. The regulatory concern of SFC was to ensure that private rating information would not be disseminated to the public and amendment to paragraph 19 of the Code of Conduct was made to further reinforce this.</p> <p>Mr CHAN and the Chairman expressed concern that the amendment made to paragraph 19 of the Code of Conduct might create a loophole for "rating shopping". By way of illustration, a client might ask a CRA to conduct private rating and specify in the service agreement that the rating information would not be disclosed. The client would then, depending on whether the rating was favourable, decide whether to disclose or hide the rating result. To avoid creating this loophole, the Chairman suggested prohibiting the same CRA to rate a financial product/entity for a subsequent public dissemination or distribution by subscription if the same product/entity had been previously rated by the CRA under a private rating arrangement.</p> <p>ALA8 pointed out that a client might commission private rating for either (i) a financial product that he/she intended to offer to the market or public investors; or (ii) a third party that he/she intends to make loan to it or to invest in the securities or bonds issued by such part. "Rating shopping" would not happen in the latter scenario, Because in that case the client of a CRA would only want the credit risk of their investment. As for the former scenario, there should be a reasonable expectation of a CRA that the rating information would be disseminated to the public. Under the proposed regulatory regime, it would be a contravention of conducts if the CRA agrees that the rating information about a financial product which is intended for public subscription would not be disseminated to the public. Noting ALA8's advice, members considered that the risk of rating shopping could be effectively mitigated under the proposed regulatory arrangements.</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>Mr CHAN enquired about the meaning of the term "firms" in paragraph 14 of the paper and the Chairman remarked that it referred to an entity providing private rating. Mr CHAN also asked whether such firms should be required to obtain licence. The Chairman remarked that it would not be necessary because it would be illegal for them to disclose the rating information.</p>	
<p>010154 – 011343</p>	<p>Administration Chairman Mr WONG Ting-kwong ALA8</p>	<p>The Administration briefed members on paragraphs 15-17 of the paper regarding the term "reasonable expectation" in the definition of "providing credit rating services".</p> <p>At the Chairman's invitation, ALA8 said that he considered the term "reasonable probability (or likelihood)" to be preferable to the term "reasonable expectation" in the context of the definition of "providing credit rating services", because it is more objective than the term "reasonable expectation". He however did not object to keeping the term "reasonable expectation" in view of consistency in the same legislation.</p> <p>The Chairman enquired about the availability of case law examples that could show whether the court would use subjective or objective test in examining the term "reasonable expectation". ALA8 responded that while he had no case law examples in hand, his understanding was that the court would adopt a "reasonable man" test as mentioned in the Administration's paper.</p> <p>The Chairman remarked that the term "預期" (anticipation) might be more appropriate than the term "期望" (expectation) for use in the definition of "providing credit rating services", because a person's anticipation was usually based on objective factors. The Administration advised that the word "expectation" (i) had a broader meaning than the word "anticipation" and (ii) covered the meaning of "anticipation". The Chairman asked the Administration to explore whether there existed common law jurisprudence showing that the word "expectation" covered the meaning of "anticipation".</p> <p>The Administration stated that maintaining consistency in the use of the term "reasonable</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>expectation", as mentioned in paragraph 16 of the Administration's paper, was also an important consideration. The Chairman opined that maintaining consistency was a secondary consideration and the primary consideration should be whether there existed common law jurisprudence showing that the word "expectation" covered the meaning of "anticipation".</p> <p>The Chairman requested that regarding the term "reasonable expectation" in the proposed definition of "providing credit rating services", the Administration should review whether there was any judicial authority on the interpretation of this term in Hong Kong or other common law jurisdictions, and whether the word "anticipation" ("預期") would be more appropriate than and thus could replace the word "expectation" in the context of the proposed definition.</p>	<p>The Administration to take action as per paragraph 2 of the minutes.</p>
011344 011802	– Administration Chairman	<p>The Administration briefed members on paragraphs 18-22 of the Administration's paper. Members raised no questions.</p>	
011803 011927	– Administration Chairman	<p><b><u>Section-by-section examination of the subsidiary legislation</u></b></p> <p><b>Securities and Futures Ordinance (Amendment of Schedule 5) Notice 2011</b></p> <p><u>1. Commencement</u></p> <p><u>2. Securities and Futures Ordinance amended</u></p> <p>Members raised no questions.</p>	
011928 014436	– Administration Chairman SFC ALA8	<p><u>3. Schedule 5 amended (Regulated activities)</u></p> <p>Regarding the proposed definition of "credit ratings" (信貸評級), the Chairman requested the Administration to consider whether a catch-all clause should be added to the definition to cater for future novel financial products, whose credit rating may be disseminated to the public.</p> <p>Regarding the exclusion clauses of the definition of "providing credit rating services", the Chairman asked and the Administration confirmed that the intention was to exclude,</p>	<p>The Administration to take action as per paragraph 2 of the minutes.</p>

Time Marker	Speaker	Subject(s)	Action Required
		<p>among others, activities of credit reference agencies from the definition. The Chairman was concerned that the activity mentioned in (d) might be conducted by a CRA incidental to the preparation of preparing credit ratings. He asked whether the exclusion clause (d) needed refinement, such as by revising the wording to "an activity consisting of <b>only</b> gathering, collating,...". ALA8 said that the proposed definition, viewing from its entirety, should not give rise to interpretation problems.</p> <p>Regarding the proposed definition of "debt securities" (債務證券), the Chairman requested the Administration to confirm whether the present construction of the definition was sufficiently wide to cover financial products that might not involve "indebtedness" (whether in pecuniary form or not) but the credit rating of which might be disseminated to the public.</p>	<p>The Administration to take action as per paragraph 2 of the minutes.</p>
<p>014437 – 014552</p>	<p>Administration Chairman</p>	<p><b>Securities and Futures (Financial Resources)(Amendment) Rules 2011</b></p> <ol style="list-style-type: none"> <li>1. <u>Commencement</u></li> <li>2. <u>Securities and Futures (Financial Resources) Rules amended</u></li> <li>3. <u>Section 2 amended (Interpretation)</u></li> <li>4. <u>Section 5 amended (Paid-up share capital requirement for licensed corporations)</u></li> <li>5. <u>Section 56 amended (Licensed corporations to submit returns to Commission)</u></li> </ol> <p>Members raised no questions.</p>	
<p>014553 – 015519</p>	<p>Administration Chairman SFC</p>	<p><u>6. Schedule 1 amended (Financial resources requirements)</u></p> <p>Regarding the minimum amount of paid-up share capital for licensed corporations licensed for Type 10 regulated activity, the Chairman enquired on what basis the figure \$5,000,000 was determined. SFC responded that the figure was so determined in order to align with the capital requirements of licensed corporations of other comparable types of regulated activities under SFO. In practice,</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>the requirement would be nil for CRAs, because the amended section 5(d) of Cap. 571N provided that a licensed corporation licensed for Type 4, 5, 9 or 10 regulated activity, which is subject to the specified licensing condition (i.e. not holding any client assets) is not be covered by the paid-up share capital requirement.</p> <p>Regarding the minimum amount of required liquid capital for licensed corporations licensed for Type 10 regulated activity, the Chairman enquired on what bases the figures \$100,000 and \$3,000,000 were determined. SFC responded that the figures were so determined in order to align with the corresponding requirements in respect of Type 4 regulated activity under SFO. SFC also remarked that Type 4 regulated activity was chosen because it was comparable to Type 10 regulated activity.</p>	
015520 – 015536	Chairman	The Chairman said that the Clerk would liaise with the Administration regarding the date of next meeting.	